meridiam infrastructure

INVESTING FOR THE COMMUNITY

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How to foster capital markets investment in Project Bonds?

EU consultative meeting on EU 2020 Project Bonds Initiative

11 April 2011

Agenda

I. Meridiam is a long term equity investor in greenfield infrastructure projects

II. Capital markets financing is critical to bridge the infrastructure financing gap

III. Meridiam experience in North America shows that targeted financial support and flexible tendering processes can foster capital markets investment in projects

IV. Preliminary thoughts regarding the Europe 2020 Project Bond Initiative

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Our vision

ASSETS

Need for public services infrastructure

Long term financing

LIABILITIES

Matching investors' liabilities

Long term investment

MERIDIAM INFRASTRUCTURE

A leading 25 year maturity infrastructure fund with € 1.5 billion of assets under management dedicated to the **development**, **construction** and **management** of **public services** infrastructure in OECD countries (European Union and North America)

Our strategy

MERIDIAM is a solely PPP Infrastructure Fund

Transportation sector
in urban and sub-urban areas:
Roads, Rail, Ports, Intermodal connections

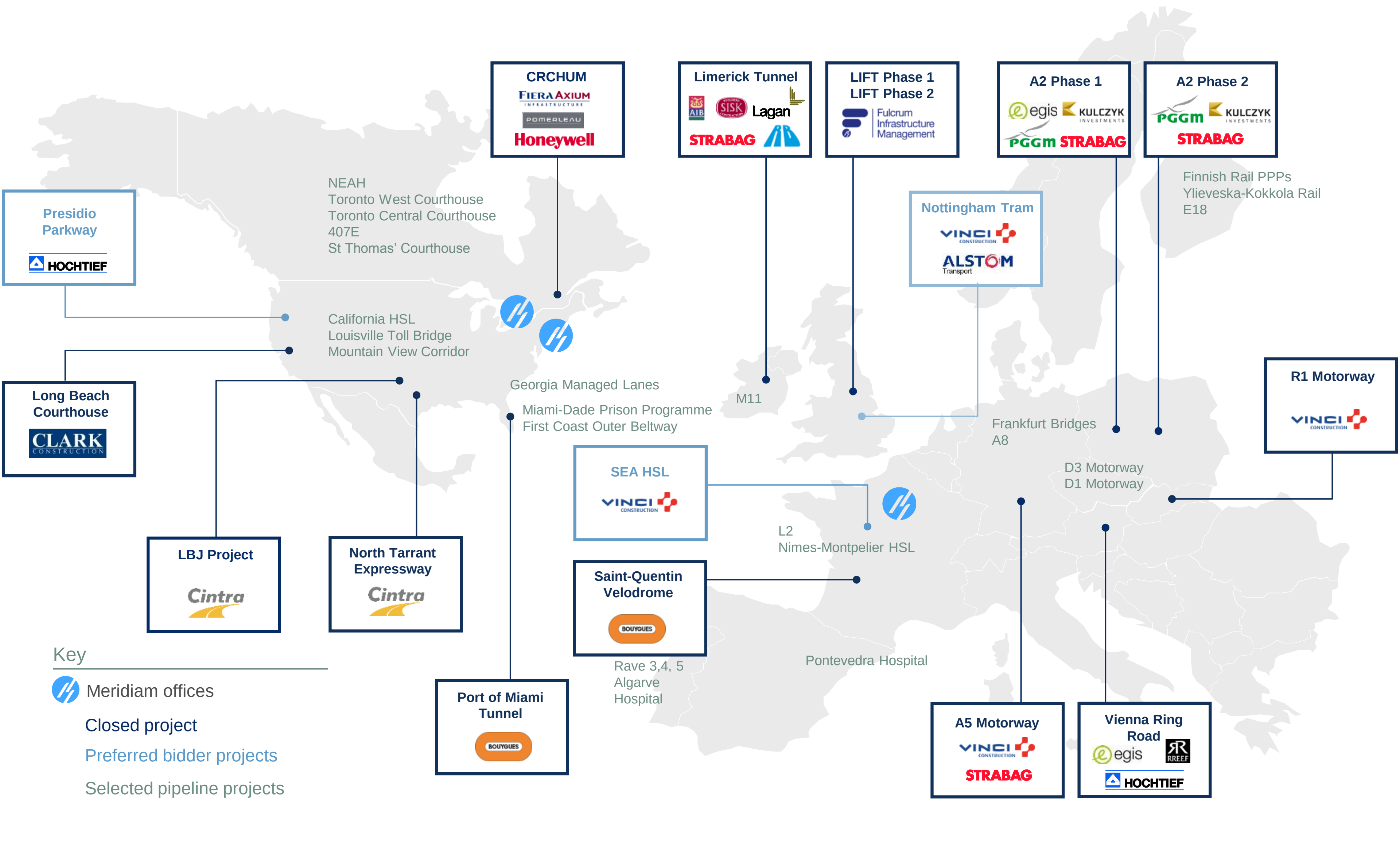
New public infrastructure needs:
Healthcare,
Education,
Environmental facilities, water and waste
Public accomodation

MERIDIAM invests equity and quasi equity in **infrastructure projects**

Mainly primary projects (Greenfield) including the construction period and does not differentiate funding between construction and operation

As an investor over the life of the project providing steady annual contracted returns for its investors, Meridiam strongly prefers **long term fixed rate debt to be** in place **for both construction and operations periods**

A leading infrastructure fund



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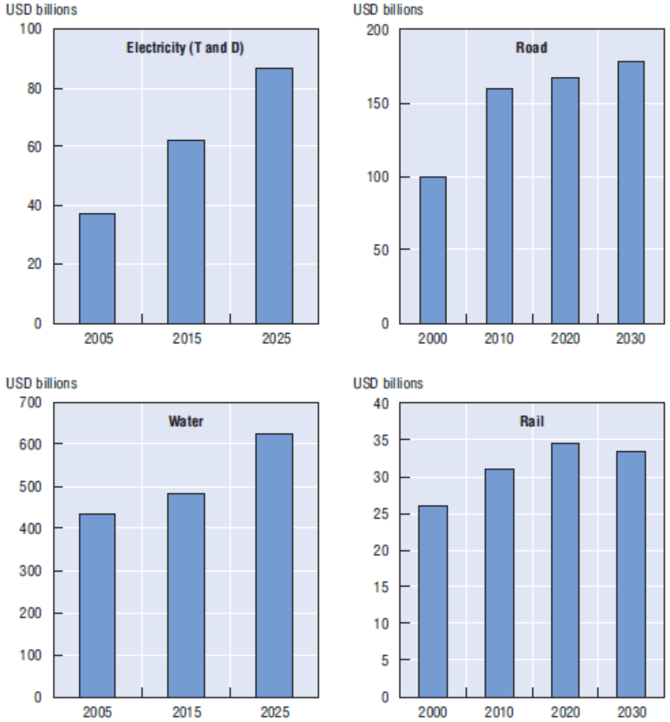
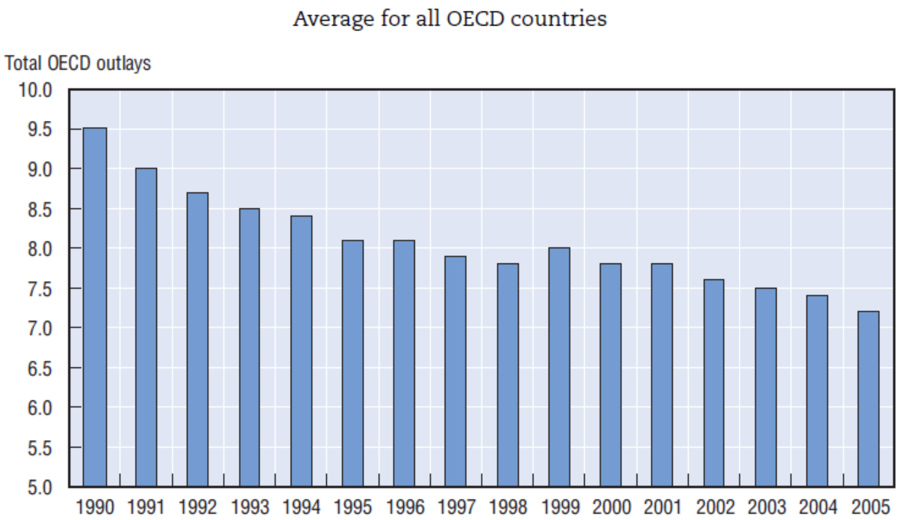
Private sector funding (equity & debt) is essential to bridge the infrastructure financial gap

Average annual infrastructure investment requirements in OECD countries



Source : OECD, 2006

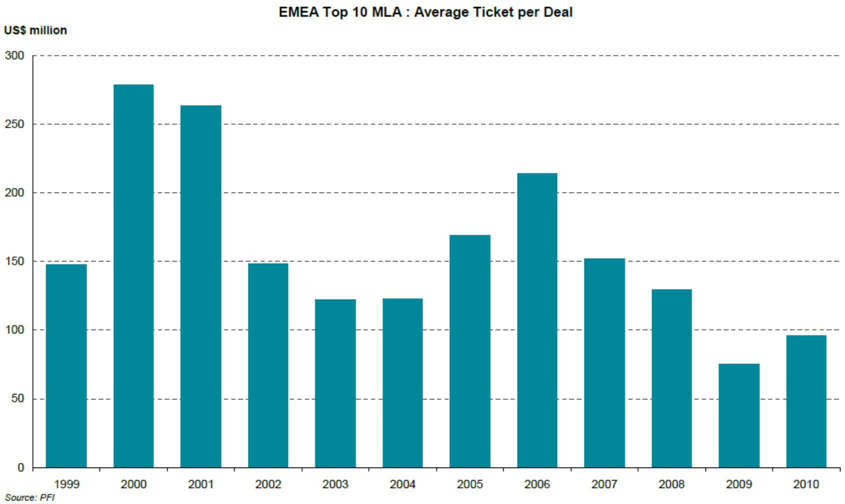
General government gross fixed capital formation (GFCF), as percentage of total government outlays, 1990-2005

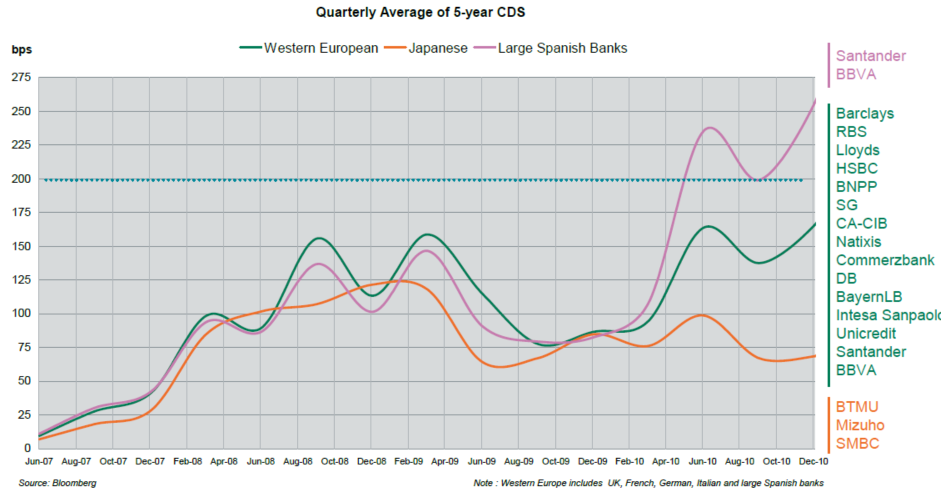


Source : OECD, 2006

To complete of the TEN-T program alone, the EC White Paper estimates that € 550 billion of funding is required until 2020

The banking sector will not be able to provide alone the amounts of debt that are required





- ‘Abundant and flexible’ long term bank loans may belong to the past after the ‘Great Financial Crisis’ and also taking into account the potential impact of the implementation of Basel III

- Identifying (again) alternative long-term debt sources is critical, both in terms of available amounts for projects and pricing conditions

Meridiam therefore fully supports the EU 2020 Project Bonds Initiative to be implemented as soon as possible

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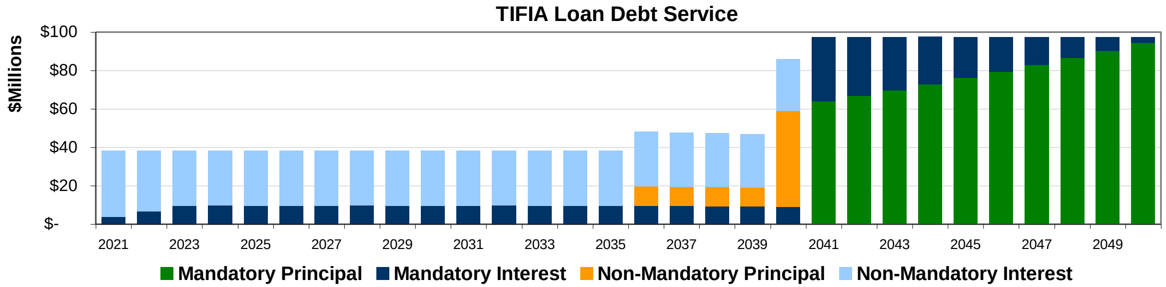
Existing US programmes facilitate the access to capital markets for infrastructure projects in the US

- Implementation of the Transportation Infrastructure Finance and Innovation Act (TIFIA) offering direct financial assistance to develop infrastructure projects
  - ✓ Secured (direct) Federal budget loan – Maximum term of 35 years from substantial completion, with repayments starting no later than 5 years after substantial completion
  - ✓ Loan guarantee
  - ✓ Standby line of credit – Contingent loan available for draws as needed for up to 10 years after substantial completion of project.



Profile of the TIFIA subordinated loan for the NTE roject

- Tax exemption for private activity bonds (PAB)
  - ✓ $15 billion in tax exempt facility bonds, again supported by the Federal budget, aiming at providing low-cost financing to projects with private involvement to increase private sector investment in U.S. transportation infrastructure
  - ✓ Low-cost financing for private projects that serve a public purpose. In present value terms, the Federal tax-exemption subsidy for PABs could represent approximately a 15–20 percent reduction in the borrowing costs of the borrowed funds

Against this background, Meridiam and its partners issued recently long-term Project Bonds

NORTH TARRANT EXPRESS MOTORWAY (Texas) **52 years**

Construction and management of 21,4 km length sections of the NTE motorway on Dallas – Fort Worth axe. Original financing by TIFIA and PABs bonds raised on the market.

- *Revenue generation: users paid tolls*
- *Total project cost: $2 billion*
- *Total PAB proceeds: $400 million (rating BBB-/Baa2, max maturity 30 years)*
- *TIFIA tranche: $650 million*
- *Public subsidy: $573 million*

IH-635 (LBJ) Managed Lanes (Texas) **52 years**

Construction and management of 20.8 km length sections of the primary circumferential roadway in Dallas within the Dallas-Forth Worth International Airport area. Original financing by TIFIA and PABs bonds raised on the market.

- *Revenue generation: users paid tolls*
- *Total project cost: $2.7 billion*
- *Total PAB proceeds: $606 million (rating BBB-/Baa3, max maturity 30 years)*
- *TIFIA tranche: $850 million*
- *Public subsidy: $499 million*

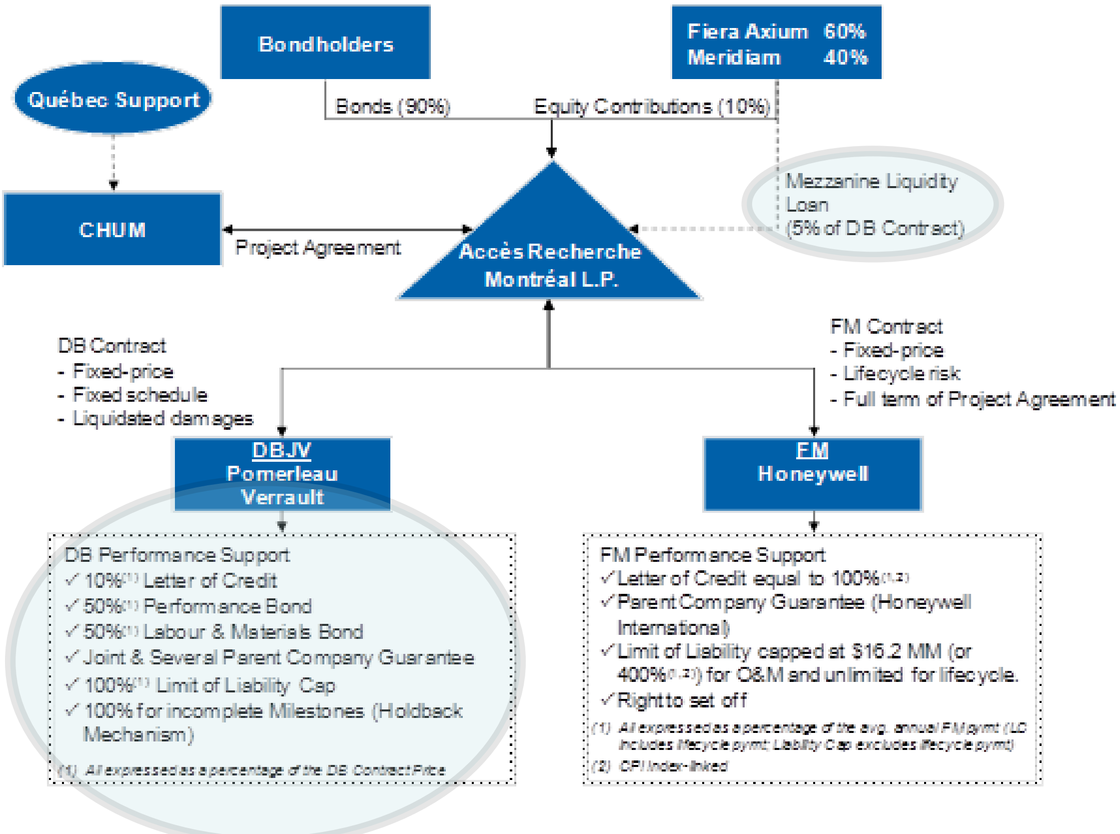
➢ In addition to the federal financial support, these bond issues were made possible by adapted procurement processes at State level

  ✓ Significant period of time (12 to 18 months) between commercial and financial close to ensure best market conditions available for capital market usage

  ✓ Protection of the private partner against any variation of risk free interest rate for 360 days after concession contract signing

Meridiam also issued Project Bonds to finance CRCHUM, a major healthcare PPP in Canada

Contractual structuring enabled to mitigate adequately the construction risk



DB : Design Build
DBJV : Design Build Joint Venture
FM : Facility Management

- Key point: rating was achieved through contracts and liability package enhancement
- A A3 rating of senior debt by Moody’s
- C$ 384 m raised through private placement (for c. C$ 44 m of equity) with a tenor superior to 32 years

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Preliminary thoughts on this Initiative

- This Initiative could clearly act as key catalyst to bridge the infrastructure funding gap
  - ✓ Critical signal to the market
  - ✓ Likely to make a significant impact on project ratings with level of support envisaged
  - ✓ Likely to foster similar initiatives from the private sector

- Some aspects may still need further development
  - ✓ The scheme is still a blueprint, which needs to be modeled and priced to be eventually validated by rating agencies and the institutional investors' community
  - ✓ The unfunded option ("debt service guarantee") raises a number of practical issues, notably for availability projects which could not bear large contingent debt
  - ✓ Will the EIB and the EC be able to deliver the required budgetary and staff resources in a timely manner?

- Key areas of focus for Meridiam
  - ✓ Need to stimulate funding for full project period from financial close to project maturity so need to allay investors concerns about funding over the construction period
  - ✓ Refinancing may be of limited interest – problems with swap breakage and market conditions
  - ✓ Controlling creditor – Meridiam preference is for an efficient straightforward funding with non conflicted and educated points of contacts for bondholders, keeping however in mind that in North America bond issues are usually made without controlling creditors.

Meridiam first suggestions to make the Initiative a success

- This Initiative should have a broad sector scope to generate a sufficient deal flow and create a new asset class of ‘EU Enhanced Project Bonds’: social PPP infrastructure should notably be also covered as well as major transport and energy projects

- Regarding the instrument itself, Meridiam considers that a blending of limited debt service guarantee and subordinated funding could be envisaged to gather the advantages of the two options

- EC and EIB may also consider offering a shorter term ‘backstop facility’ to purchase unsold Project Bonds in order to make the initial offerings successful. These could then subsequently be sold in the marketplace, providing a potential trading platform and allow liquidity

- In addition to the financial support, practical issues at project level will be key:
  - ✓ Construction risk mitigation will be key : should the provision of the EC/EIB support be linked to the provision of minimum construction/operation security packages to create market standards and strengthening the intrinsic robustness of European PPP projects?
  - ✓ Could EU institutions promote flexible tendering processing, such as the ones Meridiam experienced in North America, to make available alternative sources of funding (banks and capital markets for funding) for projects?