



FRESHFIELDS BRUCKHAUS DERINGER

The landscape for lending: the shifting sands of Middle Eastern infrastructure investment

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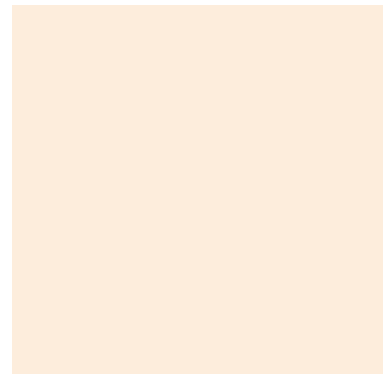
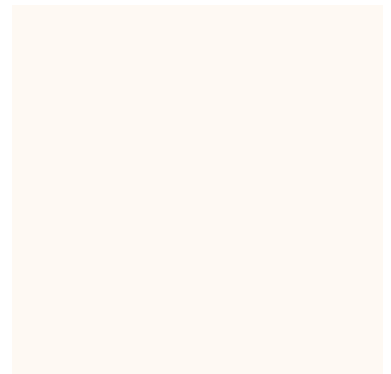
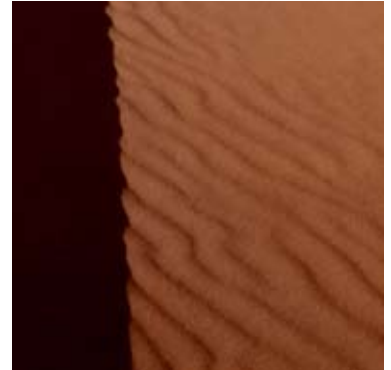
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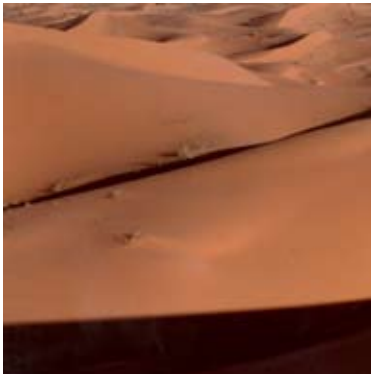
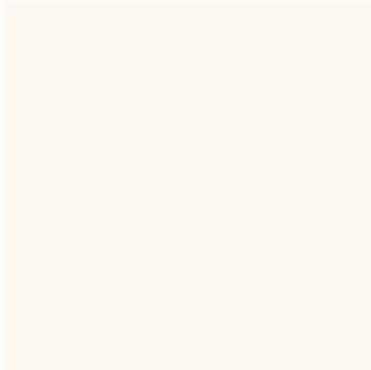
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Introduction

This paper considers the current position of infrastructure investment by the private sector in the Middle East. It reviews the impact on the pace of infrastructure development of certain trends affecting sectors in the region. In particular, it considers how the shortfall in the availability of project finance has been addressed on recent transactions and whether these techniques represent a short-term solution or whether they will become the new normal for infrastructure financing. Finally, it looks at some of the challenges involved and suggests ways in which governments in the region could facilitate further private sector investment in infrastructure projects and improve the economic and legal environment for the financing of these projects.





The current position

We now know that the initial assessment that the economies of the Middle East would survive the financial crisis and subsequent global economic recession unscathed was overly optimistic. Much of the demand for regional project financing had been met by international lenders, whose liquidity and general credit concerns meant that they were no longer able to fund projects at the previous rate. With certain exceptions, the local banks were not strong enough or prepared to advance funds for the durations required for infrastructure financing. The rapid decline in global energy demand led to an oil price collapse, with consequent pressure on government budgets, although this has been alleviated by the surpluses achieved in the recent past.

The position has improved gradually in recent months and projects have been financed; however, availability of long-term commercial bank debt remains scarce. Despite efforts to encourage the development of regional capital markets, it is fair to say that these do not currently offer an alternative source of long-term financing for projects.

However, the outlook for equity investment in the infrastructure space is brighter; developers with a successful track record of delivering well-structured projects are still able to attract equity investors. If there has been any difficulty in raising equity for direct investment in projects, that difficulty has mostly come from international investors.

There has been no decrease in the demand for infrastructure investment in the region. Under-investment in the past, a growing population and increasing per capita wealth all mean that the need for high-quality infrastructure across the region is considerable. Despite falling oil revenues, governments in the region have remained committed to their ambitious infrastructure development plans. These should also stimulate local economies – particularly the construction sector, that has been hard hit by the bursting of regional real estate bubbles. However, even where governments can support infrastructure development plans there is a growing awareness that to deliver this through conventional procurement methods with public sector funding is not always the best solution. By involving the private sector, whether through BOT style projects or PPPs or otherwise, governments are realising that they can achieve greater efficiencies and value for money over the life of projects. It is also apparent that involving the private sector will lead to more balanced and diversified regional economies.

The challenge for the public sector in this extremely difficult economic climate is how to facilitate such private sector participation in circumstances where the conventional means of financing, namely long-term commercial bank debt, is so scarce.

Countries in the region have responded to this challenge in different ways and with varying degrees of commitment.

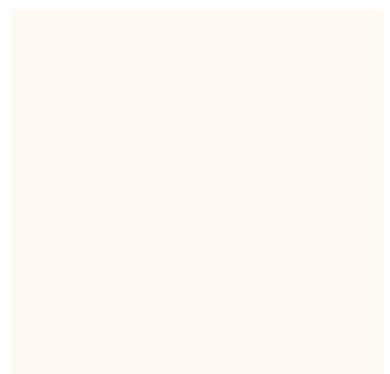
Saudi Arabia: yin and yang

Mixed messages have come out of the Saudi Arabian infrastructure market over the last twelve months. First, there is the success of the Rabigh independent power project (IPP), procured under the aegis of the Saudi Electricity Company (SEC). The winning bidder, the ACWA Power/Kepeco consortium, will use Chinese contractors to construct the plant – the first time that a regional IPP will see Chinese involvement. Of equal note is the fact that there will be no government guarantee of the offtake agreement, the credit standing of the newly privatised SEC being acceptable on a stand-alone basis. Perhaps of more significance was the make-up of the debt, nearly 80 per cent being provided through a SAR tranche by local banks and of the KEIC-covered dollar tranche more than 50 per cent being provided by the Bank of China. The traditional providers of project debt (international commercial banks) played a more limited role than usual.

The future for private sector involvement in Saudi power appears, at least as far as SEC's programme is concerned, to be encouraging. Nonetheless, funding capacity in the Kingdom may provide a stumbling block. To increase competition on its next IPP, PP11, SEC has restricted bidders to no more than three local banks and Alinma, Al-Rajhi and Samba have already come together to offer a financing package of SAR 3.8bn (just over \$1bn) to all bidders. One welcome sign is that bidders for PP11 need to find only 50 per cent of the required financing to qualify, rather than make a fully funded bid – a sensible recognition that tender terms need to be made more flexible to allow for the tight finance markets.

Earlier in the year, the Ras Al Zour project, an independent water and power project (IWPP) that was part of the Water and Electricity Company programme, was withdrawn from the market by the Saudi government, in large part due to uncertainties regarding the availability of debt at acceptable levels of pricing. The project was given to the Saline Water Conversion Corporation – currently still state-owned – to be constructed on a standard procurement basis. Despite the successful financial close of the Rabigh IPP in the meantime, the planned Marafiq IWPP and the proposed Yanbu 3 IWPP have received the same treatment. There appears to be a clear distinction between the IPP and the IWPP sectors in the Kingdom in terms of private sector participation. This is unlikely to be resolved until the future of SWCC has been finally determined.

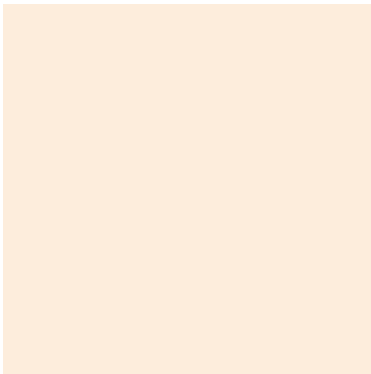
Similar trends applied in other sectors. In the rail sector, the Makkah-Madina rail link, now renamed the Haramain High-Speed Railway, which was once intended to be privately financed, is being paid for by the Saudi Government. However, the 'trophy' nature of the project and the influence of non-commercial factors had always cast some doubt on the appropriateness of private sector participation. More recently, the



Saudi Landbridge has undergone the same change in treatment. But the scale of this project would have challenged the private sector's ability to fund it even if the financial markets had been more buoyant. The message to the private sector from these projects is therefore mixed. However, there are several more manageable surface transportation projects under consideration that, if they had come to the market earlier than the Haramain High-Speed Railway and the Landbridge, might have reached a successful financial close with the private sector.

Similarly, in the ports and shipping sector, the decision to permit the development and financing of the port located at the King Abdullah Economic City by the private sector, without the benefit of any state subsidy, is not in compliance with international norms of port development. This will, no doubt, need to be revisited in light of the inability to source long-term commercial debt for the required tenors to match the expected economic life of in-water infrastructure. Some degree of public sector financing will need to be provided; hopefully this will complement and not replace private sector financing.

If one of the key trends in the Saudi market is the progressive shift towards financing by local financial institutions, one matter of concern is the exposure of these institutions to the restructurings of the Alghosaibi and Saad Groups, which are estimated by HSBC collectively to owe Saudi banks between \$4bn and \$7bn. At this stage, it is difficult to assess the impact of the Alghosaibi/Saad restructurings on the domestic Saudi project finance market, as not all banks have indicated the size of the provisions that they expect to make, nor is it known if this is a one-off event or if more family-owned businesses are similarly affected. Nevertheless, the recent announcement that a deal is close to being settled with the Saad group is welcome news. Although these events should not negatively impact on local banks' willingness to finance government-backed projects, it has made them far more cautious about funding projects sponsored by family-owned businesses. They are also wary about funding the equity bridge facilities for such sponsors participating in government-backed infrastructure projects. The fact that the proposed Saad deal applies only to Saudi banks makes it even less likely that international banks will be keen to increase their exposures to the Saudi project market except for the very best credits. The comparative difficulty that Aramco experienced obtaining commitments to the international tranche (now oversubscribed) on the Jubail refinery project confirms this.



Financing techniques: how the market has smoothed the credit crunch

The Al Dur IWPP in Bahrain faced initial funding difficulties as a direct result of the credit crunch. However, the financing was rescued by the use of a hard mini-perm. The \$1.7bn non-recourse loan has a tenor of eight years, with an 80 per cent balloon repayment, at the end of which it must be refinanced or the project will go into default. A 100 per cent cash sweep applies during the last three years of the loan, with full dividend lock-up during this period. The attraction to the banks was that their exposure was shortened (banks did not want to make available even 10-year money at the time); for the sponsors there was the ability to get the deal away and the confidence that credit markets will improve considerably over the next eight years. Note that the Bahrain Ministry of Electricity & Water did not take any refinancing risk under this structure.

Whether the Al Dur mini-perm was a one-off solution to a difficult situation at a time when the markets were virtually frozen, or whether it will become the new model for infrastructure financing, remains to be seen.

Already there are signs that the market is improving and terms are becoming more favourable. For the recent ISTP2 wastewater project in Abu Dhabi, the sponsors secured a \$400m soft mini-perm with a tenor of 20 years. The project is backed by a 25-year sewage treatment offtake agreement from government-owned ADSSC. Also in Abu Dhabi, the Shuweihat S-2 IWPP financing was successfully completed. A \$900m bridge loan, put in place for nine months in December 2008, was eventually taken out by a 22-year loan with lower pricing than on the Al Dur mini-perm. Steps had been taken to increase the attractiveness of the project. The tenor of the power and water purchase agreement (the PWPA) was extended by five years and Suez sold 20 per cent of the project to Marubeni, opening the way for \$1.1bn of JBIC financing. It is notable that, unlike in the Saudi projects, the bulk of this financing did come from international banks.

The current lack of interest from European banks in Oman's Salalah IWPP project may in part be due to the fact that it is only covered by a 15-year PWPA. However, given that the project is using Chinese EPC contractors, it is sensible for the sponsors to seek a Chinese financing solution through a Sinosure/C-Exim-covered ECA facility.

We should remember that these financings have largely related to legacy transactions in the power and water sector that would have been financed last year but for the credit crunch. New projects, particularly those in sectors such as roads, social housing, universities and hospitals, that are expected to come to the market in the near term, may find it hard to source financing. Such projects will need to be structured as PPPs incorporating an availability-based pricing structure



under a concession with a creditworthy government entity and with a clear obligation by that party to pay a termination sum that enables the banks to recover the outstanding debt. More adventurous structures (such as attempts to shift demand risk to the lenders) will simply not fly, notwithstanding the gradual increase in market confidence. Similarly, manufacturing plant or other industrial projects will require firm offtake obligations from creditworthy purchasers providing more than just volume support (unless pricing risk can be effectively hedged). These projects are always harder to finance, particularly where the project is expected to take a degree of merchant risk.

Clearly, longer PWPA and other offtake contract tenors resulting in longer project tails beyond the scheduled repayment date of the debt, plus the involvement of a sponsor who can access export credit agency financing for a project, do appear to be pragmatic answers to some of the current problems.

Making up the shortfall: how to obtain additional infrastructure finance

Funding with a splash – ways to deepen the liquidity pool

Long-term infrastructure lending capacity, particularly in dollars, remains in short supply. For projects where a significant part of the capital expenditure can be sourced locally and which do not have export earnings, sponsors and authorities should maximise local currency tranches and encourage national and regional banks to play a greater role. However, not all of the banks in the region are as strong as those in Saudi Arabia and Abu Dhabi and they face their own liquidity issues. Regional and local banks have already moved to develop their structuring expertise through skills enhancement programmes and by selective recruitment with a view to assuming greater prominence in project financing transactions, but this is currently a work in progress. In the short term, additional funding capacity must be sought from further afield, as considered below.

China Inc. – money from the Middle Kingdom

The presence of Chinese contractors in recent power and rail sector transactions in the region has been noticeable and this trend is likely to continue. The availability of cover from Sinasure/C-Exim and funding from Chinese commercial banks is likely to give Chinese contractors a considerable competitive advantage over other suppliers: Sinasure/C-Exim are not bound by the terms of the OECD consensus and can therefore offer more aggressive funding than other ECAs. Perhaps the key question here is not whether there will be Chinese involvement in infrastructure finance, but whether Chinese banks will replace the more traditional international commercial lenders on projects where there is not a 'China Inc.' aspect. It is a question of when, not if, we will see a material level of Chinese funding activity in the Middle East.

Export credit agencies – help us to help you

The involvement of export credit agencies (ECAs) is an obvious solution to the current funding shortfall. While tied cover from ECAs has long been seen on financings globally, greater flexibility to provide untied support and, more importantly, direct lending is being shown by a number of ECAs. The support from the Italian ECA SACE to the Ras Laffan C IWPP is a recent regional example where there were no Italian goods or services involved. The availability of ECA funding will, to the extent that it does not do so already, have a critical impact on the way sponsors structure projects and in particular on the selection of contractors and co-investors. Note the recent efforts of GdF Suez to seek Japanese sponsors for the Shuweihat 2 and Al-Dur projects in order to access JBIC funding.



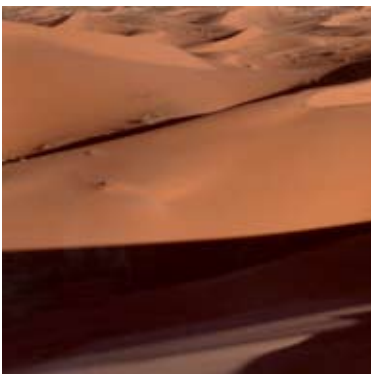
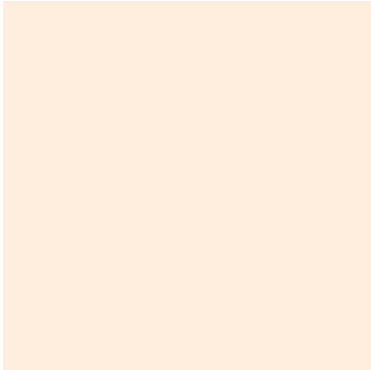
Regional financial institutions – a collective solution to a collective problem

There is scope for regional financial institutions to provide additional funding to projects. While their investments in projects to date has been limited (but see the investment by the IDB's infra fund in AES Oasis), there appears to be an increasing appetite for greater participation by regional bodies. The Islamic Development Bank, the Arab Fund for Economic and Social Development and similar regional development agencies seem likely to get involved in future infrastructure financings. The interest in Oman's Salalah IWPP is an example. In particular, regional shared facilities such as power transmission grids, nuclear generation facilities, water transmission systems and regional rail systems could benefit from such development agency funding. Since these agencies fund themselves from the global capital markets, they could act as a conduit to enable project sponsors indirectly to tap into these vast credit pools.

Domestic development agencies – a new role for SWFs?

The Saudi Industrial Development Fund (SIDF) and the Public Investment Fund (PIF) have been regular lenders to projects in the Kingdom. PIF is now prepared to increase its funding to 40 per cent of project debt and to extend the tenor of its loans from 15 to 20 years, although PIF participation in the project equity is typically a condition of its funding. The Saudi government has also established Bank Al-Inmaa, with a share capital of \$4bn, whose functions include supporting infrastructure projects.

SIDF is not expected to widen its mandate to support anything other than industrial projects, utilities projects for captive use within an industrial complex and infrastructure for industrial cities. However, the apparent readiness of the Saudi government to fill the funding gap is encouraging and should encourage private sector-sourced lending alongside it.



Saudi Arabia apart, there does appear to be room for other governments in the region to establish domestic development agencies with a remit to provide debt and equity to key infrastructure projects or to encourage existing agencies to focus more on the infrastructure space. In Abu Dhabi, the government-linked infrastructure funds, Mubadala Infrastructure Partners and ADIC-UBS, will hold an interest in the project company for the Mafraq-Ghweifat Highway, one of the largest PPPs currently under consideration. However, it is debatable whether such equity investments are needed for these projects to reach financial close when what is required is additional long-term funding that the commercial banks are unable or unwilling to provide. Even if their terms of establishment preclude these infrastructure funds from providing debt funding, many governments in the region have established sovereign wealth funds (SWFs) to invest their oil revenues. The SWFs are not so restricted in their investment capability. By investing in the region's infrastructure, these SWFs would be encouraging non-oil based economic growth and the diversification of local economies, something that is consistent with their objectives. Some of these SWFs are already active players in the infrastructure sector and have the ability to analyse the relevant risks. Those that do not can always secure the necessary capability from external advisers.

'Grey brick building' – pension funding of infrastructure

The need to secure long-term assets to match long-term pension liabilities should mean that pension funds and government-owned social security organisations are natural funders of infrastructure assets, but this is rarely so. There are many reasons why these institutional investors are absent from the market and it is perhaps unrealistic to expect them to be direct investors in project equity or debt. Nevertheless, there has been some recent activity. In Saudi Arabia, for example, the Public Pension Agency (PPA) may start to be seen as a lender to infrastructure projects. It has become involved as a sponsor on major real estate projects (Riyadh Financial City being one example) and there has been increasing project sponsorship from PIF and the General Organisation for Social Insurance. The Bahraini government has taken a tentative step, by encouraging the Social Insurance Organisation to take equity in the Al Dur IWPP. Major involvement of pension funds is unlikely to be seen, though, until regional capital markets can develop suitable products, such as infrastructure bonds, that will enable them to access the market more readily.

Take the money and run with it

Governments should consider providing direct funding support to projects. This can take several forms. One common form of support is the provision of capital grants and other contributions that reduce the amount of funding required by the project company, while maintaining the risk transfer from public to private sector. It also reduces the overall

cost of funding the project, as it is part-funded by the government. Government can structure bids for the project on the basis of the lowest amount of contribution requested (as was seen on the Saudi Landbridge in its original form). However, assuming that some external financing will be required, lenders may prefer to see a higher unitary charge over the life of the project, since lower repayments expose them to greater sensitivity to changes in operating costs. These may result in the need for more stringent financial covenants and higher margins to compensate for the increased risk. The timing of payment of capital contributions can also be critical: if they are paid at the end of the construction period, sponsors will still have to arrange construction finance, albeit of a short tenor.

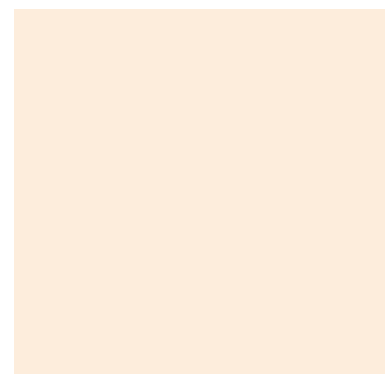
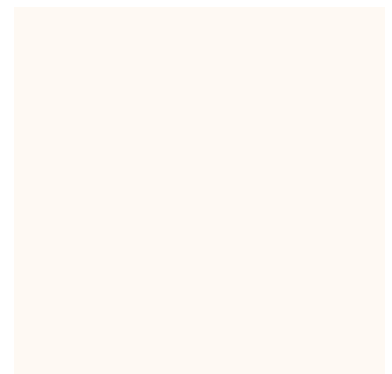
Turning the tables – government as co-lender or guarantor

There are several examples (UK, France, USA and Canada) of government lending programmes to provide finance where there is a funding shortfall. Governments in the region would do well to study these programmes. Private sector lenders have voiced concerns about governments as co-lenders under the same funding documents, as there are potential conflicts of interest for the public sector between its roles as funder and concession grantor/offtaker. This problem would be increased if government-related infrastructure funds were to participate as equity investors in the project company.

Co-lending is more attractive than providing grants or other forms of subsidy as it can be easily reversed by a commercial bank or bond refinancing when market conditions improve. It does require governments to have greater project financing skills in order to avoid undue delays to the financing of a project, but such skills are readily available in the market and can be contracted in. Government financiers may have a great deal of money, but rumours abound of more than one deal having suffered a substantial time delay due to the slow pace of activity at a national investment body. Streamlining the approvals process is thus vital.

The involvement of government lenders may also be seen (even if not used) as a stick to beat commercial lenders. With the promise (or should that be threat?) of government-backed finance on offer, a bank may cut its pricing or offer the sponsor better terms in order to remain in the deal, rather than having no business at all. This is a suggestion that has been made about the Treasury Infrastructure Finance Unit in the UK, but it has not really materialised.

Greater 'generosity' on the part of procuring authorities and/or government financiers may lead to the increased use of gain-sharing under project contracts. It is only reasonable for a government to want to benefit from a refinancing if the government has facilitated the financing in the first place. Whether sponsors will resist this or accept it as evidence of a maturing market remains to be seen.



A more sophisticated option is the use of guaranteed lending. Rather than ECA-style guarantees of commercial bank lending, in these cases it is the government that provides direct lending, thus providing long-term liquidity. The government debt is in turn guaranteed (or provided with some other form of credit wrap) by a commercial bank or other private sector entity. The key upsides of this approach are that the margin and swap spreads are lower, meaning a lower unitary charge (or equivalent) is payable, if applicable. The downside for governments is that they have to take the counterparty risk on the guarantors.

Governments should also consider intervening to cover the refinancing risk associated with the shorter maturities of available bank debt (hard and soft mini-perms). Refinancing risk could be covered through a 'no fault' termination sum payable under a concession for failure to refinance, with the banks recovering the project debt and sponsors recovering their original equity investment or taking an equity haircut. Adjustments would be made to the unitary charge to reflect the increased costs of refinancing (to a degree already covered on a soft mini-perm, which provides for margin ratchets if a deal has not been repaid at maturity) and governments would act as lender of last resort. There is an obvious tension between protecting sponsors and lenders from the consequences of a general market failure and ensuring that sponsors remain sufficiently incentivised to manage the refinancing risk. No clear market mechanism has evolved to resolve this conflict to date.

Pass the risk back

Governments could also facilitate syndication of project debt, either by guaranteeing that it will occur or by agreeing to cover specific risks that were preventing the process of syndication. The Liefkenshoek rail tunnel project in Belgium is a good example of the latter approach. Infrabel, the state-owned rail infrastructure provider which procured the tunnel, agreed to take market disruption risk for the duration of the construction period – more than four years. Infrabel's readiness to take the risk that the market disruption clause might be called during the construction phase was, above all else, what allowed the deal to achieve financial close. At the time, the lenders believed there was a real risk that Euribor would not accurately reflect their cost of funds, meaning an increase in the borrowing base rate. This is a good example of how lateral thinking by the public sector and a readiness to provide constructive support can get a deal through even under very difficult circumstances.

Showing the way – central PPP units and one-stop shops

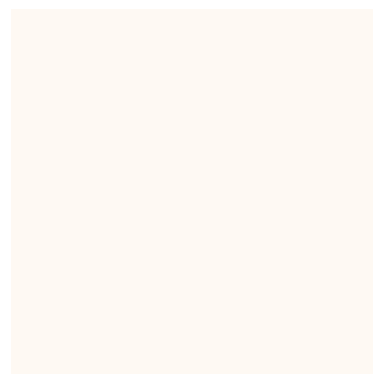
While public-private partnerships are seen in increasing numbers across the Middle East, there is often a lack of consistency in commercial terms, documentation and what procuring authorities will and will not accept. Egypt stands out from most other jurisdictions as it has a central PPP unit. Abu Dhabi also has an informal PPP cell. The Egyptian central PPP unit provides guidance and support to procuring authorities across all sectors where PPPs are used and ensures relative consistency of documentation. For investors, this provides added certainty on the terms of transactions and a more transparent procurement process. The roles of this unit include:

- establishing a national PPP policy framework for implementation;
- drafting and issuing standard project documents, contracts and PPP laws;
- co-ordinating the PPP programme and process across ministries, the private sector and the funding market;
- providing technical and advisory support for PPP transactions as well as ensuring compliance with the legislative framework; and
- acting as the:
 - centre of PPP expertise, support and intelligence gathering;
 - centre for capacity-building; and
 - central complaints resolution office for PPP investors.

By the same token, the use of a 'one-stop shop' mechanism is very attractive to the private sector. Rather than having to go to a plethora of official bodies to obtain licences, consents, permits and the like, a private sector investor is able to go to one body for all approvals. Saudi Arabia's King Abdullah Economic City (KAEC) is proposing to have the Saudi Arabian General Investment Authority act as a one-stop shop for all KAEC-related matters. This should facilitate private sector investment and thus the development of KAEC.

It almost goes without saying that clear, reliable and transparent PPP laws and privatisation laws more generally are key to attracting private sector involvement and private sector financing. A PPP unit can only be successful if it is able to operate within a sound legal framework.

Infrastructure investment would also benefit from reform of regional insolvency laws and those relating to security interests. It is regrettable that lenders cannot rely on robust security structures over project assets and in many regional jurisdictions have no certainty that an insolvency regime would permit the orderly unwind of a failed project in an objective and impartial manner.





The name's Bond...

The use of bond finance may appear attractive. Regional pension funds and wealthy private investors should be interested in purchasing these bonds, especially if sukuk are used. This would provide another source of infrastructure finance and help to develop regional capital markets. However, the very need for regional capital markets to be developed suggests that project bonds may not be a viable solution to the financing shortfall. In addition, benchmark rates have been difficult to assess.

The lack of benchmark rates is becoming less of a concern, though, thanks to government issues. Abu Dhabi's \$3bn bond issued in March 2009 – the first tranche of a \$10bn programme – and Qatar's subsequent issue of the same size have set the stage for the development of local capital markets. The issue of a \$1.25bn bond for the refinancing of the Dolphin pipeline indicates that project bonds may be coming into vogue. This theory is borne out by the current suggestion that bonds are being considered as part of the financing for Saudi Arabia's Jubail refinery.

Whether project bonds can be used for greenfield financing, as opposed to the refinancing of an existing asset, is open to discussion. Bond investors will be wary of taking on project completion risk, although this can be mitigated or removed by completion guarantees. One way in which governments could encourage the use of project bonds would be by wrapping the bonds with a government guarantee, although the financing/refinancing concern remains an issue.

One entity that has been notable in its use of bonds is Mubadala, the development company of Abu Dhabi. Mubadala has an unlimited global medium-term note programme that allows it access to the capital markets when it chooses. However, the very fact that Mubadala's programme is global rather than regional demonstrates that Middle Eastern capital markets do not yet have the depth required for major bond issuance. In addition, Mubadala's bonds are issued on a corporate (and effectively sovereign) basis rather than at a project level.

Funding competitions

Ordinarily, bidders for a project will arrange their own financing package and will often seek exclusivity from their lenders. This reduces availability and thus increases costs for all sponsors. Although this can be partially addressed by requiring a bidder to release its potential lenders from exclusivity if that bidder is not selected, this does not fully address the problem. One way of doing so would be to run an independent funding competition for the project.

The project would be tendered on a build-own-operate basis but without the requirement for bidders to obtain funding. Financiers would be invited to provide debt to the project but without bidder

exclusivity. This would, in theory, deepen the liquidity pool available and reduce the cost of financing for the project.

Clarifying tender processes

Governments have eased their tender requirements for new projects (Barka III and Sohar II in Oman and PP11 in Saudi Arabia) but more work could be done to revise inflexible procurement laws and otherwise improve the transparency and speed of the procurement process.

Smaller but more manageable

Governments should consider whether projects need to be delivered as a whole or can be broken down into more manageable phases that are easier for the banks to digest. Demand forecasts should be rigorously reviewed and adjusted to reflect the effect of the global economic slowdown as it may mean that an infrastructure programme can be more gradually deployed.



Conclusion: trial and error

At the moment it is impossible to say with confidence what the new normal for infrastructure finance in the region is likely to be. In reality, there will probably be many models, with project financiers deploying a range of structures to suit different projects. Having said that, there are three clear ways in which Middle Eastern infrastructure development can be driven forward.

Targeted government support

Although greater government participation in the short term is necessary, sentiment is improving and more banks are returning to the project finance market. What banks need now is the assurance that governments will bridge the funding gap, ideally through a combination of co-financing and by facilitating the refinancing risk, which will hopefully fall away as markets stabilise. Equally, having a government credit standing behind a concession agreement or an offtake agreement, whether explicitly or implicitly, should secure an offer of finance far more readily.

Tenors

For banks, shorter debt tenors are essentially a good thing. Their exposure is limited, an asset/liability mismatch is largely avoided and in the case of mini-perms there is an obligation (of varying strength) on sponsors to refinance. By the same token, longer project agreement tenors, that provide a tail beyond the end of the debt term, will help deals succeed. Tenors are lengthening again, but are unlikely to return any time soon to the durations seen in recent years. This means that refinancing risk will become a feature of most project financings.

The China option

Greater involvement of Chinese contractors should bring huge benefits to Middle Eastern infrastructure development. Chinese firms should win an increasing number of contracts. The key question is whether Chinese banks will be permitted to support such contracts to the required extent or whether the demands of China's domestic infrastructure programme will curtail such funding sources.

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