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Alternative funding solutions are needed

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Morgan Lewis' Tarek El-Assra looks at project financing beyond oil money

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IMF managing director, Christine Lagarde, said on her recent visit to the UAE that the collapse of oil prices is causing a paradigm shift in economic landscapes where stability is hinged on petrodollars.

With a growing population in the region, the capital costs for infrastructure to support growth are high, at a time when governments are facing drastically cut revenues and budget deficits. In the long term, adjusting to the new environment requires governments to tap alternative sources in order to fund their project requirements.

While expensive or non-essential projects are on hold for now, alternative financing options are being explored to secure funding of core projects. There is a need to diversify away from government balance sheet finance.

We may see greater export credit agency (ECA) coverage with, for example, Chinese contractors bringing financing solutions through Sinosure/C-Exim-covered ECA facilities, or perhaps consortiums seeking Japanese sponsors to access Jbic [Japan Bank for International Cooperation] funding.

Perhaps regional financial institutions such as the Islamic Development Bank and the Arab Fund for Economic & Social Development might step up to bridge some of the gap. Islamic finance liquidity may also contribute to alleviating the shortfall. Another alternative could be greater pension funding of projects, where there are synergies in matching long-term assets to long-term pension liabilities.

Could project bonds ignite the project finance market? To date, they have been limited in the region, but as governments seek to find alternative financing solutions, project bonds could be the answer, as they allow access to non-bank liquidity and they have long tenors.

The case for public-private partnerships (PPP) in the Middle East and North Africa (Mena) has also been trumpeted for many years. By involving the private sector, governments can achieve increased budgetary certainty, generate enhanced value for money over the life of the project and benefit from private sector efficiencies.

In Egypt, for example, the PPP Central Unit acts as a “one-stop shop” and has proved to be attractive to the private sector. If other countries adopt a similar approach, and ensure that they have a solid legal and regulatory PPP framework, we may see PPPs really taking off in the Mena region.

To stimulate the project finance market, governments may consider slicing projects into different phases to make them easier to finance.

In Mexico, for example, the government struggled to find bidders to build eight prisons, but when they dissected the project as a hospitality business with different PPPs set up for food, laundry and cleaning, instead of the usual prison contracts, they were able to capture greater interest in the project.

What is clear is that for the foreseeable future, there is unpredictability in the market as to what the new financing norm for regional projects will be, and it is likely that governments and project financiers will use different structures and financing techniques depending on the type of project.

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