RBC Capital Markets

Project Bonds — How to Attract Investors?

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RBC Capital Markets®

Lessons Learnt from Canada

The Canadian PPP project market was established in the mid to late 90's but gained significant momentum in 2004/05

- There is a clear pipeline of projects which enjoy strong political support across sectors (e.g. Health, Transport, Justice)

Humber River Regional Hospital

Windsor-Essex Parkway

Durham Region Courthouse

Procurement processes are designed in such a way that allows bonds to participate

- A crisp process with tight timelines
- Standardised contractual documentation wherever possible

Projects are often rated in the A range without the need for structural enhancements

- Contractors are often robust, investment grade entities themselves
- Strong bonding support from Construction and FM contractors

Long term bank debt was never readily available in the Canadian market

- Although this lack of competition may have led to higher prices in earlier years it allowed the bond market to flourish

Early projects were challenging but Canada built a 'virtuous circle' for Project Bonds

What Challenges Must Project Bonds Overcome?

Projects can be highly complex and difficult to analyse from a credit perspective

- Investors are guided by external credit ratings but perform their own analysis as well
- Time consuming especially where specialist teams are not in place
- Greenfield projects with construction risk can be a particular challenge

Investors will not generally be prepared to offer a fixed spread in advance of a bond being launched

- This does not fit with RFP processes in some member states
- Where projects are highly geared it is difficult to push this risk back to bidders

Monitoring operational projects

- Operational projects need to have systems in place to manage the project and make decisions
- Many investors are not currently resourced to do this
- RBC has seen solutions developed to manage complex decision making processes in other sectors and countries

The key challenge is to 'break the cycle' and encourage investors to build project teams

What Do Investors Need?

Infrastructure as an asset class has a number of attractive characteristics for institutional investors

- Infrastructure projects deliver stable, long dated cash flows which can match investor liabilities
- Offer a pick-up in yield versus Government bonds
- There is a clearly defined need for large scale infrastructure investment across Europe

Many investors have a preference for assets in the A or AA category

- Long dated BBB paper is challenging given Solvency II regulations
- Some form of credit enhancement is therefore welcome if the underlying project has a lower rating

A clearly defined pipeline of projects is needed to incentivise investors to build up sector teams

- Other frequent bond issuing sectors (e.g. Utilities) benefit from having sector coverage teams
- Improved understanding of the credit and competition between investors both help to drive down pricing

Infrastructure will always need to compete with other sectors for institutional money

Build on what already works in the bond market and keep it simple where possible

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