

Project Finance

Presentation to
The APGAS Forum, Perth WA

1 – 2 September 2005

Michael Dulaney

Freehills

What is Project Finance?

The financing of an asset where debt service and returns on equity are derived from the cashflows generated by the asset



Freehills

Features

- **Cashflow**

- is the most important consideration
- sufficiency to service debt and provide return on equity

- **Limited recourse to Sponsors**

- **Security over project assets**

- **Technical and economic evaluation**

- directly related to ability to produce cashflow and the degree of risk associated with that cashflow

Freehills

What's important to a Lender?

- **Anything that affects the cashflows of the project**
 - Cash control (information)
 - Expenditure control (feedstock)
 - Dividend restrictions (clawbacks)
 - Production payments (off-take)
 - Risk / volatility of any of the above
- **Sponsor recourse**

Lenders cont.

- **Step-in rights**
 - cure rights/sale rights
- **Risk allocation in project documents**
 - alignment of interests of project participants
 - resilience of the project to shocks and still able to service debt
- **Reputation, creditworthiness and operational experience of the Sponsor**
- **Security over the Project**

What's important to a Borrower?

- Balance the cost of funding vs. flexibility
- Achieving returns from the project company
- No hair-trigger defaults
- Balance between strict controls and a successful operation
- Ability to refinance
- Ability to sell-down its interest

Project risks

Resource Risk

- Mitigants
 - addressed at feasibility and due diligence stages (geological, metallurgical and mining reports)
 - documents monitoring and ratio provisions.

Completion Risk

- Mitigants
 - sponsor guarantee/direct liability
 - third party support (letter of credit, bank guarantee, builder performance bond).

Freehills

Project risks

Technological Risk

- Mitigants
 - similar to Completion risk.

Operational Risk

- Mitigants
 - project covenants re performance standards
 - Additional security
 - insurances
 - replacing sponsor operator with appropriately experienced third party operator.

Project risks

Environmental Risk

- Mitigants
 - environmental assessment or audit as part of feasibility or due diligence
 - warranties and covenants.

Cost Overrun risk

- Mitigants
 - direct sponsor support (ie cash injection undertaking)
 - sponsor procured support.

Project risks

Market Risk

- Mitigants
 - feasibility study initially, and subsequent monitoring and reporting (eg traffic volumes for tollway, patronage levels for passenger rail service)
 - long term sale contracts at agreed (adjustable) prices
 - future or hedge contracts to guarantee sale price
 - take or pay contracts.

Political risk

- Acts or omissions of Governmental Authority
- Delays in obtaining permits or approvals
- Changes in Law, such as taxes, exchange controls, licensing regimes, land tenure
- Expropriation or nationalisation
- Civil unrest or insurrection leading to Project closure
- Termination or variation of Government contracts