5.1 Features of project financing

Key characteristics of Project Financing.

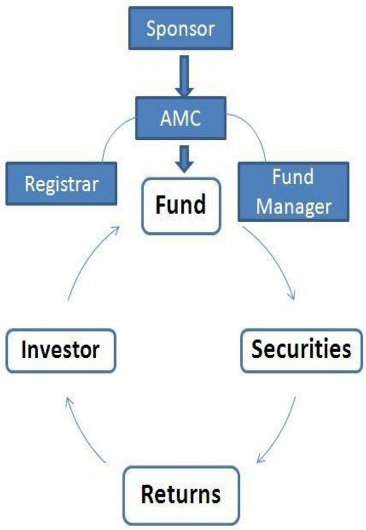
The key characteristics of project financing are:

- Financing of long term infrastructure and/or industrial projects using debt and equity.
- Debt is typically repaid using cash flows generated from the operations of the project.
- Limited recourse to project sponsors.
- Debt is typically secured by project's assets, including revenue producing contracts.(eg a contract to deliver crude oil to petroleum processes companies
- First priority on project cash flows is given to the Lender.
- Consent of the Lender is required to disburse any surplus cash flows to project sponsors
- Higher risk projects may require the surety/guarantees of the project sponsors.

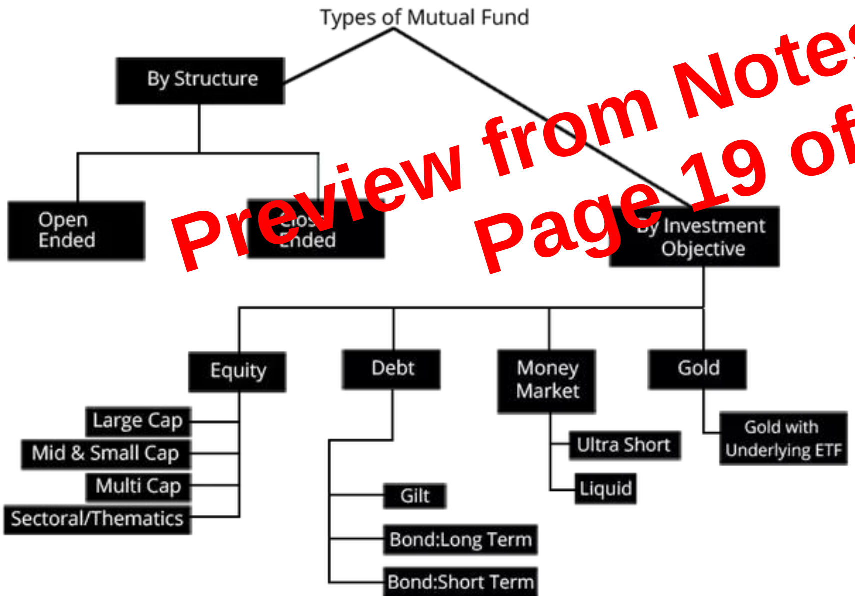
How can a project financing be identified?

Not every project financing transaction will have every characteristic, but the following provides a preliminary list of common features of project finance transactions.
Capital-intensive.
Project financings tend to be large-scale projects that require a great deal of debt and equity capital, from hundreds of millions to billions of dollars.
Infrastructure projects tend to fill this category.
Highly leveraged.
These transactions tend to be highly leveraged with debt accounting for usually 65% to 80% of capital in relatively normal cases.
Long term.
The tenor for project financings can easily reach 15 to 20 years.
Independent entity with a finite life.
Controlled dividend policy.
To support a borrower without a credit history in a highly-leveraged project with significant debt service obligations, lenders demand receiving cash flows from the project as they are generated.

Many participants.
These transactions frequently demand the participation of numerous international participants. It is not rare to find over ten parties playing major roles in implementing the project.
Costly.
Raising capital through project finance is generally more costly than through typical corporate finance avenues. The greater need for information, monitoring and contractual agreements increases the transaction costs. The highly-specific nature of the financial



There are various types of Mutual Funds that exist.



We broadly classify Mutual funds by 2 categories:

The common denominator with an equity fund is the desire for fund management to find good opportunities to invest in businesses that will grow.

Types of Equity Funds

- **International Equity Funds** are those that invest in stocks *outside* of the United States.

16.1 Determinants of debt-equity ratio

The following are determinants:
Nature of assets
Business risk
Control
Flexibility (degree of freedom)
Borrowing history

17.1 The process and means of raising equity capital

- Ordinary shares

  Ordinary shares(common shares) represent the basic voting shares of a corporation. Holders of ordinary shares are typically entitled to one vote per share, and do not have any predetermined dividend amounts. An ordinary share represents equity ownership in a company proportionally with all other ordinary shareholders, according to their percentage ownership in the company. All other shares of a company's stock are, by definition, preferred shares.

All corporations must have ordinary shares as part of their stock, as defined in their articles of association, and at least one ordinary share must be issued to a shareholder. In other words, someone has to be the owner of the corporation.

Rights and Obligations of Ordinary Shareholders

Ordinary shareholders have the right to a corporation's residual profits. In other words, they are entitled to receive dividends if any are available after the dividends on preferred shares are paid. They are also entitled to their share of the residual economic value of the company should the business unwind; however, they are last in line after bondholders and preferred shareholders for receiving business proceeds. As such, ordinary shareholders are considered unsecured creditors.

While they face greater economic risk than creditors and preferred shareholders of a corporation, they can also reap greater rewards. If a company makes large profits, the creditors and preferred shareholders are not paid more than the fixed amounts to which they are entitled, while the ordinary shareholders divide the large profits among themselves. The same occurs when companies, such as start-ups, are sold to larger corporations. The ordinary shareholders usually profit the most.

The only obligation that an ordinary shareholder has is to pay the price of the share to the company when it is issued. In addition to the shareholder's right to residual profits, he is entitled to vote for the company's board members (although some preferred shareholders may also vote) and to receive and approve the company's annual financial statements.

Value of Ordinary Shares

1) After the finalization of contract, borrowing company will have to submit the copy of Annual accounts to the lender.

2) The assets purchased will be properly maintained and insured by the borrowing company.

3) If the loan amount is big then the lender may have a representative on the Board of Directors of the company.

4) To ensure the liquidity position of the borrowing company, the agreement may stipulate the following:

a. No dividend will be paid without the consent of the lender.

b. No long term loans to the officers or directors of the company.

c. No investments outside the corporate securities.

d. No redemptions of the debt before the maturity.

Main Clauses in term loan agreement

Following are the main clauses in term loan agreement.

1) Amount of loan
2) Period of payment
3) Rate of Interest
4) Method of payment of interest
5) Nature of security offered

- ❖ **features and procedures**

Following are the features of term loans:

1) Banks or Financial institutions granting term loans are creditors and not the owners of the company. They only lend the funds to the company.

2) They are required to be repaid during the life time of the company at a pre decided interval.

3) The term loans are either secured or unsecured.

4) Return on term loans is paid in the form of interest. This interest is still paid even if there is non availability of profits.

5) This source of raising funds is very risky from company's point of view.

6) Term Loans are less risky on the part of banks and financial institution.

1. Avoidance

Avoidance is the best means of loss control. This is because, as the name implies, you're avoiding the risk completely. If your efforts at avoiding the loss have been successful, then there is a 0% probability that you'll suffer a loss (from that particular risk factor, anyway). This is why avoidance is generally the first of the risk control techniques that's considered. It's a means of completely eliminating a threat.

2. Loss Prevention

Loss prevention is a technique that limits, rather than eliminates, loss. Instead of avoiding a risk completely, this technique accepts a risk but attempts to minimize the loss as a result of it. For example, storing inventory in a warehouse means that it is susceptible to theft. However, since there really is no way to avoid it, a loss prevention program is put in place to minimize the loss. This program can include patrolling security guards, video cameras, and secured storage facilities.

3. Loss Reduction

Loss reduction is a technique that not only accepts risk, but accepts the fact that loss might occur as a result of the risk. This technique will seek to minimize the loss in the event of some type of threat. For example, a company might need to store flammable material in a warehouse. Company management realizes that this is a necessary risk and decides to install state-of-the-art water sprinklers in the warehouse. If a fire occurs, the amount of loss will be minimized.

4. Separation

Separation is a risk control technique that involves dispersing key assets. This ensures that if something catastrophic occurs at one location, the impact to the business is limited to the assets only at that location. On the other hand, if all assets were at that location, then the business would face a much more serious challenge. An example of this is when a company utilizes a geographically diversified workforce.

5. Duplication

Duplication is a risk control technique that essentially involves the creation of a backup plan. This is often necessary with technology. A failure with an information systems server shouldn't bring the whole business to a halt. Instead, a backup or fail-over server should be readily available for access in the event that the primary server fails. Another example of duplication as a risk control technique is when a company makes use of a disaster recovery service.

6. Diversification

Diversification is a risk control technique that allocates business resources to create multiple lines of business that offer a variety of products and/or services in different industries. With

However, contract agreements must:

- Be In Writing
- Contain a description of the product or service being offered
- Understood and clear between both parties
- Include services being contracted clearly
- Include cancellation or termination policy
- Have financial terms clear

Contract Agreement Types

Contract agreements vary or could have several modifications depending on the contract being executed. For example:

- Express - This type of agreement defines real well the purpose and scope of the agreement. Under this alternative, the stipulations and terms of the contract are understand clearly by each part.
- Executed - An executed contract agreement provides a warranty period or malfunction. Under this agreement services have been rendered but the contract protects one party when the other's performance fails to provide the proper warranty for defective or incorrect installation.

- Conditional - A conditional contract agreement is an agreement used when services could not be provided at the time the contract was signed. It stipulates a future date when services will be rendered if certain conditions are met.

Pricing

Fixed price contract

Contract that provides for a price which normally is not subject to any adjustment unless certain provisions (such as contract change, economic pricing, or defective pricing) are included in the agreement. These contracts are negotiated usually where reasonably definite specifications are available, and costs can be estimated with reasonable accuracy. A fixed price contract places minimum administrative burden on the contracting parties, but subjects the contractor to the maximum risk arising from full responsibility for all cost escalations. Also called firm price contract.

Completion cost over run and performance guarantees
A CO guarantee is usually a three-party agreement between the financing bank as an indirect beneficiary, the project company as a direct beneficiary, and the project sponsor acting as a guarantor. The sponsor gives the bank and the project company a guarantee that it will support the project in the event of cost overruns. The upshot is that the bank can require the sponsor to give the project company funds to cover extra costs. Naturally, the project company may demand a capital injection on its own, but, since it is controlled by the sponsor, the security lies in granting this right to the bank to protect it against a sponsor

Political risk guarantee

This is the coverage that provides financial protection to investors, financial institutions and businesses that face the possibility of losing money because of political events. Political risk insurance protects against the hazard that a government will take some action that causes the insured to experience a large financial loss. Political risk insurance can cover many possibilities, such as expropriation (e.g., government confiscation of property), political violence (e.g., acts of civil unrest or insurrection), the inability to convert local currency and repatriate it, sovereign debt default, and even acts of terrorism and war.

Types of Political Risks

1.Risk of expropriation: Government holding particular assets or goods for the company

2. Risk of changes in regulatory regime:

3. Risk of war and terrorism:

4. Risk of imposition of capital controls:

5. Currency risk:

6. Risk of political upheaval (other than war or terrorism):

7. Risk of 'crossfire' sanctions:

8. Risk of non-neutrality of legal framework:

Political Risk Management

1. Identification of Political Risk
2. Measurement or Assessment of Political Risks
3. Action Plans for Management or Mitigation of Political Risks
4. General Mitigation of Political Risks
5. Diversification*:* undertaking a wide variety of investments
6. Decentralization of decision making*:* Decentralization leads to freedom of sub-units in quickly making decisions to allow for smooth liquidation of assets, withdrawal of investments, exit from business, etc. if the political risk seems to be materializing.

4. *Avoiding long-term commitments:* of resources including labour, capital, physical assets etc. through insertion of relevant contractual clauses.
5. Implementation of intelligence system*:* to monitor recent social, political and environmental trends that may reasonably impact business. Such monitoring allows enough opportunity to respond to brewing political risks.
6. Lobbying: Influencing host government through informal negotiations, industry associations, business goodwill, personal contacts, advice from ambassadors of domestic country, etc. is strategically important.

- maintaining the infrastructure, momentum and drive to support communities of practice;
- improving, embedding and measuring capabilities to achieve higher levels of maturity;
- owning and deploying standard tools and techniques.

The P3(public- private partnership) management infrastructure may range from a single person to a large team containing many different roles and specialists including, among others:

- planners and schedulers;
- cost engineers;
- subject matter experts;
- assurance staff;
- configuration managers.

The overall infrastructure may be divided into multiple offices, some temporary and some permanent. For example, a support office might provide administrative support to a specific project or programme. This is then disbanded once the work is complete. In contrast, a community of practice, or centre of excellence, has a permanent support role independent of the creation and completion of any individual piece of work.

The shape of the infrastructure will reflect its environment, but its component groups must always have a clearly defined purpose and scope. The roles and levels of authority of these groups must be communicated to the delivery team(s) and reinforced periodically.

The concept of PPPs(3Ps)

Public-private partnership (PPP) is a funding model for a public infrastructure project such as a new telecommunications system, airport or power plant. The public partner is represented by the government at a local, state and/or national level. The private partner can be a privately-owned business, public corporation or consortium of businesses with a specific area of expertise.

PPP is a broad term that can be applied to anything from a simple, short term management contract (with or without investment requirements) to a long-term contract that includes funding, planning, building, operation, maintenance and divestiture. PPP arrangements are useful for large projects that require highly-skilled workers and a significant cash outlay to get started. They are also useful in countries that require the state to legally own any infrastructure that serves the public.