

Financing port developments in Myanmar

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Regulatory Regime for Ports

- Ports are regulated by the Myanmar Port Authority (MPA) under:
 - Myanmar Port Authority Law 2015
 - Myanmar Port Authority Rules 2016
- MPA National Development Plan for ports
- Powers of the MPA under Myanmar Port Authority Law in respect of the development of the ports:
 - Allow local or foreign investors to operate port activities through lease agreements
 - Enter into joint ventures with local or foreign investors to operate port activities
 - Privatize ports
 - Enter into Public Private Partnerships relating to ports
- So there is clear power for the MPA to enter into Port PPPs

Foreign Investment in Ports

- 100% foreign owned investments in ports is possible
- Notification No. 15/2017: List of Restricted Investment Activity
 - Port activities are not on the prohibited list or the list requiring a joint venture
 - Port investments which require approval of the Ministry of Transport and Communication include:
 - Dry port services
 - Construction of port related infrastructure
 - Inland river port
 - Expansion of port area
 - Port services
 - Deep sea port and international port

Foreign Investment - MIC Permits

MIC Permit

Required for all "**strategic**" and "**capital intensive**" investments

MIC Endorsement

New option for investors who are not required to apply for an MIC permit, but want long term leases or tax incentives



A **strategic** investment is defined in the rules as:

- In the communications, technology, **transport** or energy infrastructure, urban development, extractive/natural resources, agricultural, urban land or media sectors
- Under a **grant** of authority from the government and the expected investment value is more than USD 20 million
- In a border conflict region by a foreign entity
- Conducted across the national border
- Conducted across the states or regions
- For agricultural purposes and relates to more than 1,000 acres
- Includes the right to occupy or use more than **100 acres** of land

A **capital intensive** investment is defined as having an expected investment value of USD 100 million

Foreign Investment - Timelines for MIC Decisions

	MIC Permit	MIC Endorsement
What is the process to apply?	Similar to the process under the old law	New stream-lined process
The MIC will decide whether the application is complete or ineligible	Within 15 business days (plus 5 days for reasons, if rejected)	Within 15 business days (plus 5 days for reasons, if rejected)
If the application is accepted, the MIC will decide to grant the permit or endorsement	Within further 60 days	Within a further 30 days
Stop-the-clock provisions whereby the timeline can be suspended (for example, the MIC requires further information)	More likely	Less likely
The proposed investor may be required to give further information	Must do so within 20 business days, although this timeframe can be extended	Must do so within 20 business days, although this timeframe can be extended

Foreign Investment - Promoted sectors

On 1st April the MIC published the list of promoted sectors in Notification 13/2017.

The following are the broad categories that are promoted:

- Agriculture and its related services
- City development activities
- Construction of roads, bridges and railways
- **Construction of sea port, river port and dry port**
- Education services
- Establishment of industrial zones
- Establishment of new urban areas
- Health Services
- Hotels and tourism
- Information technology services
- Maintenance of aircraft
- Management, operation/maintenance of airport
- Manufacturing (except manufacturing of cigarettes, liquor, beer, and other products harmful to health)
- Livestock production, breeding and production of fishery products, and its related services
- Plantation and conservation of forests
- Power generation, transmission and distribution
- Production of renewable energy
- Science, research and development business
- Supply and transport services
- Telecommunication business

All such businesses are now entitled to income tax exemption under Section 75(c) of the MIL. The extent of the exemption, however, will depend on the zone in which the investment takes place

Sources of financing for port developments

Public sector owns and operates assets		Public-Private Partnership				Private Sector owns and operates assets
<ul style="list-style-type: none"> - Utility restructuring - Corporatization - Decentralization 	<ul style="list-style-type: none"> - Civil works - Service contracts 	<ul style="list-style-type: none"> - Management and operating contracts 	<ul style="list-style-type: none"> - Leases / affermage 	<ul style="list-style-type: none"> - Concessions - BOT Projects - DBOs 	<ul style="list-style-type: none"> - Joint venture - Partial divestiture of public assets 	<ul style="list-style-type: none"> - Full divestiture
Public finance				Mix of public and private finance		All private finance

Low

Extent of Private Sector Participation

High

Sources of Private Financing

- Sources of finance include:
 - equity
 - debt
 - export credit agencies
 - bonds
- In developing economies such as Myanmar equity and debt may be raised from a mix of multilateral agencies and the private sector

Sources of financing – project financing

- The main concern of the private financier is to get their money back
- A general rule (which is not always true) is that private financiers prefer an incorporated joint venture structure
- Advantages to using “project financing” for sponsors:
 - More debt = higher equity IRR

	80% equity/20% debt	20% equity/80% debt
Value of investment	1,000,000	1,000,000
10% Return	100,000	100,000
Equity invested	800,000	200,000
Return on equity	12.5%	50%

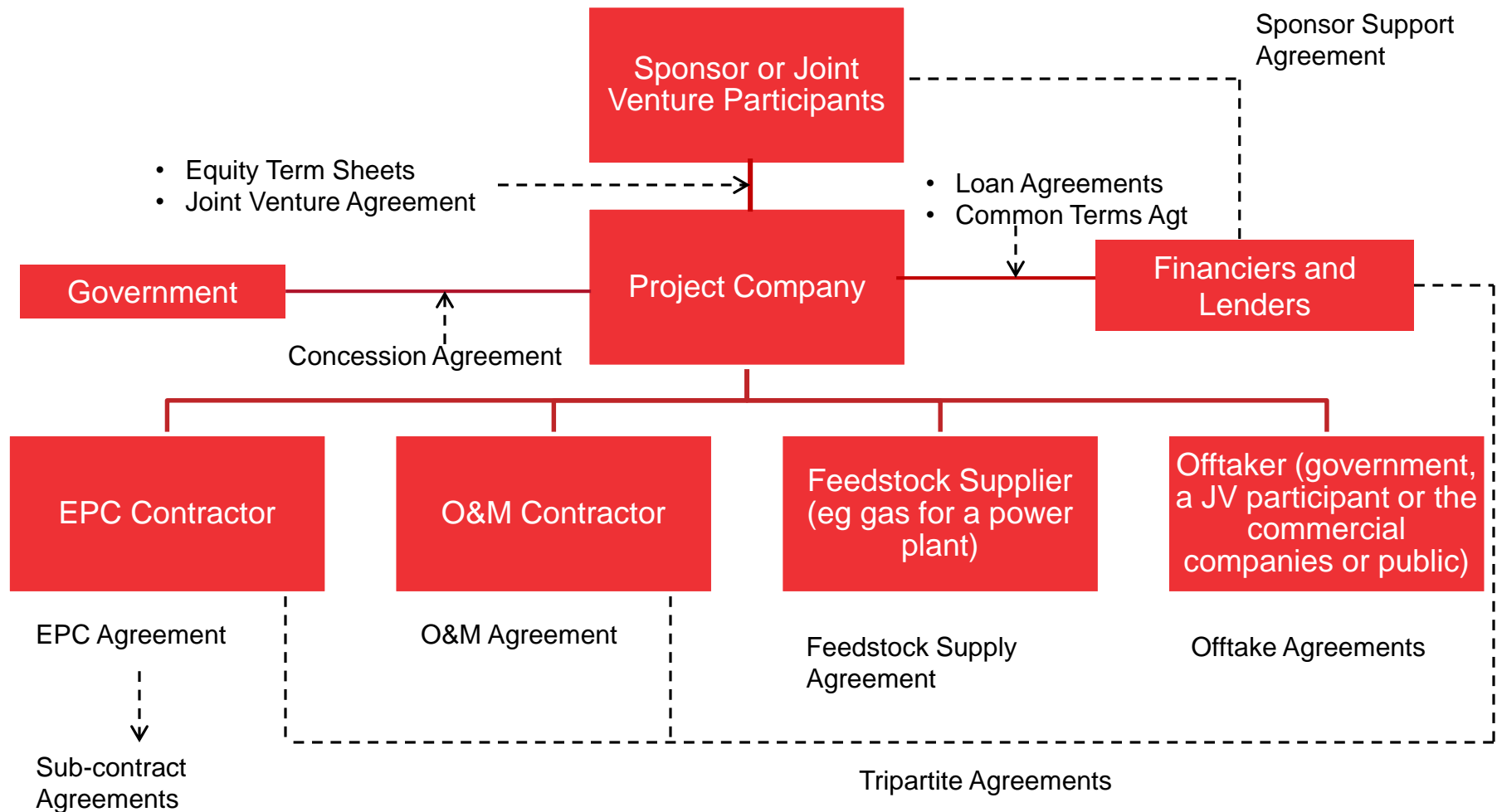
- Liabilities may need to be covered (although note sponsor support obligations are common particularly in emerging markets)
- Longer term debt better match the predictable revenues

Structuring of Port PPPs

Traditional types of PPPs:

- User pays PPP – where the private party builds or upgrade a public asset, operates it within the contract period and receives payments from users of the asset
- Availability based PPP – where private party builds or upgrade a public asset, operates it within the contract period and receives payments from Government based on the availability of the asset
- Operating Concession PPP – where the private party takes over operational control of an assets, take on the operational and maintenance risk and retain all revenue from the asset – usually a cost plus pricing approach

Structuring of PPPs - Simplified contract structure



Risks and Mitigants

Contractual structure

Issue	Risk	Mitigation Measure
Government as equity participant	<p>Sometimes being an equity participant brings risks:</p> <ul style="list-style-type: none">• Non-performance by the contractor• What happens if things go wrong and the government wants to terminate concession	<ul style="list-style-type: none">• Clearly identify roles• Clearly and specifically identify what happens if there is a breach• If there is a termination, clearly articulate what happens to the equity stake held by government
Role of project sponsors	<ul style="list-style-type: none">• Project sponsors will want to avoid any liability for a failed project• Government will generally want some responsibility on the part of private parties	<ul style="list-style-type: none">• Not full project finance• Require sponsor support through a Sponsor Support Agreement
Interactions with supply chain	<ul style="list-style-type: none">• Unclear or uncertain allocation of roles can lead to liability and disputes• Where an issue arises, can be the fault of more than 1 person in the supply chain	Clarity needed in respect of roles, responsibilities, liabilities and indemnities

Risks and Mitigants

Pre-financial close risk

Issue	Risk	Mitigation Measure
Land acquisition	<ul style="list-style-type: none">• Often major projects require land acquisition• Government and stakeholder issues need to be clearly dealt with	Project sponsor will want to ensure that, to the fullest extent possible, the concession agreement (and/or supporting lease) provides for rights to use the required land for the duration of the project life. The grant of the land should provide sufficient flexibility to allow for changes for unforeseen circumstances. Agreements must deal with rights of access during emergencies and rights of access for third parties (for example, emergency response units)
Approvals	<ul style="list-style-type: none">• Project sponsors will want government to provide support• Clearly identify T1 and T2 approvals	A list of approvals (ie licences, permits and consents) must be compiled and categorised as T1 or T2. To the extent possible, the concession agreement should address the expected timelines for approvals and remedies for delays. The EPC contractor should also be required to obtain all construction approvals (this is an example of risk allocation)
Supporting Infrastructure	<ul style="list-style-type: none">• Most projects will need to secure supporting infrastructure (ie water and power).	This will need to be addressed in the concession agreement or through agreements with infrastructure providers prior to financial close.

Risks and mitigants

Construction risk - design & construction

Issue	Risk	Mitigation Measure
Design, construction, testing, commissioning and operation	Risk will need to be allocated between the different parties for the design, construction, testing, commissioning and operation of the infrastructure	<p>Risk should be properly apportioned between the parties and passed through to customers where possible. Considerations include:</p> <ul style="list-style-type: none">• who will sign off on the design (EPC contractor or Project Co)?• what level of input will be contributed by the operator into the design• who will take construction risk (EPC Contractor / Project Co)?• who will take the risk for loss of product (operator / customer)? <p>EPC contractor should wrap completion backed by the security package. Commission test should test system under stress. Concession Agreement should include a strict definition of Practical Completion and an appropriate length of defects liability period.</p>
Fit for purpose	To reduce risk to Project Co, it should seek sign-off that the construction of the infrastructure is fit for purpose	EPC contract needs strict specifications. Defects liability period should extend for as long as possible (ie 24 months). Ongoing obligations on O&M operator to maintain standard. Proper incentives should be placed on O&M contractor to maintain infrastructure and not run down assets. Consideration should be given to extent of any sign-off by operator for input into design and operating assumptions.

Risks and mitigants

Construction risk - delay

Issue	Risk	Mitigation Measure
Delay	Delay in construction can cause significant risks to the project including substantial additional costs	<p>Liability for delay of construction usually sits with EPC contractor and be supported by a security package (LDs, bonding, parent company guarantees). Security may be limited in circumstances where delay is caused by interface with other EPC contracts. Project Co could obtain delay start up insurance, however this will be potentially limited in scope. Concession Agreement should include sunset date.</p> <p>Major delays (ie delay to sunset date in Concession Agreement) should be mitigated through negotiation on termination triggers.</p>
Force majeure (FM)	FM events could extend the project and delay operation resulting in delay of income	<p>The EPC contract should include time contingencies and require the EPC contractor to have contract works insurance. Insurance may also extend to insurance for sabotage/environmental terrorism. Any uninsurable, uninsured FM costs may be capitalised and charged to customers as a construction cost. This will require careful structuring to ensure it is bankable. There will also still be the issue for funding costs during construction.</p>
Cost-over runs	Delay and cost over runs can cause significant financial stress to a project at the time when it is not generating any revenue	<p>The EPC contract should preferably be a fixed price contract. Project Col should check whether LDs are priced into the contract and therefore what risk sits with Project Co. Otherwise, risk is mitigated by having revenue based on actual costs</p>

Risks and Mitigants

Construction risk - other

Issue	Risk	Mitigation Measure
Industrial action	Strikes or other industrial action may delay commencement of operation of the port	All parties should have a robust industrial strategy. This should be a key factor in appointing a preferred EPC contractor and any independent operators.
Change in law	Change in laws can cause additional scope and delays in construction of project and increase costs	Key contracts (ie concession agreement) should, to the extent possible, limit or deal with change in law upfront. Where this is not possible key contracts should allow for flexibility and pass through costs to customers. If this is not possible then concessionaire may want to build in an allowance for increased costs for changes in law.

Risks and Mitigants

Key financier considerations

Issue	Risk	Mitigation Measure
Completion risk	During the construction stage there is a risk that the project will not be completed on time, on budget or at all due to technical, labour, and other construction difficulties. This can create significant costs including additional loan repayments and could affect revenue streams.	Financiers may require a completion guarantee from Project Co. Project Co should ensure that a similar completion guarantee is sought from the EPC Contractor. Equity contributions by Project Co will be seen favourably by financiers as Project Co will be considered to have a significant financial interest in completion of the project. The EPC contract should be for a fixed price and operate on a turn-key basis. The EPC Contractor should be financially sound. The obligations of the EPC Contractor should be underpinned by adequate security.
Operation risk	There is a risk during operation that there will be inadequate inputs to provide a sufficient return to service any debt.	This risk will be mitigated by: <ul style="list-style-type: none">• Allowing sufficient revenue to cover any risk;• Availability payments; or• Price re-negotiations.
Technical risk	There is a risk that technical difficulties in the construction and operation of the project may create delays of prevent completion of the project.	Financiers will require that the EPC Contractor has the required skill to undertake the project. This will include sufficient skilled labour and experience. Technical risk may be mitigated by obtaining expert reports prior to lending and to withhold retention amount to be used for maintenance and defects.

Risks and Mitigants

Key financier considerations (cont.)

Issue	Risk	Mitigation Measure
Currency	<p>There is a risk that depreciation in loan currencies may increase the costs of construction where significant construction items are sourced offshore. There is also a risk that depreciation in the revenue currencies may cause a cash-flow shortage during operation.</p>	<p>Financiers will seek to mitigate risk by requiring that the currencies of the revenues of the concession to be aligned with the currencies of debt and major procurement contracts. If this is not possible then financier will seek to have the concessionaire enter into hedging agreements to reduce this risk.</p>
Regulatory	<p>There is a risk that government licenses and approvals required to construct or operate the project may not be issued. The project may also be subject to new regulation, taxes or other conditions on licences that may affect the operation of the project.</p>	<p>Financiers will require that any funding agreement includes a condition precedent that Project Co obtain all required approvals and satisfy all conditions to construct and operate the project.</p>

Risks and Mitigants

Key financier considerations (cont.)

Issue	Risk	Mitigation Measure
Political/ sovereign issues	Sovereign risks includes nationalisation of assets, increased taxes/royalties, strikes, sanctions and vandalism.	Financiers will seek to minimise exposure to sovereign risk by implementing the following steps: <ul style="list-style-type: none">• investment protection agreements (ie IPPA)• political risk insurance (traditionally this will come from government agencies)• diversifying investment risk between several countries' financiers, ECAs, development banks
FM	A FM event can affect the operation of the project and the proceeds used to service repayment of debt	Financiers will require that proper due diligence is conducted during pre-feasibility stage to understand the likelihood of FM. Insurance should be obtained for FM to the extent possible (which includes the financier as the insured). Financiers will require that risk is properly allocated between the parties to limit project sponsor risk

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