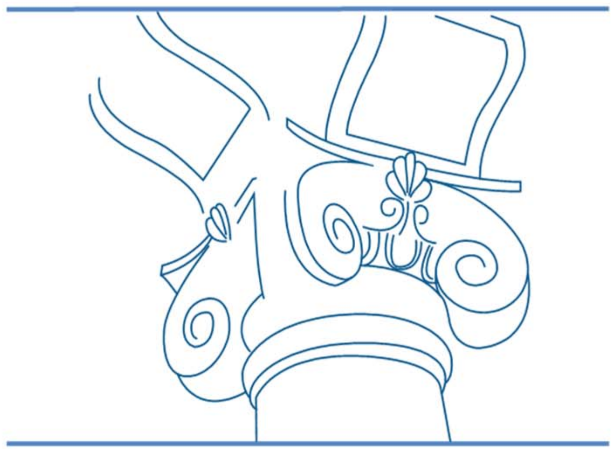

The Financing of EU Strategic Infrastructure

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THE LOGISTICS IMPACT: PORT, RAIL, AND ROAD DEVELOPMENT TO SPUR GROWTH

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Investment Climate for EU Infrastructures (i)

Market overview

- ✓ **Huge need for capital:** The total funding required for development/upgrade of infrastructure in the EU to match demand has been estimated at over €1.5 trillion from 2010-2030, of which the **TEN-T network alone requires approximately €550bn**.

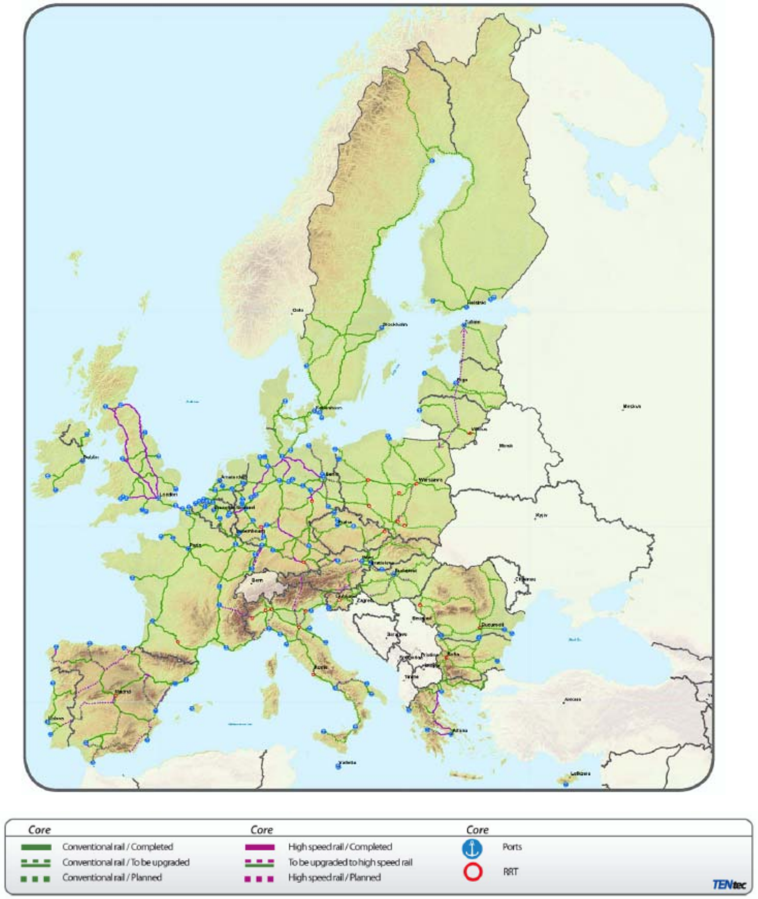
- ✓ **Decline in deal volume: 84 PPP transactions reached financial close in 2011**, which includes both project finance and non-project finance deals in Europe. This is significantly below the **112 and 118 transactions closed in 2010 and 2009**, respectively. Of the 84 PPP transactions that achieved financial close in 2011, **only 12 transactions (of which 6 were TEN-T) reached financial close in the transport sector (compared to 24 in 2010).**

- ✓ **Delays/cancellation of projects:** Constraints on government budgets have led to delays in awarding concessions and many projects have been put on hold. In other cases, for example Poland, changes to the Eurostat treatment of public debt have caused significant delays and uncertainties in the delivery of the PPP transport pipeline. In Germany and more recently France, there has been some political opposition to the continued use of PPP as the preferred model to deliver transport projects.

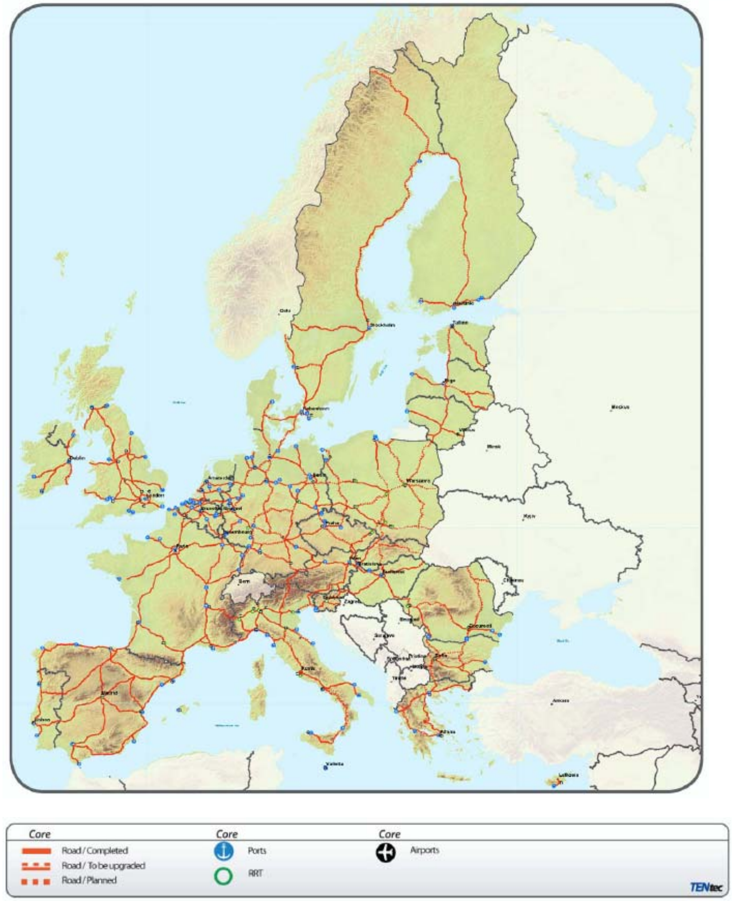
- ✓ **Possible expansion of TEN-T list of projects:** The EU Commission (DG Move) has proposed revised TEN-T guidelines that once approved by the Council and European Parliament –expected in 2013- would increase the number of eligible TEN T projects.

TEN-T – Core Network

Core Network:
Railways (freight), ports and rail-road terminals (RRT)
EU Member States

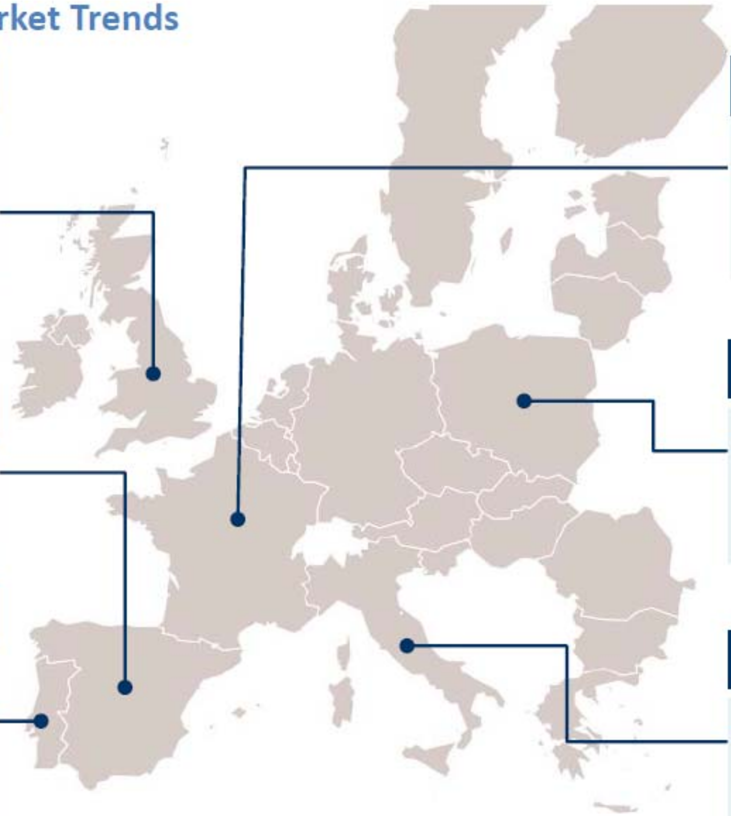


Core Network:
Roads, ports, rail-road terminals (RRT) and airports
EU Member States



Investment Climate for EU Infrastructures (ii)

Transport Infrastructure Market Trends



UK

Set up of a GBP 40bn Guarantee Scheme but delivery model still unclear.

Spain

FC of recently awarded PPPs have been delayed.

Portugal

Government has started renegotiations of all major PPPs. Availability payments will be cut by 30%.

France

Many projects have been delayed (e.g. Canal Seine Nord).

Poland

Several airport expansion opportunities coming to market.

Italy

Government has improved PPP & project bond regulation.

Across Europe

PPP – Activity traditionally concentrated in France, Spain, Portugal and the UK. Level of deals closed reached a decade low in H1 2012. Changes to Eurostat treatment of public debt have caused delays and uncertainties in delivery of PPPs in some member states.

Source: *European PPP Expertise Center, Infrastructure Journal, Linklaters*

Key Challenges for EU Infrastructures (i)

- ✓ **Tough financing conditions:** Due to the Eurozone credit crisis, lending conditions have become less favorable with banks charging higher margins, imposing shorter tenors and stricter security, coverage, cash sweep and guarantee requirements. The capacity of the banking market is also becoming an issue that limits the implementation of new projects. **EU Project Bond initiative** should help reverse this negative trend, providing alternative source of debt through capital markets.

- ✓ **Deteriorating credit rating of member states (or sub states):** In two years the long term credit rating of several member states has been significantly downgraded, leading to increased counterparty risk for non-user paid PPPs.

- ✓ **Support of member states:** All transport projects need subsidies or some form of financial and political support from the governments and public procuring bodies for successful implementation. Budgetary austerity and other related political issues create uncertainties on a number of projects in our pipeline.

- ✓ **Focus on efficiency rather than greenfield projects:** A related point is that in a number of countries (e.g Germany and the UK) the focus is more on **improving existing assets than building new ones which has an impact on the greenfield/brownfield mix of projects and leads to rolling stock projects for instance as opposed to new high speed lines.**

Key Challenges for EU Infrastructures (ii)

- ✓ **Fall in traffic:** Continuing economic weakness, public opposition to tolls and austerity measures are adversely affecting traffic levels across the sector. **Traffic volumes, especially in freight transportation being closely correlated with economic activity, have suffered**.

- ✓ **Estimating future traffic levels:** The estimation of traffic is complex. GDP growth, particularly in countries with uncertain GDP growth, is less straightforward. Shifts from one mode of transportation to another are difficult to predict. These has led to significant forecasting failures in the past. Underperformance versus forecast and consequently reduced revenue, has highlighted the risk of such project structures specifically designed to pass demand risk to the private sector. Investors, bondholders and lenders have now become very wary of such projects.

- ✓ **Competition:** The difficulties in the financial markets have considerably reduced the number of viable investment opportunities in projects which have an **acceptable risk/reward profile**. As a consequence, **infrastructure investors often focus on the same projects**, in countries maintaining acceptable credit ratings and offering plain vanilla type project structures, e.g. road projects in the Netherlands, thus creating a highly competitive environment and potentially leading **to low return expectations for investors**, if not being left out altogether.

Key Challenges for EU Infrastructures (iii)

- ✓ **Tighter credit conditions**: Loan conditions are less favorable in terms of costs, tenor, security and guarantee requirements. The **disappearance of monoline insurers**, which guaranteed the repayment of the project debt through their AAA ratings, has contributed in **limiting the ability of sponsors to secure funding**.

- ✓ **Shorter tenor:** The average tenor of senior debt financing exceeded 20 years in 2011, compared to 2010, in which half of the PPP transactions had debt tenors in excess of 25 years. In 2011 only 24% of transactions exceeded the 25-year mark of which Germany and France accounted for 80% of transactions with loan tenors in excess of 27 years.

- ✓ **High margins & club deals:** As credit has became less available, more lenders are required for each contract, implying a drastic reduction of the competition intensity between potential lenders at the detriment to the sponsor. Even if there is no collusion amongst banks, **a club deal contributes to increase the borrowing costs**, just because the interest margin is set by the marginal bank. The average loan margin was around 230 bps for the construction phase and around 270 bps approaching maturity.

- ✓ **Negative sector outlook of rating agencies**: In reports published in June 2012, rating agencies have forecasted a negative outlook **for Europe´s transport infrastructure due to the economic uncertainty that persists in Eurozone**.

EU Actions and Iniziative to Foster Investments

- ✓ **The Connecting Europe Facility - Features:** in the next financial framework for the period 2014-2020, the European Commission decided to propose a new integrated instrument for investing in EU infrastructure priorities in Transport, Energy and Telecommunications: the "Connecting Europe Facility" (CEF)

CEF	€40 billion
Energy	€9.1 billion
Transport	€21.7 billion
Telecommunications/Digital	€9.2 billion
Amounts ring fenced in the Cohesion Fund for transport Infrastructures	€10 billion
Total	**€50 billion**

- ✓ **The CEF is designed to attract and guarantee private sector** involvement and **will invest €31.7 billion to upgrade Europe's transport infrastructure**, build cross-border missing links, remove bottlenecks and make the network smarter.

- ✓ **But in the Conclusions of 7/8th February 2013 meeting, the European Council decided that the financial envelope for the implementation of the Connecting Europe Facility for the period 2014 to 2020 will be €29.299 million, of which € 23.174 million for transport sector.**

Project Bonds Initiative EU

- ✓ The financial crisis**, loss of monoline-wrapped capital issues** that were the markets mainstay, **Basel 2 and 3** have put pressure on the banks balance sheets and lending capacity.
- ✓ **The Project Bond Initiative has two objectives**: to **revive project bond markets** and to **help the promoters of individual infrastructure projects to attract long-term private sector debt financing**.
- ✓ Similar to the **RSFF** (Sharing risk in research, development & innovation) and **LGTT** (Guarantees for transport infrastructure cash-flow) instruments, the **EU budget would be used to provide capital contributions to the EIB in order to cover a portion of the risk the EIB is taking when it finances eligible projects**.
- ✓ The Project Bonds will help in improving the risk profile of projects for commercial banks, while allowing EIB to lever its available capital. **Project Bonds will be issued at project level and create an opportunity for projects to re-access capital market finance.**

EU Initiatives to improve the TEN-T

- ✓ In parallel with the CEF, the Commission proposed revised **guidelines** for the development of a trans-European transport network comprising a dual-layer structure, a comprehensive network upon which a **core network** is established, the latter including parts of the network which are of the **highest strategic importance to the EU and its Member States.**

- ✓ The **new EU infrastructure policy aims at creating a real network and no longer focuses on isolated projects**. The new regulation aims to focus spending on a smaller number of cross-border projects where real EU added value can be realized.

- ✓ The guidelines set common requirements for the TEN-T infrastructure, with tougher requirements for the core network, to ensure fluent transport operations throughout the network. The implementation of the core network will be facilitated using a **corridor approach. Ten corridors will provide the basis for the co-ordinated development of infrastructure within the core network to bring together the Member States concerned**, as well as the relevant stakeholders, for example infrastructure managers and users.

- ✓ The Commission estimates the cost of implementing the **first financing phase for the core network for at €250 bn**. The core network **is to be completed by 2030**. 80% of the CEF's €31.7bn will be used to support core network projects priority projects along the 10 implementing corridors, while the remaining funding can be made available for *ad hoc* projects, including for projects on the comprehensive network.

What could / *should* Europe do?

- A European policy for promoting investment for the EU's growth and competitiveness must act on some new fronts:

  1. The establishment of a **regulatory framework** less penalizing LTI in infrastructures and more attractive to private investors (Basel III-CRD IV, Solvency II, IAS, etc.)
  2. The development of **new sources of public funds** for LTI
  3. The creation of **innovative financial and risk mitigation instruments** (building on the experience of the EU the Project Bond Initiative and of the Marguerite, InfraMed, GIF, SMEG, RSFF, and EEEF Funds)
  4. The introduction of **tax incentives** for private investment in infrastructure
  5. An **unconventional measure by the ECB** to counter the liquidity crunch affecting LTI (with the introduction of a Very Long Term Re-financing Facility - ***VLTROs***).
  6. The introduction of some form of **Golden Rule**, now to be limited to national co-financing of infrastructure projects financed by the EU or by the EIB.
  7. And finally, the financing of large EU investment by issuing **Eurobond for Growth**

In the implementation of all these initiatives **Public EU and National Development and Investment Banks may play a crucial role as "policy oriented" European long term investors**

LT Equity Funds: Marguerite

Mandate

- ✓ The Marguerite Fund is a **long term equity** fund targeting primarily **greenfield** transport & energy infrastructure created by the EU together with some of the European largest long term development banks

Investors

- ✓ The Marguerite Fund has **total commitments of EUR 710m**, with EUR 100m from each Core Sponsor, EUR 80m from the European Commission, and EUR 30m from other investors

Core Sponsors	Caisse desDépôts	cdp S.p.A.	European Investment Bank
	kfw BANKENGRUPPE	ICO Instituto de Crédito Oficial	PKO BANK POLSKI
Other Investors		Caixa Geral de Depositos	BOV Bank of Valletta

LT Equity Funds: Marguerite

✓ The Marguerite Fund targets **Equity tickets of EUR 20-100m**

GREENFIELD INVESTOR	✓ Ability to invest pre-construction or during construction ✓ Ability to acquire operating assets with significant new capex requirements or pipeline ✓ No immediate cash yield requirements ✓ Ability to invest in quasi-equity (mezzanine, sub debt, etc.)
LONG TERM INVESTOR	✓ 10 year plus investment horizon
INVESTMENT PARTNER	✓ No requirement to take Control ✓ Preference of 50% or less shareholding: significant minority
ACTIVE INVESTOR	✓ Assistance in deal structuring / debt raising ✓ Active role post investment (board representation)

Marguerite is an attractive partner for industrial / strategic players and other long-term investors

Marguerite and a TEN-T Motorway Project (Spain)

Project

- ✓ 146 km long shadow-toll section of the dual-carriageway “Santo Tomè del Puerto – Burgos” section of A-1 connecting Madrid to North of Spain
- ✓ Brownfield TEN-T
- ✓ Total construction costs of € 227 mln
- ✓ Sacyr acted as EPC contractor
- ✓ Operated by Sacyr’s service subsidiary Valoriza

Marguerite transaction

- ✓ In 2011, acquisition from Sacyr Vallehermoso of 45% equity stake in concessionaire Autovìa Arlanzòn
- ✓ Other shareholders: Sacyr, Valoriza
- ✓ Backed by Marguerite intervention, total equity committed to the project reached € 100 mln, thus
  - ✓ improving debt sustainability
  - ✓ assuring bancability of the project
- ✓ Debt providers: EIB, KfW, Lloyds

Partners:

Valoriza Sacyr

InfraMed and the Port of Iskenderun (Turkey)

Project

- ✓ Phase I capex programme designed to remodel the existing cargo operations into one of the largest container ports in East Mediterranean
- ✓ 36-year concession agreement
- ✓ Total construction costs of $ 754 mln
- ✓ 85% of Turkey's foreign trade is conducted by sea
- ✓ The port of Iskenderun is well-positioned: nearby the Eastern Anatolian hinterland, Turkey's 4th largest economic area (largest steelworks, oil & gas terminals, refineries, shipyards)

InfraMed transaction

- ✓ In 2012, acquisition of a 20% equity stake in concessionaire
- ✓ InfraMed's participation provided additional comfort to the lending group in order to obtain the necessary internal approvals ad to reach financial close in the midst of the Eurozone sovereign debt crisis
- ✓ InfraMed's presence in the deal was considered as a credit enhancement by the MLAs' credit committee