

Sustainable Water Integrated Management (SWIM)

Regional Training Event

Funded by the EU European Neighbourhood and Partnership Instrument
(ENPI) South/Environment.

TRAINING ON EVALUATING AND STRUCTURING PPPs IN THE WATER SECTOR

Day 2 – Session 2: Credit Enhancement Mechanisms – Making PPP Bankable & Attractive

by

Jan G. Janssens

Chair IWA Task Group Performance-based Contracts

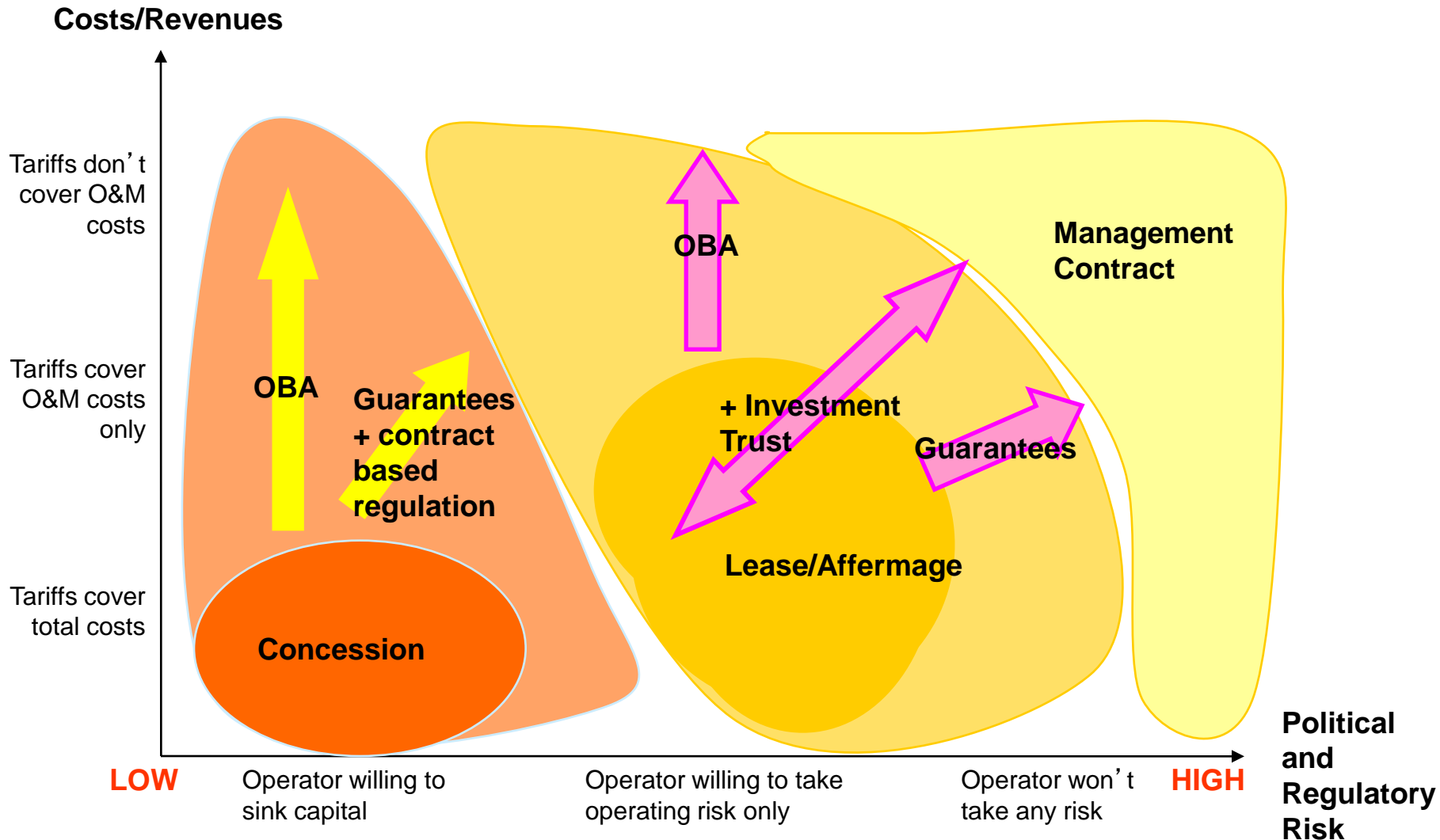
Principal Director J2C Water Ltd.

jangjanssens2009@gmail.com

8 -10 June 2015, Dead Sea (Jordan)



Choosing enhanced models



Source: Water Operators Round Table, Nov. 2004

The Role of Guarantees (1)

- Guarantees to underwrite a portion of the commercial risks has also been introduced selectively by the multi lateral banks like the EIB and the WB, while USAID offers the DCA (Development Credit Agency) program.
- Guarantees are mostly used to allow the Project company /sponsor easier and less pricey access to the capital markets.

The Role of Guarantees (2)

- The EIB/EC has initiated an instrument of risk sharing to strengthen the financial profile of promoters and projects and to improve access to debt financing for key infrastructure projects within the EU:
 - Risk-sharing Finance Facility (RSFF) in which by using convertibility between senior and subordinated debt, risk is reduced
 - Loan Guarantee Facility for TEN-Transport (LGTT)
- Financial Guarantees may prove crucial given the current situation in the MENA countries

The Role of Non-Financial Guarantees

Depending on the project Government may reduce the risk to the private sector through guarantees:

- ✓ Typically in a bulk water scheme, it may be a “take-or-pay” type of guarantee, or
- ✓ In a distribution network it could be a minimum demand guarantee.
- ✓ And in extreme cases it could even be debt guarantees to launch specific programs like NRW reduction.

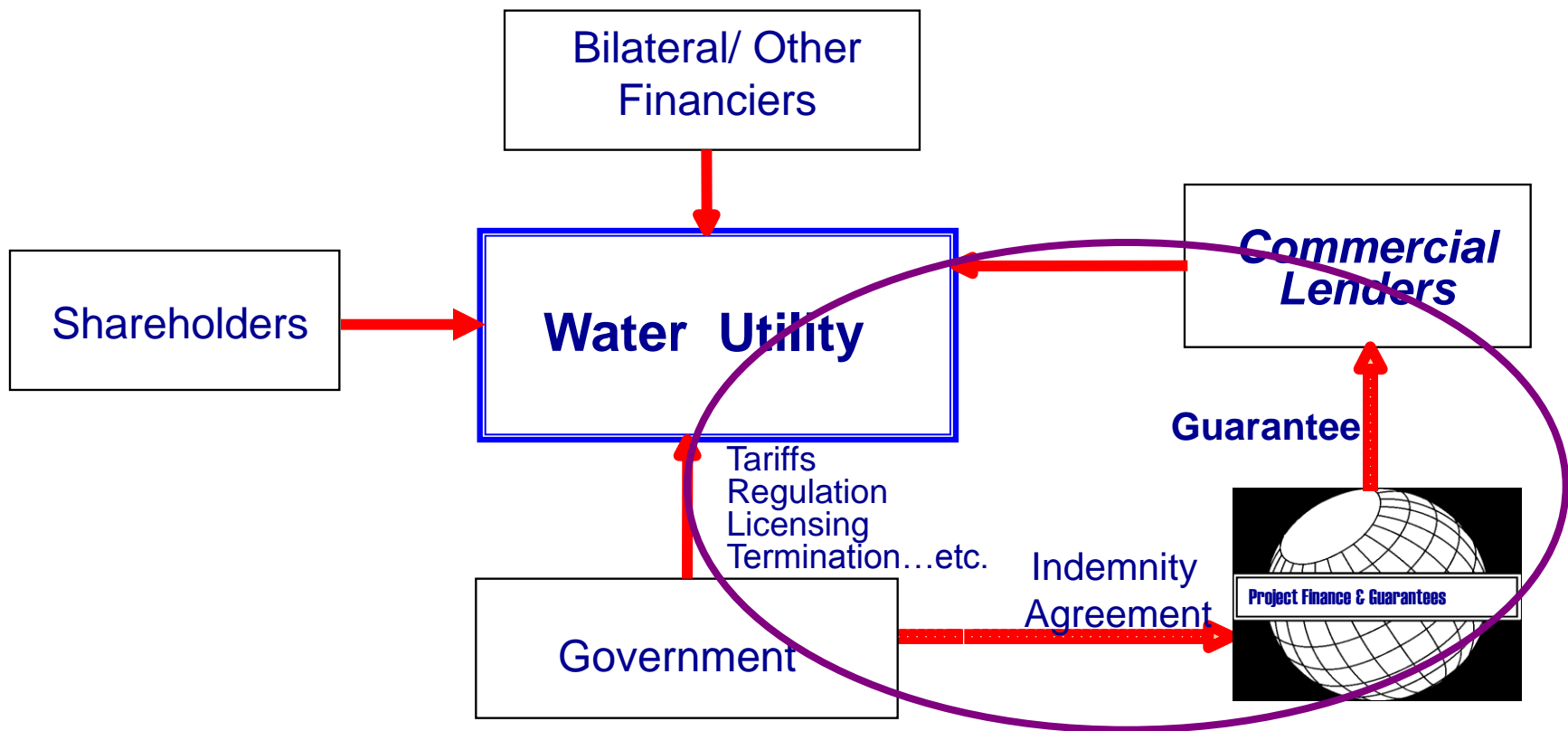
Deployment of the PRG

PRGs should be considered in the following situations:

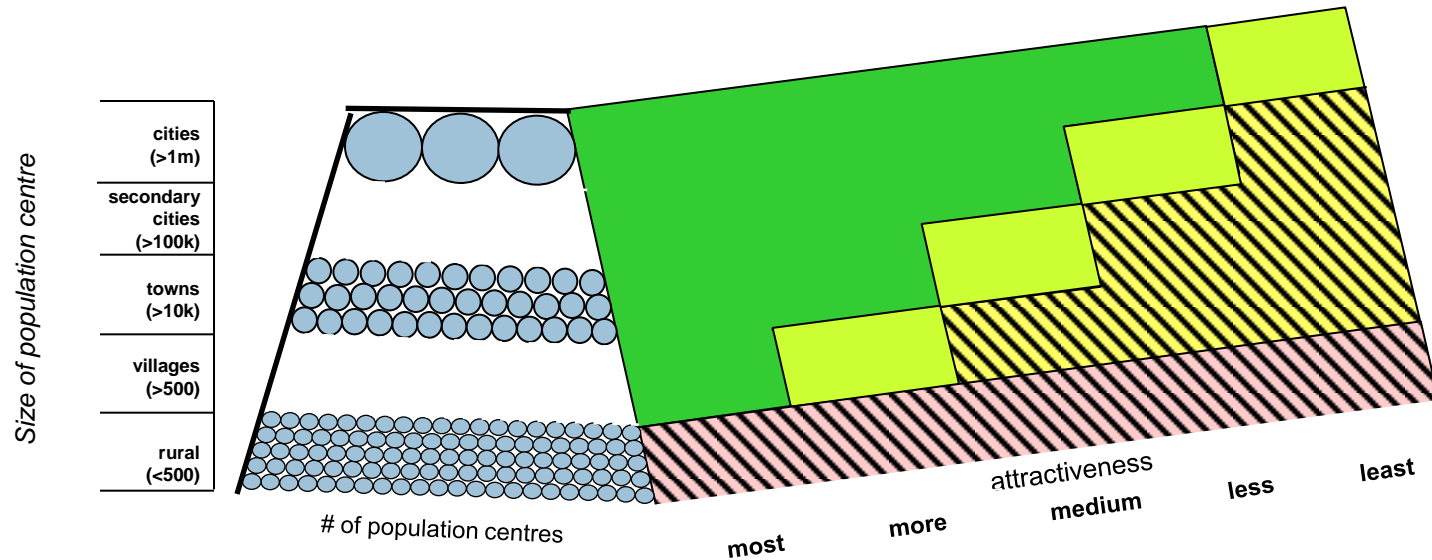
- ❖ Early stages of reform
- ❖ Larger size/riskier operations
- ❖ Operations highly dependent on support/undertakings of weaker governments/municipalities






Partial Risk Guarantee (PRG)

A PRG will cover lenders in case of a default on a covered contractual obligation to a project company leading to a Debt Service Default

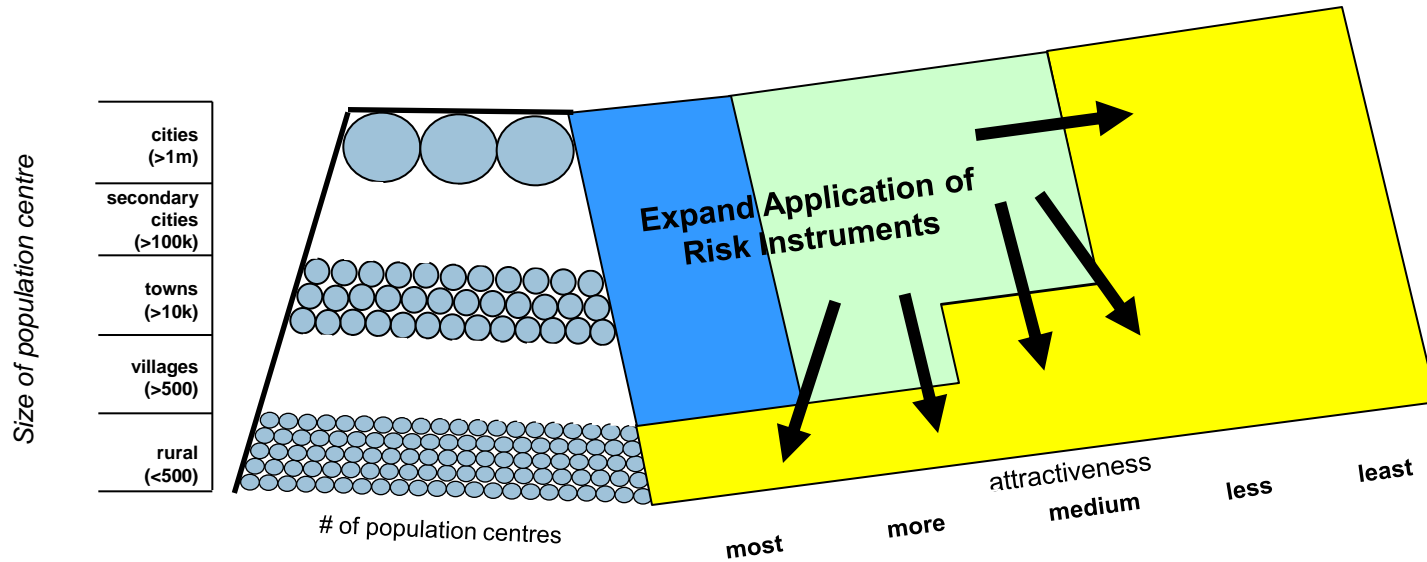





The market poses special challenges



	high potential for private financing		low potential for private financing		Need for public investment
	medium potential for private financing		Household & micro-financing		

The Risk Mitigation Instruments: Needed, Available ? Used?



	Do not require risk mitigation, Adequately credit worthy		Risk mitigation instruments could be effective: Nearly/marginally creditworthy & reforming
	Risk mitigation instruments will be ineffective: Non-creditworthy and low performing or instruments too expensive		

Where risk mitigation can make a difference

- Adequately Creditworthy – Do Not Require Risk Mitigation
- Near Creditworthiness
- Marginally Creditworthy, but Reforming
- Non Creditworthy and Low Performing

Risk Mitigation Instruments Could Be Effective

Credit Guarantees

Credit Guarantees cover losses in the event of a debt service default regardless of the cause of default (that is, both political and commercial risks are covered with no differentiation of the source of risks that caused the default).

✓ *Partial Credit Guarantees (PCGs)* fall into this category and cover “part” of the debt service of a debt instrument (regardless of the cause of default). Typically, a PCG would improve the terms of the commercial debt of the borrower, extending the maturity and/or reducing interest rate costs, through the sharing of the borrower’s credit risk between the lenders and the guarantor.

✓ *Export Credit Guarantees or Insurance* cover losses for exporters or lenders financing projects tied to the export of goods and services. Export credit guarantees or insurance cover some percentages of both political risk and commercial risk.

Political Risk Guarantees

Political Risk Guarantees or Insurance cover losses caused by specified political risk events. They are typically referred to as ***Partial Risk Guarantees (PRGs)***, or ***Political Risk Insurance (PRI)*** depending on the provider.

- ✓ PRGs cover commercial lenders in private projects. They typically cover the full amount of debt. Payment is made only if the debt default is caused by risks specified under the guarantee. Such risks are political in nature and are defined on a case-by-case basis.
- ✓ PRI, or investment insurance, can insure equity investors or lenders. PRI can cover the default by a sovereign or corporate entity but only if the reason for a loss is due to political risks.

The Role of IFI Risk Mitigation Instruments

“...is to address the need for political risk mitigation products by commercial lenders, debt and/or equity investors contemplating investment in developing countries...”

For lenders and investors these products can:

- Mitigate threshold risks—allowing investment consideration in potentially high risk markets
- Enhance credit-worthiness/lower investment costs--by insuring against specific risks
- Provide access to “honest broker” services of IFIs-- in negotiations with a government

Categories of Risk Instruments

The risks faced and instruments available to investors, lenders and bondholders in emerging markets projects fall into the following risk categories:

- Political Risks
- Contractual/Regulatory Risks
- Credit Risks
- Foreign Exchange Risks

What is MIGA ?

Multilateral Investment Guarantee Agency
(MIGA) is part of the World Bank Group.

World Bank Group

IBRD
International Bank
for Reconstruction
and Development

Est. 1945

Role: To promote institutional, legal and regulatory reform

Clients: Governments of member countries with per capita income between \$1,025 and \$6,055.

Products:

- Technical Assistance
- Loans
- Policy Advice

IDA
International
Development
Association

Est. 1960

To promote institutional, legal and regulatory reform

Governments of poorest countries with per capita income of less than \$1,025

- Technical Assistance
- Interest Free Loans
- Policy Advice

IFC
International
Finance
Corporation

Est. 1956

To promote private sector development

Private companies in member countries

- Equity/Quasi-Equity
- Long-term Loans
- Advisory Services

MIGA
Multilateral
Investment
Guarantee Agency

Est. 1988

To promote cross-border investments

Foreign investors in member countries

Credit Enhancement and Political Risk Insurance for Financial Institutions (loans) and Investors (equity & shareholders loans)

←..... **Shared Mission: “End extreme poverty and build shared prosperity”**→

What does MIGA do?

MIGA promotes foreign direct investment by providing:

- Non-commercial (political) risk insurance (guarantees) for investors and lenders. Commercial risks not eligible
- Dispute mediation services, to remove obstacles to current and future investments. Proven success in supporting resolution of investment disputes between states and investors
- Technical assistance to help countries attract and retain FDI through FIAS (Foreign Investment Advisory Services), a joint department of World Bank Group Institutions
- Online information on investment opportunities and operating conditions in developing countries

MIGA Eligibility/Terms of Coverage - 1

1. Investment must be cross border between member countries into developing member country (**North-South** and **South-South**)
2. Cannot participate in purely local deals
3. Eligible sectors: All except standard exclusions (tobacco, weapons, etc....)
4. MIGA can cover new investments, and existing projects, on a project-per-project, or portfolio, basis
5. Coverage of:
 - Equity, including shareholder loans, various profit sharing agreements (management contracts, leases...) capital market transactions.....
 - Loans, together with equity, or on a stand-alone basis
 - Loan guarantees (for the benefit of foreign or local banks)

MIGA Eligibility/Terms of Coverage - 2

6. Minimum term 1 year; maximum of 15, up to 20 in some cases
7. Amounts, Coverage and Pricing
 - MIGA typically can arrange cover for all amounts, on its own books and through the PRI market (co/reinsurance). No minimum amount for guarantee or size of investment
 - Equity typically covered up to 90% & debt up to 95%
 - Premiums are paid annually or semi-annually and are calculated as a percentage rate applied to the amount of coverage. Premium rates are decided on a per project basis and vary by country, sector, transaction and the type of risk insured

MIGA's PRI Products

- **Political risk insurance coverage**

4 categories of covered political risks:

War, Expropriation, Non Transfer and Breach of Contract

- **Credit enhancement products**

(comprehensive risk coverage, political and commercial)

Non Honoring of Financial Obligations

Types of Political Risk covered by MIGA - 1

Expropriation

- ✓ Protects against government actions which deprives the investor of ownership, control or benefit of the guaranteed investment.
- ✓ Protects against losses arising from:
 - Nationalization and confiscation
 - Creeping expropriation (e.g. through regulatory acts)
 - Partial expropriation (expropriation of funds)

Types of Political Risk covered by MIGA - 2

Breach of Contract

- ✓ Protects against failure by the host government to honor contractual obligations.
- ✓ Protects against breach or repudiation of a contract between the investor and the Host Country authorities
(non-enforcement of an arbitration/judicial award is a prerequisite)
- ✓ Applied to (typically relating to infrastructure or resource projects)
 - Supply/off-take agreements
 - License agreements
 - Sub sovereign obligations & obligations from SOEs

Types of Political Risk covered by MIGA - 3

War and Civil Disturbance

- ✓ Protects against damage/disappearance of tangible assets (including revolution, insurrection, coups d'état, sabotage, and terrorism).
- ✓ Protects against prolonged business interruption resulting from revolution, insurrection, coups d'état sabotage and terrorism.
- ✓ Acts must have a primary intent of achieving a political objective

Types of Political Risk covered by MIGA - 4

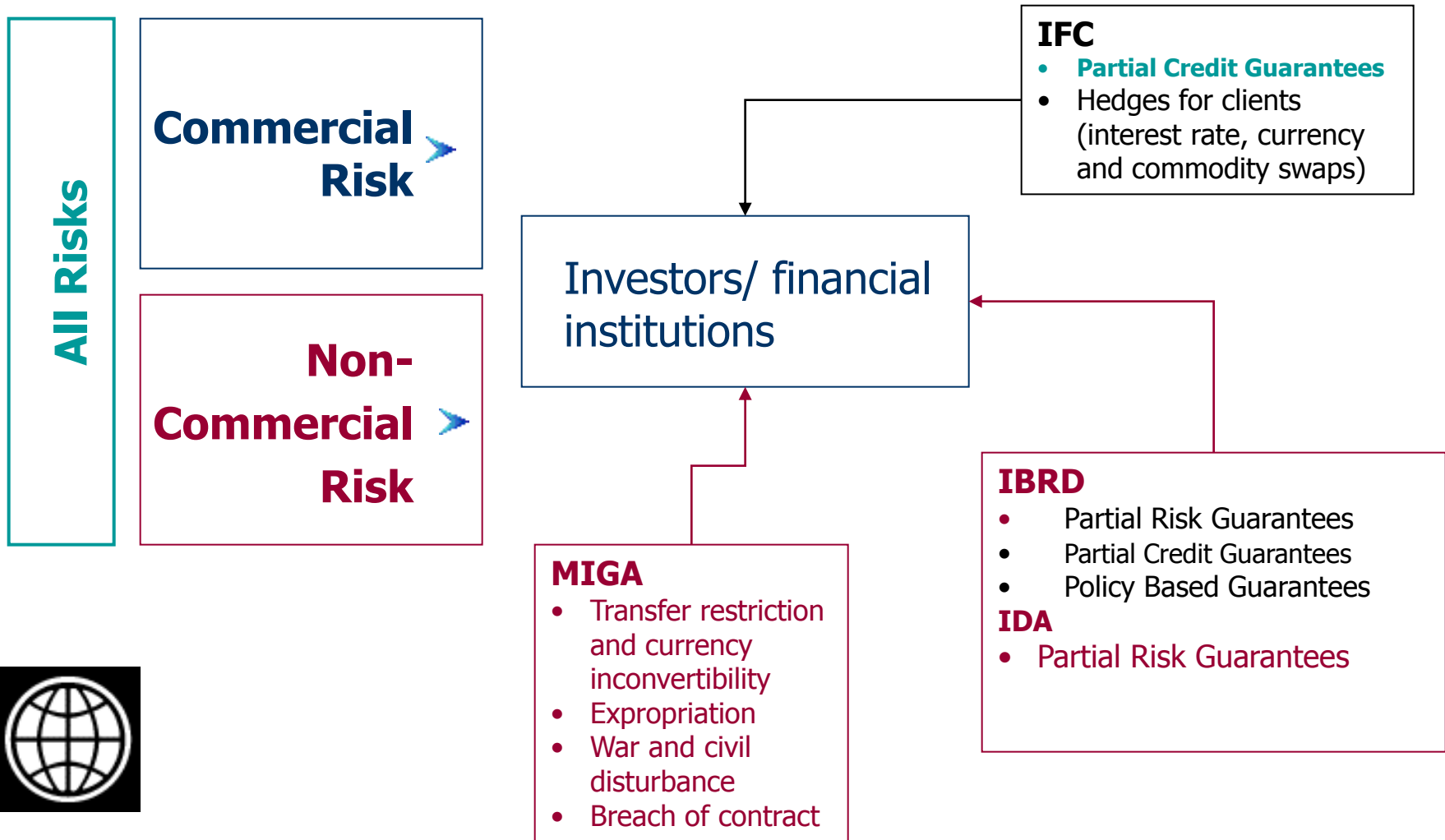
Currency Transfer Restriction & Inconvertibility

Protects against losses arising from:

- ✓ Inability to convert local currency into foreign exchange
- ✓ Inability to transfer funds
- ✓ Excessive delays in acquiring funds

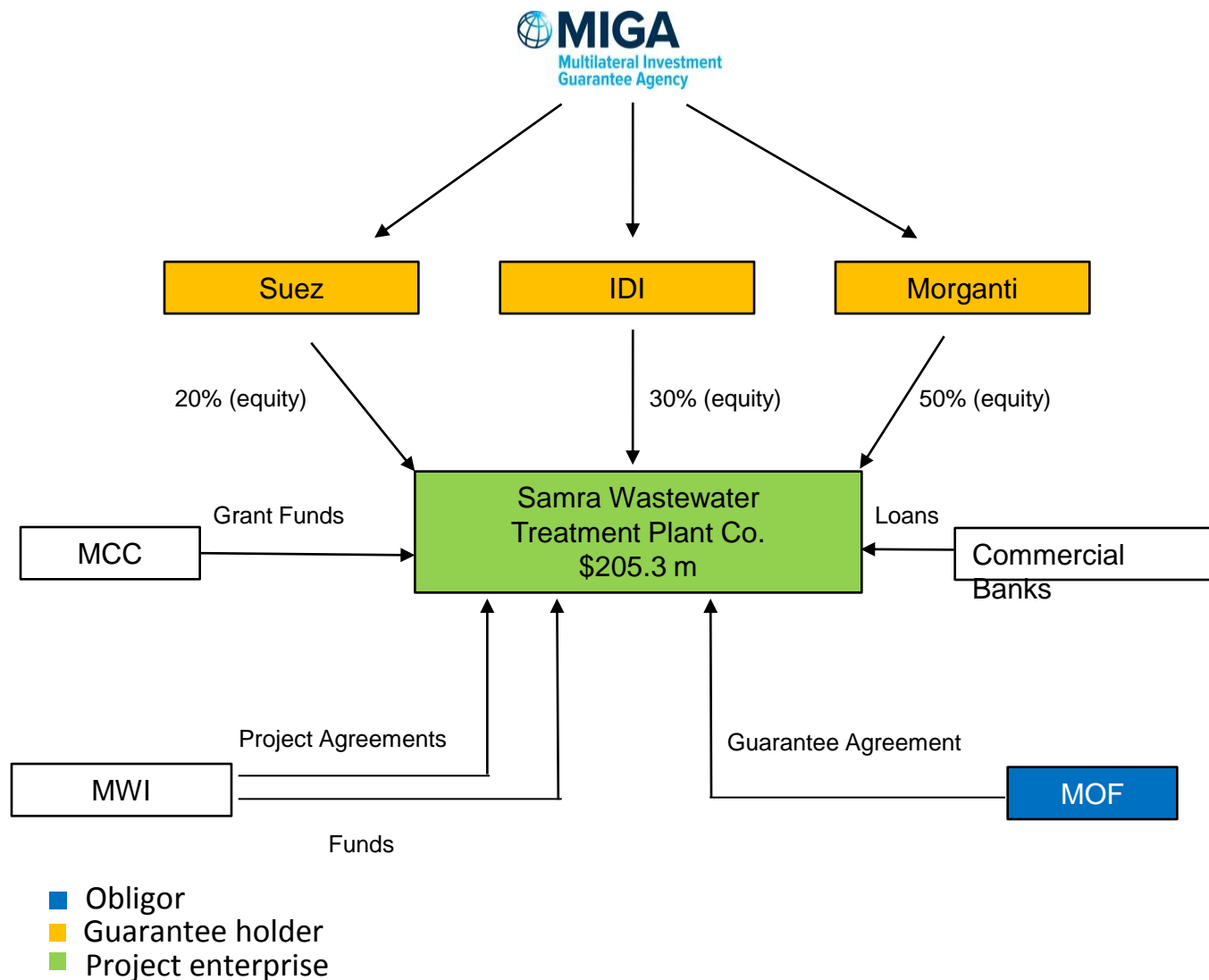
Note: Exchange risk (currency depreciation) is not covered

World Bank Group Guarantees Framework



Political Risk Insurance – Breach of Contract Cover

AS Samra Wastewater Treatment Expansion Project, Jordan



- ❖ **Project:** expansion of the existing wastewater treatment plant at AS-Samra, northeast of Amman by Samra Wastewater Treatment Plant Company, Ltd.,
- ❖ **MIGA cover**
 - Amount: \$13.1 million
 - Tenor: 20 years
 - Issued: June 2013

Source: Bertrand Marchais (2014)



Thank you

