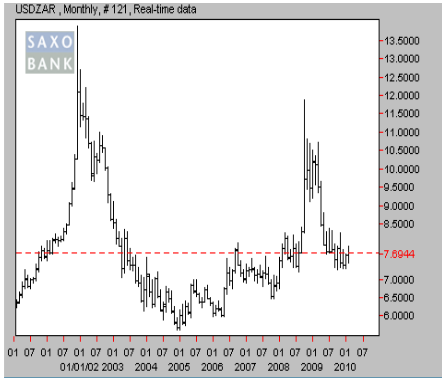
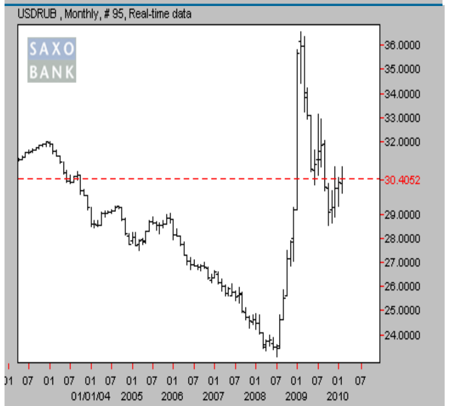
Local Currency Finance

From Theory to Practice

Innovating to Enhance Access to
Finance: Long-Term Finance for
Essential Public Infrastructure
March 2010, Paris

Impact of currency fluctuation





- Typical peak to trough over last decade > 50% - even more extreme during 1998 Asia / Russia crisis

- Most moves are gentle but occasionally they are brutal

- Spotting short / medium term trends possible but most major capital projects require long term finance

- For exotic currencies long term hedging often not possible or very expensive

- We are all wise in hindsight but if we could predict the future none of us would need to attend this conference………

Why local currency finance?

Better solution at project level

- Local currency finance matches currency of revenue to debt service
- Even if a project has the right to pass on currency losses, prices / tariffs may be unaffordable - contractual agreements may fail
- Involving local lenders can reduce the risk of discriminatory action

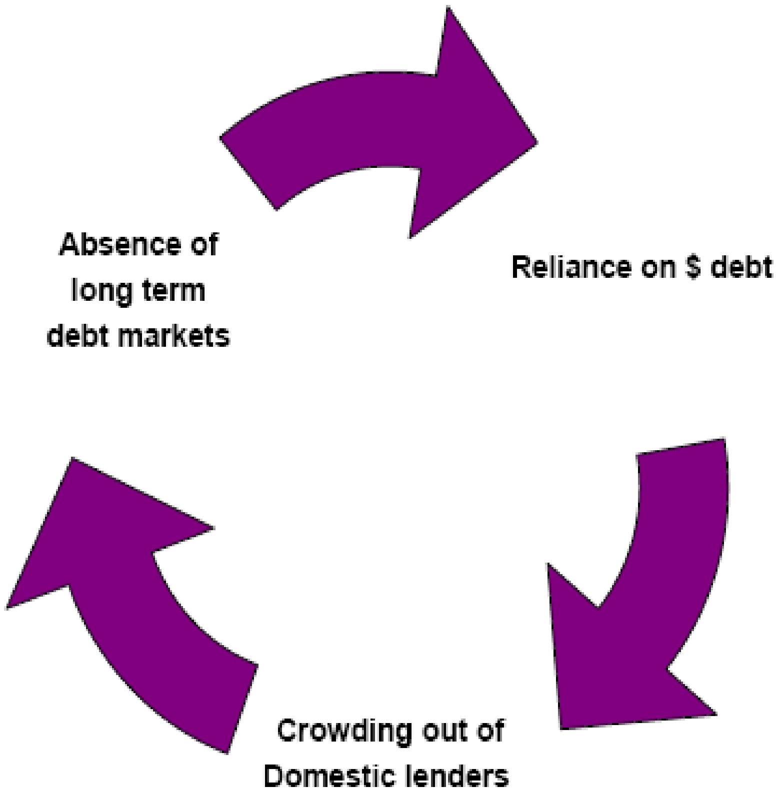
….. But also country level – responsible banking!

- Local currency financing involves productive recycling of savings <u>within</u> a country rather than increasing the country's <u>external</u> debt burden
- Involving local lenders helps build capacity to finance future projects

….so why are many projects still financed cross border in $ or € ?

We're all used to working in traditional ways……

- International lenders dominate project finance – they find it easier to lend in $ or €
- Silo mentality
- Product led not customer focussed
- National utilities are used to accepting pass through of currency risks from developers



That said……..

- Local banks often lack expertise
- Local tenors often short / interest rates high

Capacity building in local markets – partnership approach

- Funding of projects by domestic banks / pension funds who take as much or as little risk as they wish
- Guarantee from GuarantCo for remaining risks - in particular, tenor extension
- Happy to work with international or regional banks with a local presence
- There is empirical evidence that risk sharing builds confidence, competence and greater risk appetite of lenders
- GuarantCo anticipates most of its transactions will eventually be refinanced without need for credit enhancement -and actively encourages this transition

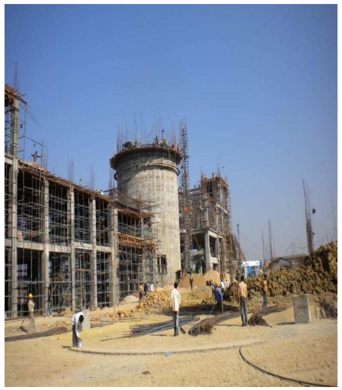
Impact of credit crisis

Developed markets crisis:

- Margins rising / tenors falling
- Reduction in active lenders
- Return to base mentality
- Uncertainty over future capital and regulatory environment
- New sources of risk cover being sought

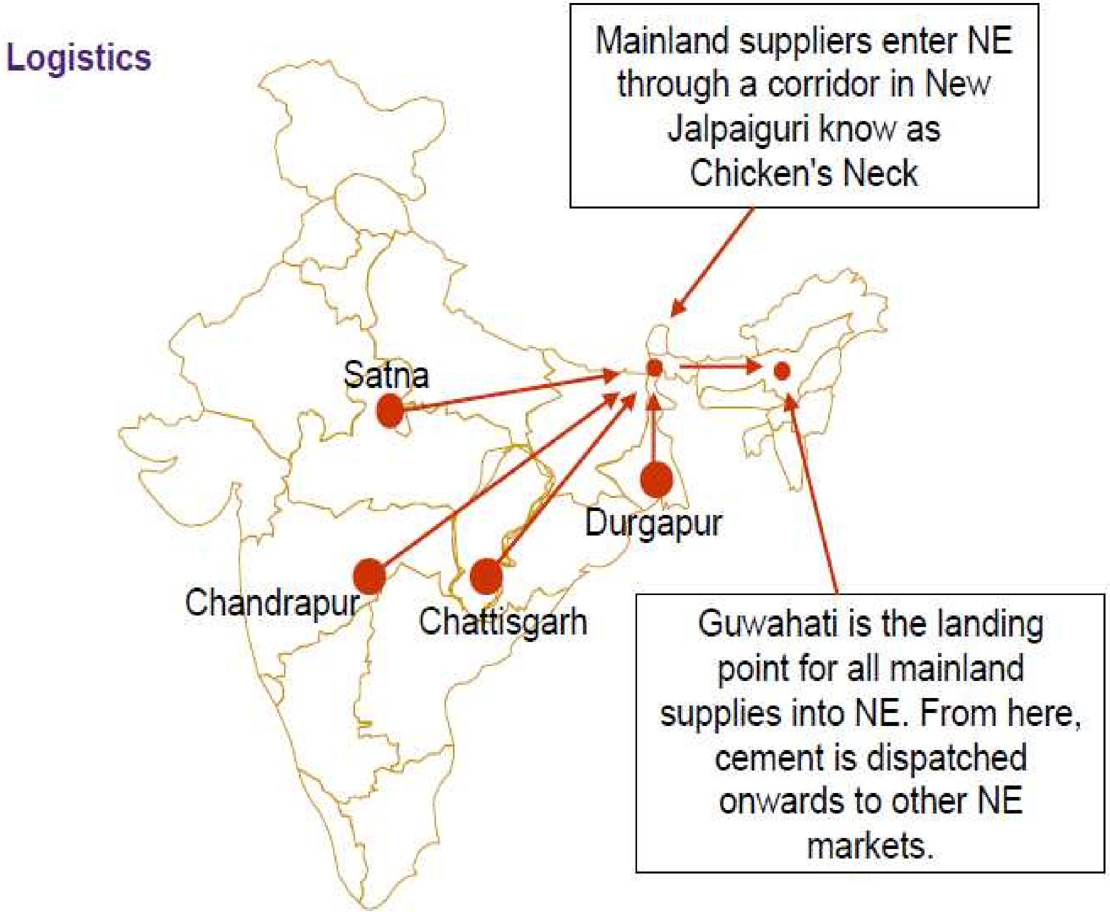
- Local Finance no longer last resort

Case study - 1.7m ton cement plant, Assam, India



- Equity from local cement producer, FMO, DEG + Govt. of Assam
- Total project cost INR 5.5bn
- Main equipment imported from ThyssenKrupp, Germany
- Debt / equity 70 : 30
- 10 year tenor, limited recourse project finance structure
- GuarantCo guaranteeing 34% of debt, partly syndicated to Cordiant Capital, Montreal
- Axis Bank lending against partial risk gtee, HDFC Bank lending against 100% gtee
- Currently considering an INR 400m increase in guarantee to meet capacity expansion

Calcom Cement
Why GuarantCo?



Calcom is strategically placed, owns access to limestone, low cost and latest technology…….

but…………

- *Assam has a history of insurgency*
- *the developer is small compared with competition – expanding capacity five-fold*
- *Limited Indian bank appetite*
- *Dfi's only used to lending $ or Euro*

Wataniya Palestine Telecom

- Second GSM operator in Palestinian Territories
- Initial equity from QTEL / PIF > $200m
- $85m senior secured 7yr limited recourse debt facility
  - $22m from Ericsson Credit / Standard Bank with partial risk guarantee from EKN
  - $30m from IFC Washington
  - *<u>$33m from 3 Palestinian Banks with partial risk guarantee from GuarantCo</u>*
- Highly politicised transaction
- Global Trade Review best ME Telecom deal 2009

Wataniya Palestine Telecom - Why GuarantCo?

- Wataniya wanted to maximise involvement of local banks
- Local banks had no project finance experience but liquid and very motivated to join financing
- Palestinian Monetary Authority imposes single obligor limits on lending
- Regional banks did not step up

- EKN could take political risk but could not guarantee local lenders
- Mounting tension between Israel and Palestinian Territories

GuarantCo's credit decision taken on purely commercial grounds

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