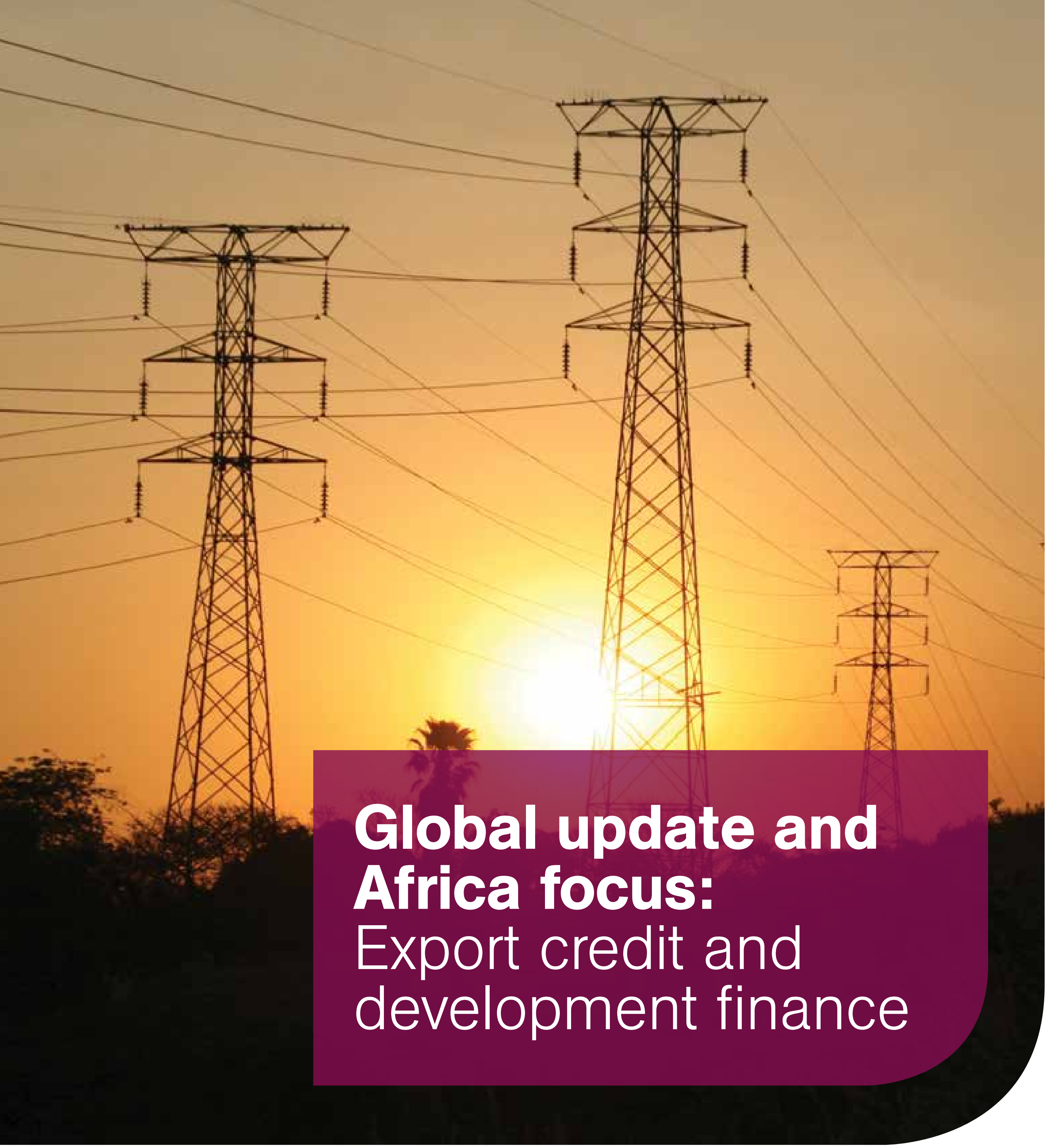


Global update and Africa focus: Export credit and development finance

Baker & McKenzie

IJGlobal

Infrastructure Journal and Project Finance Magazine

Welcome

Welcome to this update to "Power Shift", our 2013 Report on the Rise of Export Credit and Development Finance in Major Projects. In this paper, we provide an up-to-date snapshot of volumes and sources of project funding on a global, regional and pan-Africa basis. We have also included a Focus on Africa, featuring contributions from leading practitioners in the market. We would highlight the following findings:

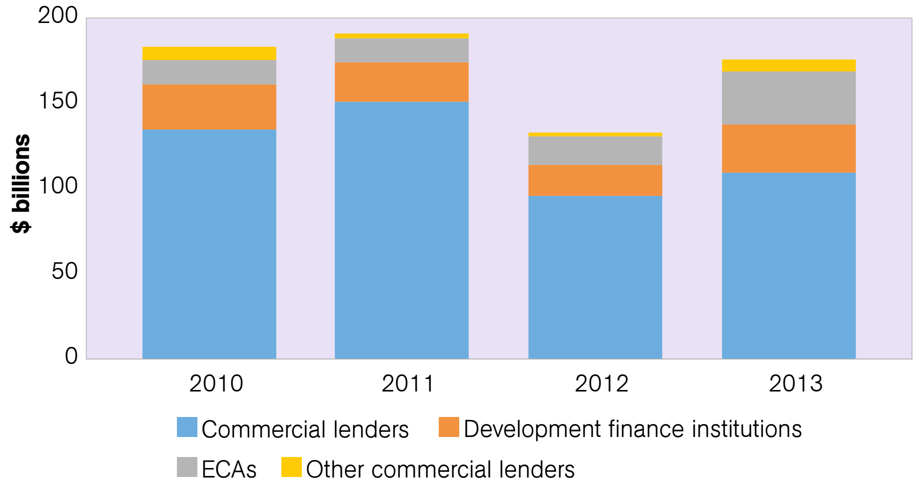
- ECA and DFI loan volumes rose by more than US$15 billion and $10 billion respectively in 2013
- DFIs and/or ECAs remain an essential funding partner for infrastructure projects in Africa
- the Power Africa initiative will see US Ex-Im lending around $3 billion and the World Bank $5 billion into the African market over the next 5 years

This report was researched and written in August, 2014 and was presented at the World Infrastructure Summit 2014, held at Barcelona on September 23 to 25, 2014.

I hope you enjoy reading it,

Calvin Walker
Global Head of Project Finance
Baker & McKenzie

Project finance loan volumes by type of lender* 2010 – 2013



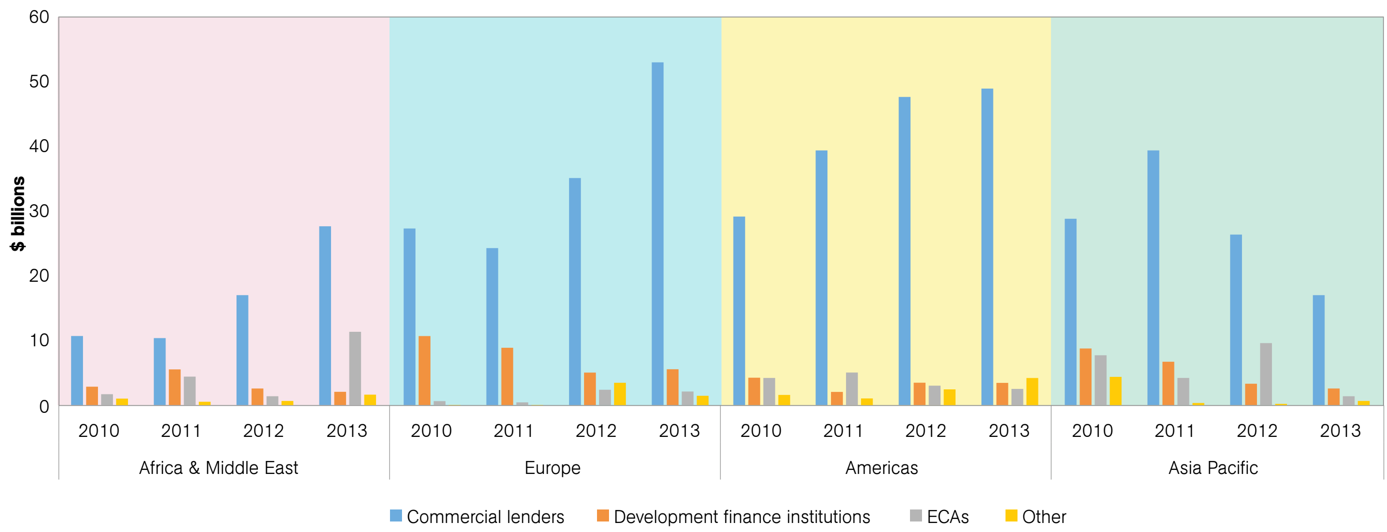
The 10 largest DFIs and ECAs alone provided more than $500 billion in loans, guarantees and insurance in 2013.

Globally, ECA lending with commercial banks doubled in 2013, to more than $31 billion.

Africa and the Middle East saw the highest global ECA investment in 2013 – $11.33 billion.

Infrastructure spending in sub-Saharan Africa is forecast to exceed $180 billion by 2025.

Regional breakdown* 2010 – 2013



ECA and DFI numbers exclude lending independent of commercial banks.

Africa in Focus

While new investors look for opportunities in Africa, DFIs and ECAs are continuing to play a leading role in bringing energy and infrastructure projects to completion in the region.

Anchor investors

Whilst commercial banks account for the largest portion of lending on African energy and infrastructure financings, ECA and DFI lending volumes have been on a strong upward trend for several years, growing to $5.8 billion in 2013.

However, these figures exclude loans that do not involve commercial lenders, meaning that the total amount of funding in Africa provided by these institutions is actually considerably higher. Even on deals primarily financed by commercial banks, these non-bank institutions have disproportionate importance to the projects that they support.

Most non-regional project finance banks are still cautious in their approach to Africa. International banks more often than not still need to lean on DFIs and ECAs to supply due diligence, guarantees, and influence with host governments, in order to participate in infrastructure transactions.

Indeed, local and international DFIs are often the only lenders on smaller infrastructure deals, and without their support many of these would not be completed. *David Tinel, an investment officer at the IFC, said: "Excluding South Africa, we have been involved in the financing of over 80% of all of the IPP and PPP core infrastructure projects that have closed in Africa in the last five or six years."*

The balance sheets of ECAs make them increasingly important to major transactions in the region, and even historically cautious lenders such as US Ex-Im seem keen to flex their muscles. *Rick Angiuoni, director for Africa at US Ex-Im, said: "Structured products backed by ECAs that match long-term cash flows are critical to de-risking a project and encouraging international lenders to provide long-term funding."*

Even the most developed of African countries still suffer from major core infrastructure and power deficits. According to research from PwC, infrastructure spending in the Sub-Saharan African region is forecast to grow by 10% per year over the next decade – and exceed $180 billion by 2025.

Increased issuance volumes for ECA-backed bonds are likely, as institutional investors seek low-risk ways to support African infrastructure.

With infrastructure investment returns looking less favourable in many developed markets, Africa looks increasingly attractive to many international banks, as well as to new infrastructure funds that are emerging. It is clear that DFIs and ECAs will continue to offer comfort to investors in the region and help make deals bankable. But now they are also turning their attention to using their presence to help to unleash the avalanche of new lenders, equity and institutional investors needed to bridge the continent's funding gap.

Frances Okosi, partner at Baker & McKenzie, said: "What we hear about appetite for risk across Africa is that a lot of people are now prepared to look at it, and see it as a place for potential yield, but they want protection."

New entrants

The US government's Power Africa initiative is the most visible sign of increased investor interest in Africa. In August 2014 US President Barack Obama announced commitments of $12 billion in private sector investment and $7 billion in US government loans to support power projects in Ethiopia, Ghana, Kenya, Liberia, Nigeria and Tanzania. This investment will support US developers and exporters involved in the construction of new power plants, fuel import terminals and transmission networks

Over the next five years US Ex-Im will lend around $3 billion and the World Bank $5 billion as part of the initative. These commitments are substantial, but, as Angiuoni explains, the investor environment is not yet necessarily in place in order to capitalise on these commitments.

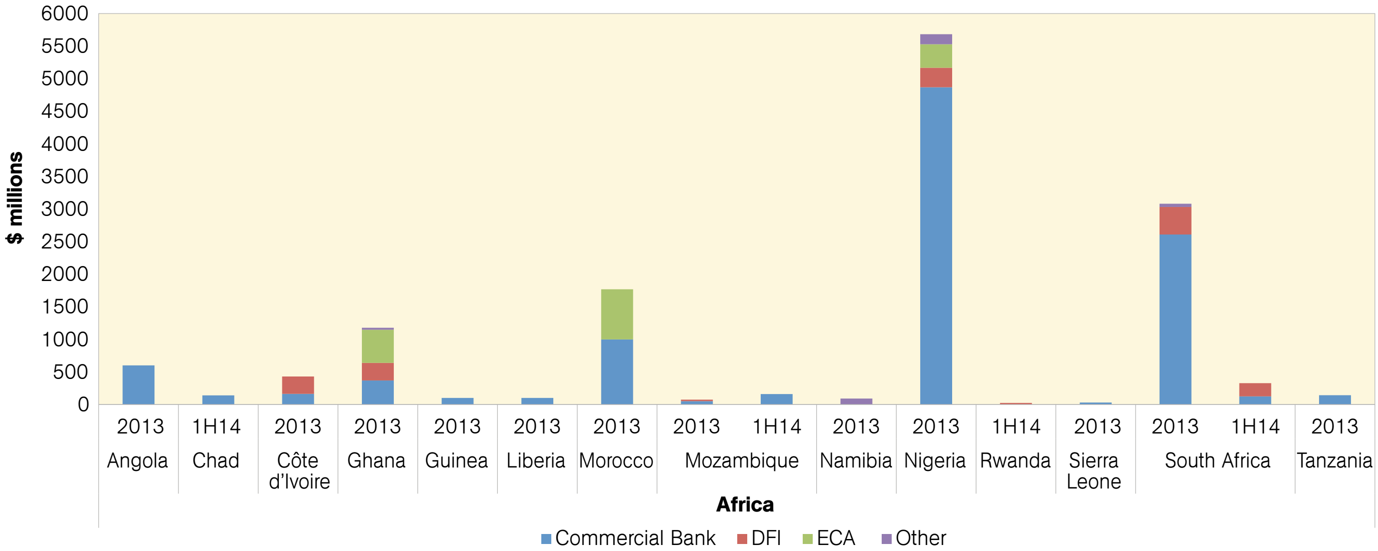
US Ex-Im's Angiuoni said: *"Power Africa has attracted quite a bit of attention to the fact that many financial institutions have begun expressing interest in developing new approaches to create alternatives to sovereign guarantees and address risks related to currency exposure."*

Many institutional investors are considering the risks associated with African projects for the first time. In the last year ARM, Meridiam and the African Development

Top 5 DFIs EMEA 2013

Rank	Institution	Investment ($ millions)
1	European Investment Bank	3671.20
2	Cassa Depositi e Prestiti	973.96
3	International Finance Corporation	763.25
4	European Bank for Reconstruction and Development	427.34
5	Islamic Development Bank	375.00

Debt investment – Africa 2013 – 1H14



Bank (AfDB), for instance, have launched Africa-focused funds.

Baker & McKenzie partner Calvin Walker said: "Overall there has been a fairly limited appetite from private equity in African opportunities to date, but with the proliferation of these Africa-focused funds that is going to change."

Starved of healthy deal pipelines in developed markets, many large commercial banks, which have largely ignored the continent in the past, are also now looking for investment opportunities in African infrastructure.

Persistent problems

This increased interest has not changed the typical challenges facing investors into Africa, however.

Regulatory risk, land rights issues and a lack of both associated infrastructure and human capital all still hinder many investors' participation in transactions. DFIs and ECAs have long attempted to mitigate some of these risks through their due diligence and, where necessary, guarantees.

EKF, the Danish ECA, and two DFIs – the European Investment Bank and the African Development Bank – have had to provide a package of guarantees on the $523 million financing for the 300MW Lake Turkana wind farm in Kenya, which signed in March. The 95MW Tobene IPP in Senegal needed similar DFI backing, this time from the World Bank, to proceed to financial close.

Over the next five years US Ex-Im will lend around $3 billion and the World Bank $5 billion as part of the Power Africa Initiative.

IFC's Tindel said: "It is very likely that you will see more deals like Tobene. The World Bank, IFC and MIGA provide a service which is completely unrivalled, which allows us to address most if not all of the issues faced when trying to structure an IPP."

"We can provide long-term advisory services to governments to try and fix power sectors, supply financial instruments to mitigate political risk or a lack of creditworthiness on the part of the offtaker, and also provide capital to private entities."

Neither Lake Turkana nor Tobene featured commercial debt from non-African banks, however, demonstrating the market's continuing reliance on DFIs. For the sponsors of Lake Turkana, the risks associated with a purpose-built 428km 400kv transmission line to connect the wind farm to the grid required a PRG.

James O'Brien, a partner at Baker & McKenzie, said: "A major challenge is still the creditworthiness of the offtaker, whether it is a state utility or the State itself, which is why you need a DFI to provide some credit comfort."

The most developed country in the region in terms of existing infrastructure, a track record of project development, and a sophisticated local banking sector is South Africa. But outside banks struggle to participate in this increasingly vibrant market because of currency risk. The South African government requires power purchase agreements to be denominated in local currency, although there are some suggestions that it may soften this stance over the next few years.

IFC's Tinel said: "In markets such as Nigeria and Kenya it is very much the intention to focus on mobilising capital from commercial institutions. As a few power markets become more developed, and more like South Africa, we hope that we will be able to attract African banks and more traditional global project finance lenders."

Natural resource-based projects represent a more viable market for new entrants, largely because of the sheer scale of their funding requirements, and their US dollar revenue streams. The $20 billion Simandou mine development in Guinea for example, and proposed LNG projects off the coast of East Africa, will need to tap every funding source available. The returns on natural resource-based projects can be more reliable, but can expose lenders to complex risks.

Many international commercial banks are now looking for investment opportunities in African infrastructure.

Michael Foundethakis, partner at Baker & McKenzie, said: "The biggest problem for international banks looking at these African projects is actually performance risk, not in terms of extracting the resource but often the transportation of the goods to market."

The LNG opportunities off the coast of Mozambique and Tanzania will require high capital expenditure on onshore associated infrastructure, including transport links – much more than the costs of field development.

New debt sources and competition

Increased issuance volumes for ECA-backed bonds are likely, as institutional investors seek low-risk opportunities to support African infrastructure. African DFIs are also hoping to create new investment structures which will give greater comfort to investors.

Angiuoni said: "I expect innovation as well as proliferation of existing ECA-backed products to mitigate risks and mobilise private financing with the expectations of encouraging lenders to increase risk-taking to projects through new capital or through higher debt to equity financings."

DFIs like the AfDB, African Finance Corporation, Proparco, FMO and DEG have experience of working in Africa, and understand the political landscape and physical challenges facing projects. Most ECAs have less experience of the market but have larger funding resources and can provide robust guarantees.

Christophe Maurat, an executive director at Bank of Tokyo-Mitsubishi said: "One question we have is whether DFIs and ECAs can work efficiently together. In other jurisdictions we have had issues in regards to inter-creditor provisions which on occasion have led to one or the other leaving the transaction."

The ERC refinery project in Egypt, which signed in 2012, offers hope however. EIB and JBIC were able to resolve a disagreement over priority that arose towards the end of the documentation process. It also involved DFIs the IFC, DEG and FMO all taking equity stakes, something that can increase both sponsor and lender comfort in Africa.

High risk help

DFIs try and focus their attention on less attractive sectors. The AfDB approved almost $7 billion worth of investment in African projects in 2013, but a large proportion of this will have been directed, through grants and direct loans to government, to smaller, non-bankable social infrastructure projects.

The European Bank for Reconstruction and Development (EBRD) has expanded into three African nations (Egypt, Morocco and Tunisia) in the last few years. It has committed to creating a broader pipeline of infrastructure projects for commercial lenders.

Thomas Maier, managing director for Infrastructure at the EBRD, said: "In emerging markets the real challenge is not so much the availability of financing, the issue is a supply-side one where there are too few good quality projects for which commercial banks, capital markets and ECAs to be interested in."

Newer ECA entrants are also becoming a significant source of funding. Chinese contractors, investors and ECAs have stepped up over the last five to ten years. They promise to fund resources development quickly, without the need for intrusive due diligence, and often build associated infrastructure as part of any agreement.

This approach has attracted criticism of its impact on communities, and DFIs like IFC say they are working to try and introduce these investors to more rigorous investment standards.

Most ECAs have less experience of the African market than DFIs but have larger funding resources and can provide robust guarantees.

Tinel said: "From our side there is definitely an appetite to work with Chinese investors and contractors, and on their side there is a desire to broaden their offering and be credible bidders in PPP and IPP tenders."

Conclusion

As the data from *IJGlobal* show, commercial bank lending across Africa is sizeable and of growing importance, but these lenders still need the comfort that DFIs and ECAs bring to transactions. Opportunities exist for new lenders to enter the market but Africa is not a promised land for those chasing yield, and historical risks persist. Although the due diligence procedures of DFIs and ECAs can be time-consuming, without this groundwork and the guarantees they can offer, many of the largest upcoming infrastructure projects in Africa will not be completed.

Top 5 ECAs globally 2013

Rank	Insititution	Investment ($ millions)
1	Japan Bank for International Cooperation	9,822.89
2	Export Import Bank of the United States	5,879.64
3	KEXIM	4,775.72
4	Korea Trade Insurance Corporation	2,175.00
5	Export Development Canada	1,695.45

Top 5 ECAs EMEA 1H14

Rank	Institution	Investment ($ millions)
1	Japan Bank for International Cooperation	1,605.74
2	Euler Hermes	479.90
3	Korea Finance Corporation	169.70
4	Export Import Bank of the United States	160.00
5	Export Development Canada	123.40

Top 5 DFIs globally 2013

Rank	Insititution	Investment ($ millions)
1	European Investment Bank	3,783.44
2	BNDES	1,384.00
3	International Finance Corporation	1,084.95
4	Cassa Depositi e Prestiti	973.96
5	China Development Bank	663.67

Top 5 DFIs EMEA 1H14

Rank	Institution	Investment ($ millions)
1	European Investment Bank	2,308.48
2	European Bank for Reconstruction and Development	393.63
3	African Development Bank	201.96
4	Development Bank of Japan	149.09
5	International Finance Corporation	120.00

Top 10 commercial lenders 2013

Rank	Institution	Investment ($ millions)
1	Mitsubishi UFJ Financial Group	8,340.28
2	Sumitomo Mitsui Financial Group	7,759.33
3	Mizuho Financial Group	4,364.43
4	Commonwealth Bank of Australia	4,147.77
5	Citigroup	3,990.75
6	HSBC	3,921.90
7	National Australia Bank	3,558.65
8	ING Group	3,432.37
9	Credit Agricole Group	3,318.04
10	BNP Paribas	3,244.89

Top 10 commercial lenders 1H14

Rank	Institution	Investment ($ millions)
1	Sumitomo Mitsui Financial Group	3,594.46
2	Mitsubishi UFJ Financial Group	3,268.79
3	Commonwealth Bank of Australia	2,671.26
4	Australia and New Zealand Banking Group	2,360.39
5	BNP Paribas	1,980.62
6	Mizuho Financial Group	1,845.21
7	National Australia Bank	1,793.05
8	Credit Agricole Group	1,789.73
9	ING Group	1,726.65
10	Citigroup	1,572.19

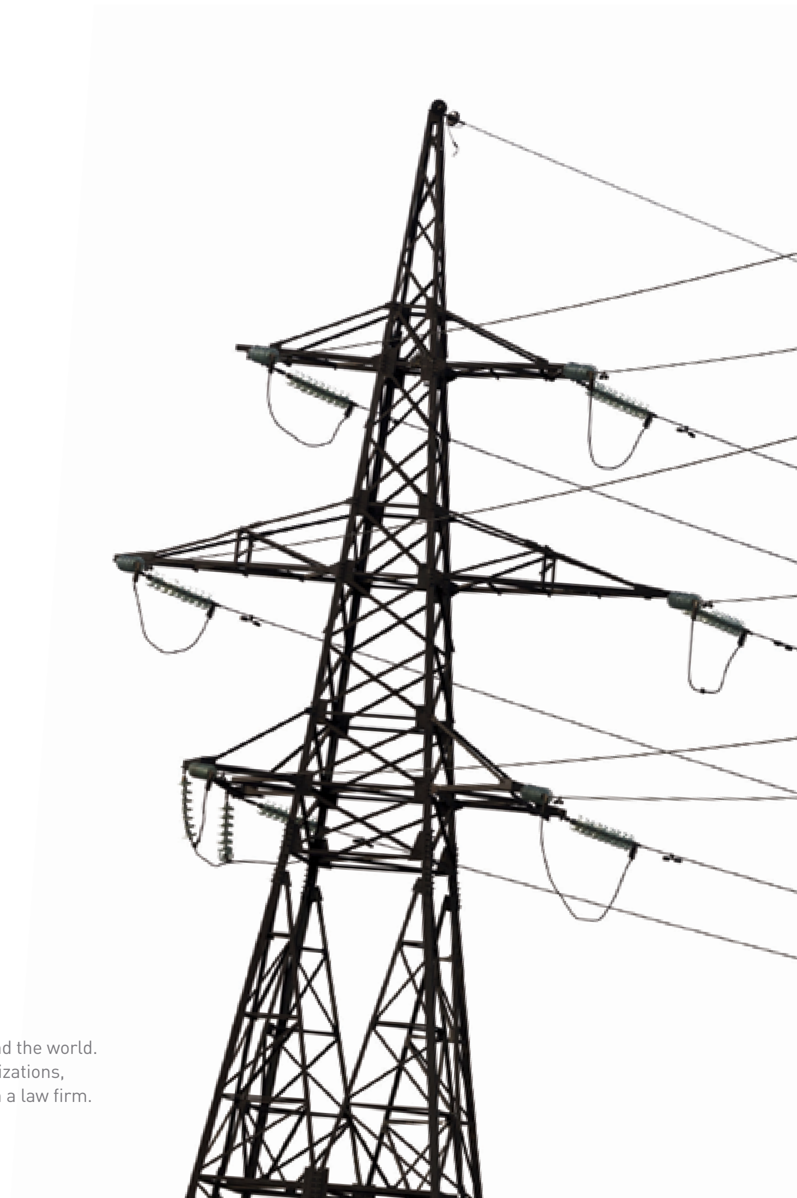
Top 5 deals with ECA and DFI involvement 2014 1H

Sector	Deal name	Investment ($ millions)	Location	Financial close
Mining	Roy Hill iron ore mine	32,019.60	Australia	29/04/2014
Renewables	600MW Gemini Offshore Wind Farm	11,635.35	Netherlands	15/05/2014
Transport	Intercity Express Programme Phase 2	11,074.62	United Kingdom	15/04/2014
Transport	Queensland New Generation Rolling Stock	5,372.52	Australia	17/01/2014
Renewables	330MW Sarulla Geothermal Project	4,621.44	Indonesia	16/05/2014

Top 5 deals with ECA and DFI involvement 2013

Sector	Deal Name	Investment ($ millions)	Location	Financial close
Oil & Gas	Ichthys LNG Financing	220,000	Australia	30/01/2013
Oil & Gas	Sadara Complex Loan Financing	137,992	Saudi Arabia	17/06/2013
Oil & Gas	Nghi Son oil refinery and petrochemicals complex	90,000	Vietnam	05/06/2013
Mining	Emirates Aluminium Taweelah Smelter Phase 2 (Emal)	27,600	United Arab Emirates	15/04/2013
Oil & Gas	Surgil Petrochemical and Natural Gas Complex financing	27,573	Uzbekistan	25/11/2013

Power network.



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