

Kick Starting the Infrastructure Finance Market

March 2009

Strictly Private & Confidential





- State of the funding markets and why we find ourselves in the position that we do today
- How Governments worldwide are responding to the funding crisis
- How this funding log jam can be unblocked



To help kick start infrastructure lending Government needs to


- First recognise there is a problem which won't self correct itself but needs affirmative action
- Improve the existing procurement process
- Promote new product attractive to both banks and investors



- Recession is good for essential infrastructure
 - Governments use it as a fiscal stimulus
 - Though volumes fall, roads, ports, power stations and airports continue to be used

- Infrastructure gets into trouble when it is too highly geared as a result of
 - Funding on the basis of over optimistic growth prospects
 - Assuming too much refinancing risk

- The infrastructure boom was driven by an oversupply of cheap money and an the assumption that refinancing would always be an opportunity not a challenge

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Funding for the PPP market has been badly affected by the current credit crisis, despite the strong fundamentals of the sector


Bank Finance

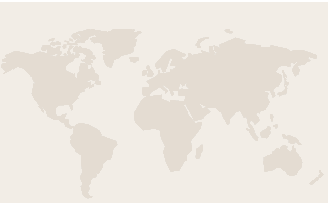
- Banks are not natural long term fixed rate lenders
- Despite this they became the dominant source in the PPP market in 2000–2007 due to tight pricing and aggressive terms
- As balance sheets have become constrained and funding more costly, these banks are now withdrawing capital from the market
- This problem has been exacerbated by :
 - The collapse of the specialist long dated, infrastructure lending banks who had lent globally — Depfa, Dexia, Eurohypo, Fortis etc. and
 - The failure of the bank syndication market so transactions have become dependent on club deals with banks committed to take & hold over the long term

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Bond Finance

- At the same time, access to the bond market has been restricted by the failure of the monolines who
 - Traditionally have been the route for accessing the bond markets in a number of jurisdictions for instance UK and Australia, and
 - Were willing to accept weaker credit rating than institutional investors on deals on an unwrapped basis
- Nevertheless, global bond investors are currently
 - Highly liquid
 - Underweight duration (i.e. maturity) and CPI / RPI
 - Overweight financial institutions and underweight corporate exposure
 - Keen on “utility style” credits

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- As a result there are a significant number of stranded PPPs around the world, where the proposed financing terms have become increasingly fanciful particularly for larger PPP transactions
 - Governments now need
 - To find a solution for existing deals at preferred bidder stage due to inappropriate financing structures
 - To re-impose discipline on current bids to ensure that pricing is realistic and the financing deliverable
 - We believe there are a number of ways in which Government can be more proactive in the procurement of finance by
 - Unblocking the funding markets for existing and upcoming PPPs
 - Encouraging access to both bank and non-bank sources of funding



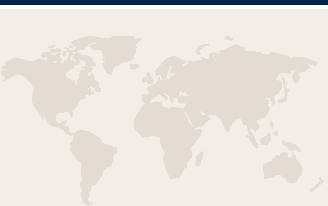
- 935 PFI deals closed in UK between 1995 – 2008 with a combined value of £66 billion
 - Number of signed PFI deals over last 12 months at **lowest** level since 1995
 - 34 transactions have closed during 2008 versus 60 in 2007, amounting to c. £6.5 billion
- These breakdown between
 - Defence (£3.2 billion, including £2.2bn FSTA project)
 - Education (£1.6 billion)
 - Health (£500 million)
 - Transport (Nil)
- In Europe, 22 PPPs closed in 2008 with combined value of €5 billion versus €7.4 billion in both 2007 and 2006
- In Canada, 10 PPPs closed in 2008 totalling C\$4.8 billion versus 22 PPPs totalling C\$3.8 billion in 2007

Europe — challenging deals

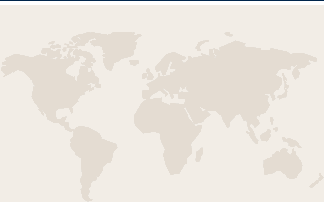
Deal	Size & Tenor	Initial Funding Solution	Status	Expected Outcome
M25 (UK)	STG1.2bn 27 years	Syndicated Bank debt and EIB	PB	<ul style="list-style-type: none"> ■ STG500–600m bank club deal ■ EIB and Govt funding. Refinancing incentives at years 7 and 10 ■ 100% cash sweep from year 7
Manchester Waste (UK)	STG600m 23.5 years	Bank debt and EIB	PB	<ul style="list-style-type: none"> ■ Bank Debt, EIB + Capital contribution from public sector and additional equity support
Fife Hospital (UK)	STG300m 29.5 years	Bank Debt	PB	<ul style="list-style-type: none"> ■ Bank Debt + Capital contribution from public sector
GSMR (France)	€600m Up to 14 years	Bank debt	PB	<ul style="list-style-type: none"> ■ Bank debt
French High Speed Rail Schemes (France)	Up to €10bn Up to 30 years	Bank debt	Initial bids submitted	<ul style="list-style-type: none"> ■ Bank debt and Central and Regional Government support
Nord Seine Canal (France)	Up to €4bn Up to 30 years	Bank debt and / or bond and Government support	RFQ stage	<ul style="list-style-type: none"> ■ Bank debt and / or bond and Government support

Canada — challenging deals


Deal	Size & Tenor	Initial Funding Solution	Status	Expected Outcome
Port Mann Highway	C\$2,100m	Bank debt	Closed March 2009	<ul style="list-style-type: none"> ■ D & B ■ Fully funded by Province
Niagara Hospital	C\$600m	Bank debt	PB	<ul style="list-style-type: none"> ■ Bank debt and / or bond with increased capital contributions from Government to reduce external financing requirement
McGill University Health Centre	C\$1,000m	Bank Debt and / or bond	Shortlisted	<ul style="list-style-type: none"> ■ To be determined
Centre Hospitalier de L'Universite de Motreal (CHUM)	C\$1,000m	Bank Debt and / or bond	Shortlisted	<ul style="list-style-type: none"> ■ To be determined





Government Action

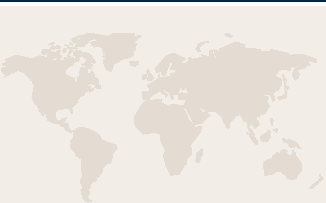


- European Investment Bank (EIB)
 - Providing liquidity, by increasing their participation in deals and relaxing lending criteria
 - M80 where they lent more than the sacrosanct 50% of total funding, and
 - Though education projects are outside their remit, EIB now has agreement to lend up to GBP 300 million via the UK's 'Building Schools for the Future' programme
- The European PPP Expertise Centre (EPEC)
 - Launched by EIB in September 2008 in collaboration with European Union Member and Candidate States and the European Commission
 - Designed to enable EU Member and Candidate countries to share experience, expertise, and best practice relating to PPP transactions

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- UK has been indecisive to date but on 3rd March announced a programme — *“Safeguarding Government Infrastructure investment”*
 - Some £15 billion of projects will be eligible, £8 billion due to close this fiscal year
 - Up to £1–2 billion available to ensure that PFI infrastructure projects get under way as swiftly as possible whilst preserving the benefits of the PFI procurement method
 - Key points
 - Will be run on an arms length basis and have its own credit committee
 - Price taker not maker
 - Minority lender (though reserve right to fund 100%)
 - Equal rights as commercial lenders — at least as a starting point
 - Still no help to the secondary market
 - Seen as a “short-term fix” to get the current backlog of deals to financial close - a longer-term plan for how PFI will be funded to be formed

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- The French Government is the most pro-active Government in Europe to address the issues facing the PPP markets
 - France's needs are the greatest, given the number of large PPP projects in the pipeline
 - Infrastructure is at the heart of the 'Plan de Relance' recently announced parts of which are directly aimed at facilitating PPP Financing
 - A €10 billion 'envelope' has been earmarked to provide guaranties for this purpose
 - The French Government will guarantee up to 80% of the PPP consortium's senior debt on selected projects
 - The Government could also underwrite the refinancing risk following a mini-perm financing
 - In addition, the CDC has a €8 billion 'envelope' to lend to large infrastructure project
 - CDC is increasingly being used as a provider of stapled financing

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- Two high-profile deals have been stalled in Canada
 - Niagara Health System AFP project
 - Port Mann / Highway 1 PPP project — recently closed as a D&B
 - Large pipeline across the provinces, particularly in Quebec, Ontario and British Columbia
 - Provinces across Canada are considering a number of options to assist in getting PPP deals to close
 - Increased capital contributions in the form of construction milestone and substantial completion payments
 - Fast closing from bid date
 - Requirement for bidders to engage potential funders on a non-exclusive basis throughout the bid process



What else can Governments do ?

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What else can Governments do ?

- Run a funding competition post Preferred Bidder
- Stapled Debt — Procuring Authority sets the funding parameters and sources the debt
 - Attractive to debt providers encouraging them to offer lower cost funding
 - Gives the Authority more control and confidence over funders and structure selected
 - Bidders remain free to offer more competitive solutions

Some Solutions — Alternative Funding Options





- A Bond solution — Unwrapped Bonds
- A Bank solution — Mini-Perms
- A Public Sector solution — Guaranteed Debt


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- Capital markets remain a natural fit for long-term infrastructure assets
 - Market remains open — several long dated bond issues for Utilities and Housing Associations have been successfully launched in last couple of months
 - Comparison in Europe is largely with utilities and indicates maximum liquidity would be achieved for bonds rated BBB+ / A-
 - This rating can be achieved by a variety of structural changes though the key with the rating agencies seems to be construction risk mitigation

Other issues to Address

- Confidentiality
- Institutional investors have to date relied on the monolines for surveillance

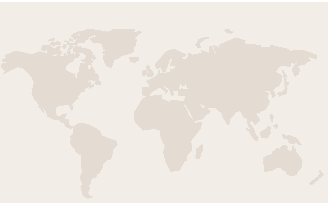
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- Mini-perm structures are common in North America and match investors more closely.
 - Banks understand construction risk
 - Capital markets want long term stable yield
 - Mini-perm — strong incentives to refinance early (i.e. margin step-ups, dividend restrictions, cash sweeps)
 - A mini-perm structure relies on a capital markets take-out be it into the bond market or the bank market
 - Who takes refinancing / term-out risk — price and availability of term market?
 - For highly geared structures equity could not reasonably take these risks
 - Some flexibility could be achieved by long term-out periods (e.g. 5 years of steadily ramping margins post completion)

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- A faint, light-colored world map is visible in the background on the left side of the slide.
- Structured as a “soft” mini-perm
 - Combination of commercial bank debt, EIB and Government funding
 - 27 years debt with refinancing incentives in years 7 and 10 in form of
 - Margin step-ups
 - Cash sweeps
 - Strong construction package
 - L / C for a % of construction price
 - Joint and several guarantee from parent companies
 - Gearing of 80:20
 - Implied rating of low investment grade
 - Pricing starting at LIBOR + 250bps stepping up to LIBOR + 350bps
 - 20 banks have shown an interest but how many will turn up at the party?!

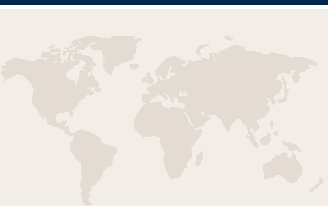
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- Financed by public sector either through grant, debt or guarantee
 - Range of models have been tried and tested and largely abandoned
 - DBFT where project is transferred to Authority on construction completion e.g. Evergreen
 - Equity only models where the Authority provides all the debt e.g. RSME
 - “Cession Dailly” — model in France and the Netherlands where Government guarantee is triggered on construction completion
 - Public / Private co-lending seems to be the preferred direction in which certain European Governments are heading

BUT

- It raises inter-creditor issues particularly where Government lends more than 50% of debt
- It raises potential conflicts of interest between Government as lender and Government as Procuring Authority
- Will it stifle the bank debt market?



- Appropriately structured and priced infrastructure remains a very attractive asset class
- Sudden loss of appetite for long term lending NOT an issue of credit quality nor a sector specific to PFI
- Governments can help in a variety of ways
 - They can improve the procurement process and ensure maximum available capital is sourced
 - They can encourage the development of new product and stimulate new sources of finance
- All are relatively easy to implement and all require minimal changes to the PFI procurement process and documentation

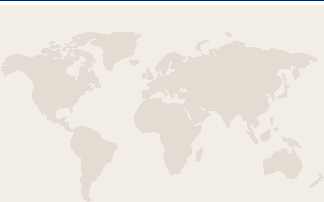


Appendix

Landmark Deals over last 12 months — Bank Debt



Deal	Size & Tenor	Funding Solution	Closing Date	Pricing
FSTA (UK)	£2,200m 23.5 years	Bank debt	February 2008	<ul style="list-style-type: none"> ■ BBB+ externally rated ■ LIBOR + 105bps
Kromhout (Netherlands)	€265m 27 years	Bank debt	July 2008	<ul style="list-style-type: none"> ■ Unrated ■ EURIBOR + 100bps
A30 (Canada)	C\$1,100m 30 years	Bank debt	September 2008	<ul style="list-style-type: none"> ■ Unrated ■ CDOR + 170 – 225bps
Lieftenshoek Tunnel (Belgium)	€840m 35 years	Bank debt EIB	November 2008	<ul style="list-style-type: none"> ■ Unrated ■ LIBOR + 105bps ■ Cash sweeps ■ Margin step-ups ■ Gov. guaranteed lending rate for 4 years
Douro Interior Highway (Portugal)	€767.5m 27 years	Bank debt	November 2008	<ul style="list-style-type: none"> ■ Unrated ■ LIBOR + 230 – 250bps ■ Cash sweep from year 8
M80 (UK)	£300m 32 years	Bank debt EIB	January 2009	<ul style="list-style-type: none"> ■ Unrated ■ LIBOR + 190 – 210bps ■ EIB more than 50%



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