HSBC – BRT team
October 2012

Suggested structures for financing South African Cities' BRTs

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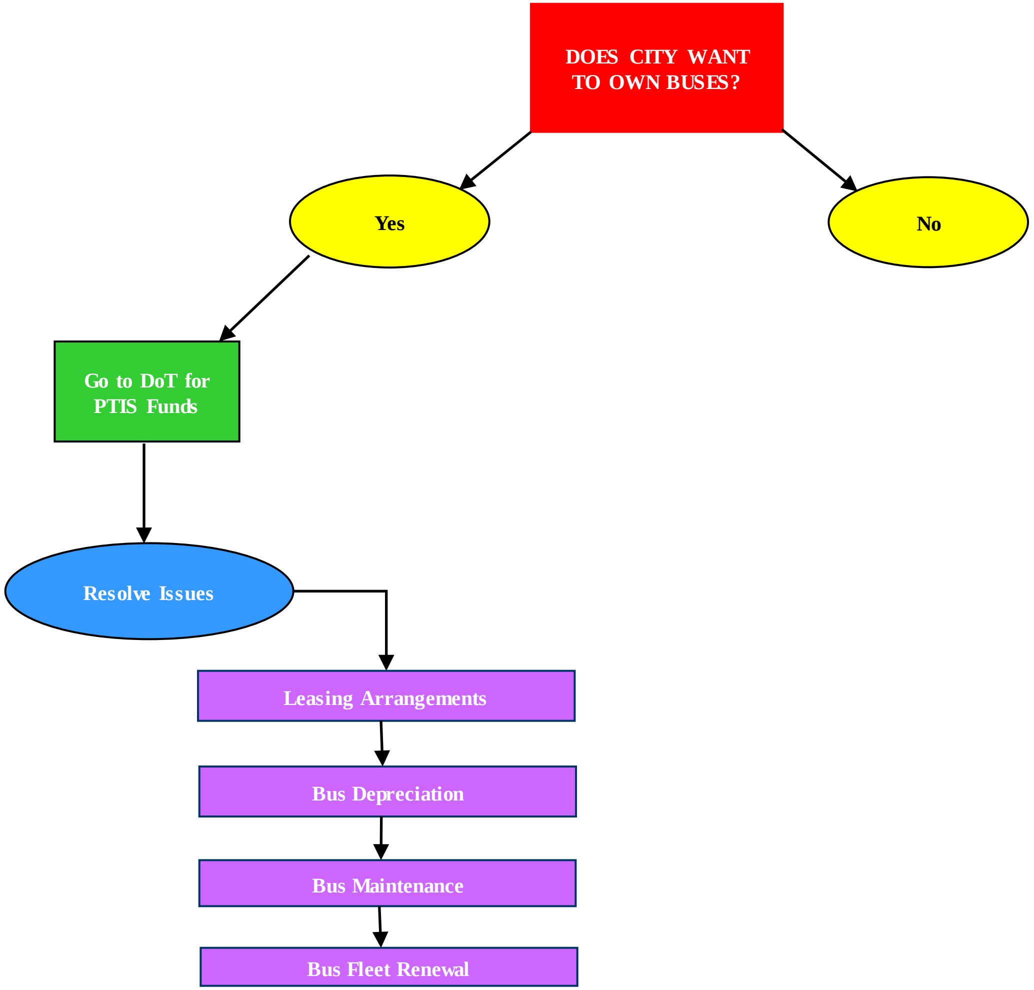
Does your City want to own its Buses?



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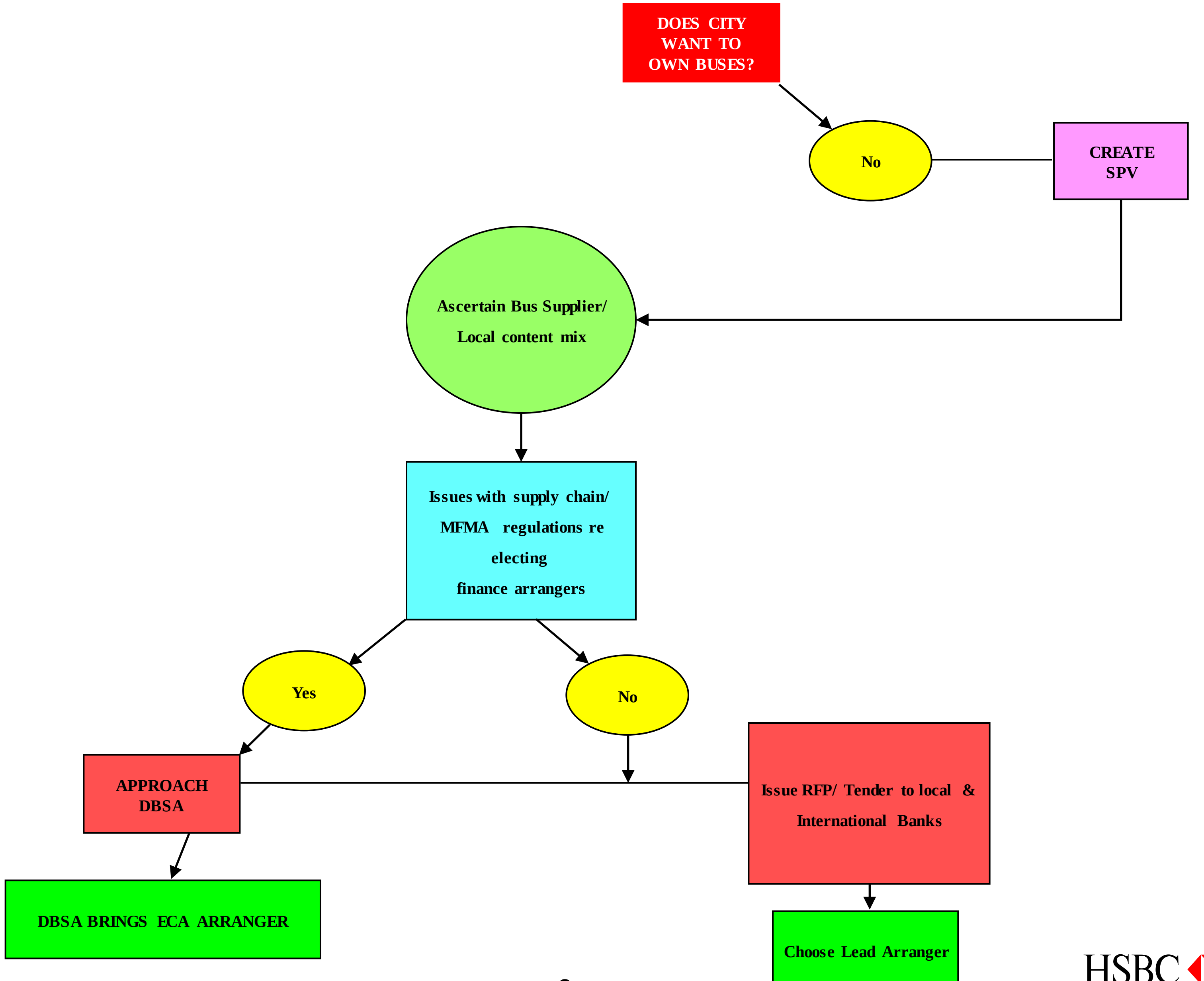

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If you want to engage financiers - what does your project require?

- Financing for:
  - BRT Infrastructure?
  - Depots/workshops for Operators?
  - Buses?
- Use of the Private Sector as borrower?
- Risk workshops to design out potential issues?
- Assistance in writing tenders and concession documents?
- Help to turn existing operators into BRT operators?
- Investor Roadshows?

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What financiers need to know Cities should also be thinking of…

- Is the Project potentially profitable? Who will control fare collection and what is the level of support/protection from Government/City
- Is there Government support?
- Are multiple Government or City Agencies involved?
  - Coordination can be an issue
- How protective is PPP/concession contract law for *lenders' interests*?
- Can risks be assessed/mitigated?
  - Traffic / technical / legal /environmental due diligence
- Is financing available?
  - Reasonable project size? – Should be manageable given onshore and offshore liquidity/appetite constraints but large enough to be economically feasible

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Cities should test their thinking with their financiers at an early stage

- What do they want delivered
- Will the project be potentially profitable?
- Is there anything similar-tested/failed?
- Will there be competition between service providers?
- Risk of “adventurers”
- Can they regain control of transport from the current operators in order to go for a BRT?
- Can demand for services in the future be reasonably predicted
- Do the private sector parties they wish to work with have the expertise to deliver

Know your customer (KYC) — **Legal Framework for BRT/Concession** — **Equator Principles / Environmental Impact Analysis**

General Risks

Political Risks

- “White Elephant Risk”
- Sources of Funding Assured?
- Political Will to Make Change?
- Strength of vested interests? Who wants the Project to fail?
- Timeframe?
- Project being bid in stages?
- Ability of Government to withdraw/change the rules?

Operator Performance Risk

- Experienced BRT Operator involved?
- Pirate Buses
- Workforce?
- Culture?
- Plans for Removal / Distribution of “Old” Buses

Technology Risk

- New technology?
- Proven?
- Working in similar conditions?
- Guarantee of operational costs/ Spare Parts costs and availability?
- Bus life?

Collection Risk/ Demand Risk

Operators

- Robust cashflows looking at worst case scenario?
- Capital Base?
- Security Package built into bid/concession documents?
  - Cash reserve?
  - Ridership Fee?
  - Inflation/Fuel / FX variations covered?

Collection

- Closed Collection Points / Closed Bus Stops?
- Speed of loading passengers?
- Smart Cards or cash?

Ticket Price

- Variable ticket price
- Political Acceptability
- Public Reaction

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BRT – Structuring Considerations

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What previous project structures can you borrow from?

Transmilenio

- Trust Bank funds old bus destruction
- Old operators “paid” to stay off streets
- Future income promised

Transantiago

- Infrastructure built out gradually
- Minimum income guaranteed to attract operators in
- Some routes reserved for old operators

Rea Vaya

- SPC operator created to incentivate taxi operators to join system
- 3 separate elements to operator income
- City undertakes to cover financing costs for first refusal on buses

Panama City

- “Open book” on all project costs by Operator
- Government funded “cushion” deposit to obtain Sovereign risk rating

Manaus

- Major fare increases in return for new buses
- Farebox part funded by local industry
- Compensation law provides additional protection

What BRT Operator Payment Structures have managed to attract financing from the private sector?

- **Transantiago, Chile**

  Payment per passenger transported *but*

  Guaranteed minimum revenue, payments per km and per place offered, income increased in line with costs

- **Rea Vaya, South Africa**

  Payment per km *but*

  Undertaking to always cover financial and operating costs

- **Metrobus, Panama**

  Payment per passenger transported *but*

  Monopoly operator, income increased in line with costs, protection from competition from Metro

What are the typical sources of financing for BRTs and Collection Systems, how do you access them, what are their advantages and disadvantages

The largest sources of funding for BRTs are Central Government funds and Export Credit Agencies

- Central government or City funding
- Multilaterals and DFI's – World Bank, IFC, ADB, NIB, DBSA

  Which can apply?
- Commercial Banks

  Risk profile? Liquidity constraints? Hurdle returns?
- Concessionaire Equity/commercial financing
- Export Credit Agencies

  Direct loans, Buyer's credit?

But what about funding infrastructure?

Can rights of way be obtained?

Is the developer responsible for road/slum clearance?

What if the project does not proceed after the concrete has been poured so there is no source of revenue?

Is the infrastructure in the right place to attract investors?

Is the infrastructure a key nodal point for the City/transfer point for other transport modes?

Can other development rights be added to provide revenue (shopping centres/hospitals)?

Can the City sign a long term take or pay contract for using the corridor?

Can an overseas contractor be used to attract concessionary funding?

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What are Export Credit Agencies ("ECAs") and why have they been key for BRT bus financings

ECAs cooperate with commercial banks to provide attractive financing solutions to importers of equipment

ECA financing is very common for BRT projects

- ECAs work with commercial banks, such as HSBC.
- The Banks act as arrangers/lenders under the ECA loans (not the ECAs themselves) and draw up the financing structures and documentation
- ECAs charge an insurance premium/"finance charge" and provide a guarantee to lenders. Most of the finance charge can be financed within the ECA supported loan.
- ECA financing is commonly used for BRT projects to finance imports of buses and equipment:
  - **Rea Vaya – US$ 43m Brazilian ECA loan**
  - **Transantiago – US$ 508m in Swedish and Brazilian ECA loans**
  - **Panama City – US$ 197m Swedish ECA loan**
  - **Saudi Haj buses – US$150m Shariah Financing**
- As they have a role to support exports ECAs have more appetite for the risks involved in BRT projects than commercial banks and can be used to offer loans with extended tenors – up to 10 years.

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Case Study: What did HSBC do in Johannesburg?

- Advised the City on potential risks, and ran risk workshops and project reviews for the Mayoral committee
- Arranged a roadshow to potential external sources of financing
- Drew up a Project Information Memorandum and helped draft the operator concession document
- Created the SPC that became the borrower and interim operator
- Provided payment guarantees to bus supplier
- Liaised with the National Treasury and National Department of Transport
- Drew up loan and security documentation
- Set up the security structure
- Provided funding for working capital and pre-funded the Debt Service Reserve Account for the SPC

Case Study: What were the key benefits of the Rea Vaya financing?

- The BNDES fixed interest rate is 3.2% - which was 2% less than the interest rate originally expected (a saving of almost USD5m of interest costs over the life of the loan)
- The City of Johannesburg (COJ) acts neither as the borrower nor the guarantor of the Bus Operator Company financing
- Rea Vaya was the first ever BNDES financing in South Africa
- The 11 year financing was priced below South Africa's Sovereign USD and Euro bonds
- Clidet had no shareholders and no equity and no guarantors yet successfully raised USD50m of BNDES and HSBC South Africa financing

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Case Study: What didn't the City of Johannesburg like about the financing?

- They didn't like being the Guinea Pig

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What didn't the City of Johannesburg like about the BNDES financing?

- The finalisation of the agreements took longer than anticipated. Some of the reasons for the delay included:
- Language problems: In February 2010 changes in BNDES policies required the loan agreement to be translated into Portuguese, and all documents and comments have had to be translated from English to Portuguese and vice versa
- Unfamiliarity with the South African legal system: this was the first deal for the BNDES in South Africa, and many questions arose out of the BNDES' need to understand the South African legal system.
- The complexity of the deal and the requirement that COJ act in the best interest of the BOC and the COJ
- Appointment of a new BNDES underwriter in March 2010 resulted in almost all documents changing
- Many players: The COJ was not dealing directly with the BNDES but through the transaction advisors. In addition to the BNDES, the transaction was also managed on the Brazilian side through the BNDES' lawyers and they needed to engage a number of other Brazilian governmental agencies.

Why is Export Credit Agency (ECA) financing potentially very valuable for your BRT project?

- Low Cost
- Does not utilise local South African risk appetite (keeping funding lines open for Cities and Bus Operating Companies)
- 10 year repayment terms allow financing costs to be spread across the life of the concession
- Grace periods allow the Bus Operator or City to start to generate income from the Project before it has to make the first repayments
- ECAs can be more flexible if there are problems in the future than commercial lenders

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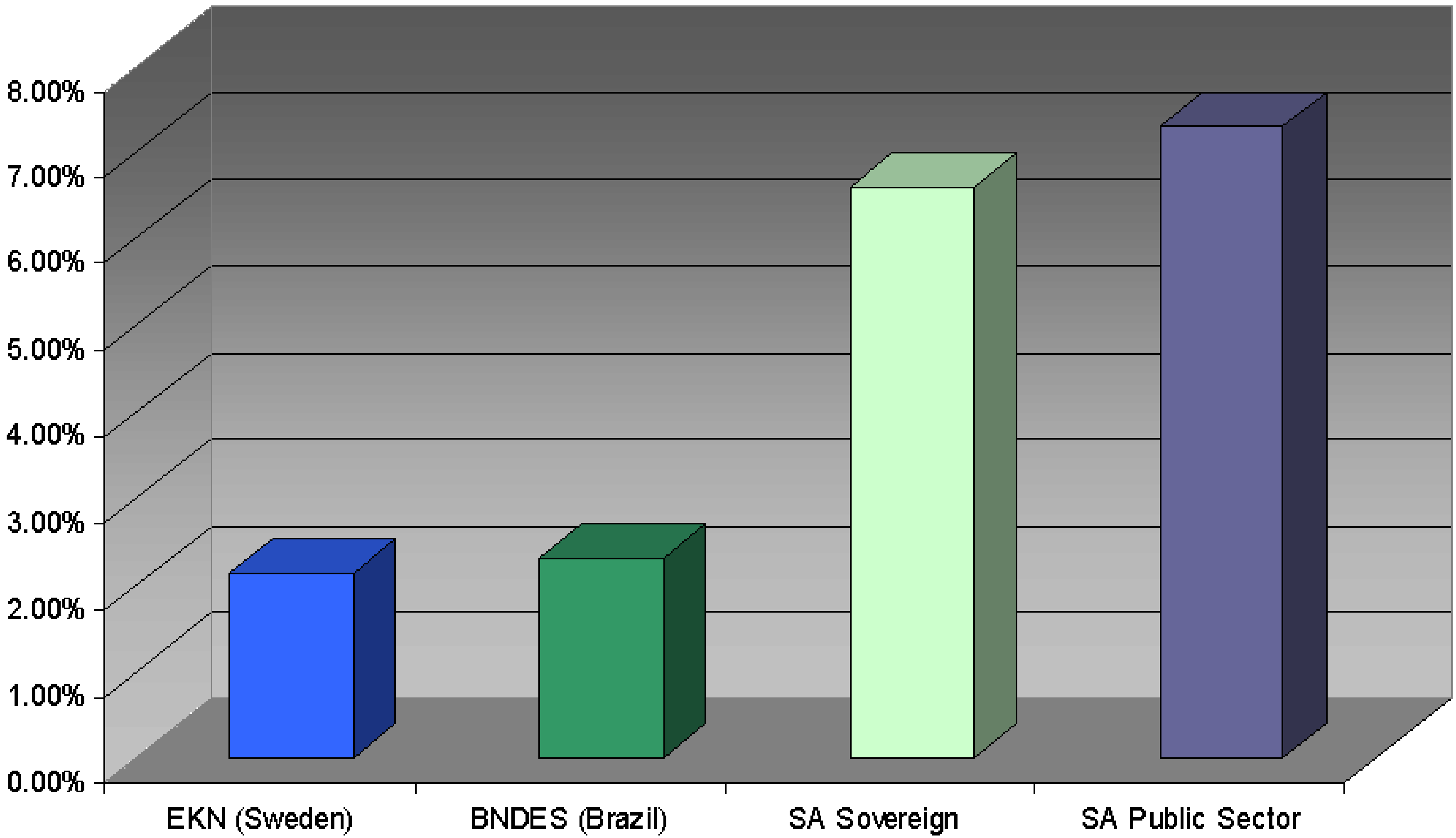
10 year USD ECA loans vs South African 10 year USD Bonds



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But what happens if the Project or borrower fails?

The main risk is that the concessionaire/borrower cannot service its debt or the City withdraws its concession for non performance

The lenders will have step in rights into the Project Company and a lien or pledge on the buses and will use this leverage to sit down with the City

The City typically can opt to 1) take over the loan payments 2) buy the buses/project assets for the outstanding value of the financing or 3) find a new concessionaire(s) to act as the borrower

What would loan default mean for the bus supplier/the Bus operating Company?

The bus supplier should have been paid *without recourse* for buses supplied so no comeback to them. Any equity in the concessionaire would potentially be lost unless the new concessionaire is required to pay an acquisition fee. Potential reputational risk/damage of relationship with City and ECA if concession cancellation due to non performance is linked to the bus supplier's or the BOC's performance

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