Infrastructure Finance
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Lecture - 23
Project Finance Markets – Financial Intermediation

Hi welcome back to this course on Infrastructure Finance, this is a lecture 23, we will continue our discussion on Project Finance Markets in this lecture, the topic that you are going to talk about, in this lecture is Financial Intermediation. We will try and cover, some of these salient aspects that we see in financial intermediation in the project finance markets.

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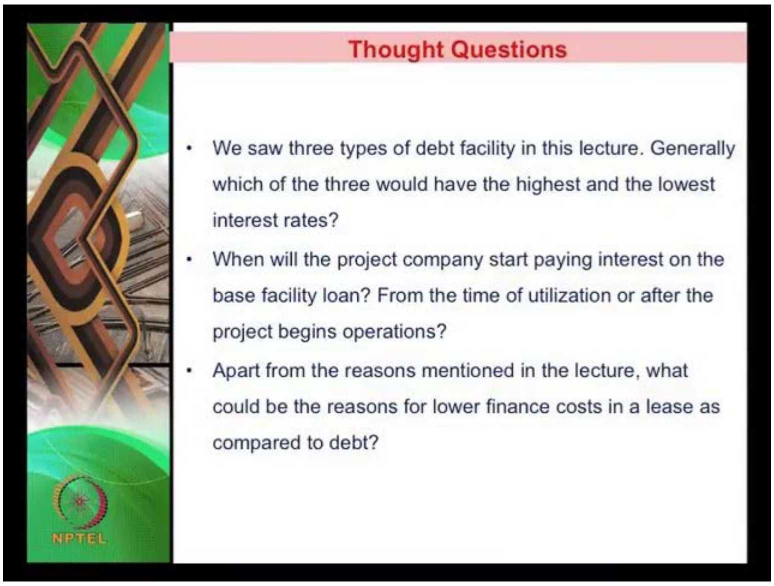

But before we actually do that, we will try and answer the thought, that we actually put forward in the previous lecture. So, question number 1 was, we saw 3 types of debt facility, generally we had a base facility and then we had the working capital facility and then we had the standby facility. So, the question was which of these would have the highest and the lowest interest rates. So let us try and analyze, the major features of a each of these 3 loan facilities and then by process of a indexation, let us try and derive, what would actually, be which of these facility will have the lowest and the highest interest rates. So, let me write it on the board, so we have a 3 types of facility.

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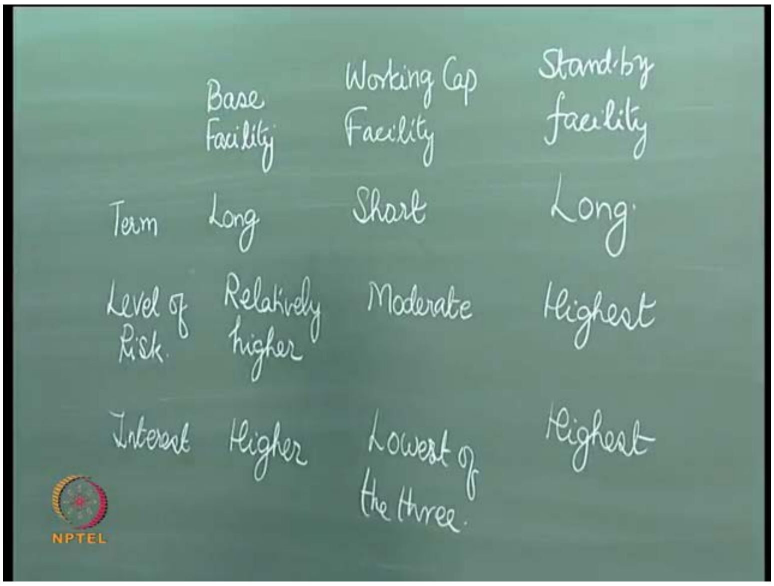

We have the base facility, then we have the working capital facility, then we have the standby facility, so let us analyze, these 3 loan facilities in terms of the various features of these facilities. The first feature would be let us say the term of the facility, so base facility is a moralize like a term loans, so therefore, it is going to be a long term facility. So, this will be a long term a facility whereas, working capital facility is essentially a facility that is available after the project begins operations and is needed to take care of the working capital requirements that is to bridge, the deficit in the cash flow cycle.

So, essentially the duration of the working capital facility will technically be you know short and it is going to be on a revolving credit basis, so we have what is called as a short term credit, for working capital facility. And then what is going to be this standby facility, standby facility is essentially to take care of any exigencies, any excess in terms of a requirements as compare, what has been budgeted. So, therefore, the standby facility yield is actually going to boost up the facility that is available, for construction and development of the a project.

So, in terms of term a standby facility will have a term that is very similar to what we have for the base facility, so standby facility is also going to have a long term duration. The next that will actually have to look at, in terms of analyzing a loan feature is a the level of risk involve in each of these facilities right level of risk. So, if you look at the base facility, it is actually being provided at the earliest phase of the project life cycle, so therefore, the risk is necessarily going to be relatively higher.

So, the level of risk will be relatively higher, when a come up working capital facility by the time construction is already complete, the project is in operation stage, so in the operation stage the level of risk is going to be a relatively moderate, as compare to what we have in the construction phase. So, a level of risk working capital facility will be moderate and what we actually look at for a standby facility is facility to be used, when the expenditure exceed, the budgeted amounts, when there is exigencies, when there are an unpredicted expenses.

So, that is actually used to meet the to meet the to meet the financing needs, so therefore, a standby facility is actually utilized, only when the situation, which is not been accounted, for at the budgeting stage. So therefore, when a project starts utilizing the standby facility, it gives a indication that, there is something, that is going on in a way that has not been flat at the budgeting stage. So therefore, the project is probably a little bit more risk year or in the standby facility being used, so in the level of risk, the standby facility will among the 3 will probably highest.

So, now we look at the 2 characteristics, for this a loan types and this will give in indication in terms of you know, which of those loans have the highest interest rate. So, if you compare these 2 features, we find standby facility has a long term loan and it is probably has a highest risk. So, therefore, in terms of the interest rate a standby facility will be the highest and a base facility is also a long term loan, so it is a very general rule of term that, the of the interest rate in the long term loan is going to be higher than interest rate on a short term loan.

So, when we compare on that basis, long term loans are going to have a higher interest rate as compare to a short term loan of working capital facility. So, therefore, the interest rate on the base facility and the standby facility is going to be definitely higher, now between these 2 long term loans, which one will have higher interest rate, the one which actually has a highest risk exposure will have highest interest rate. So, therefore, standby credit facility will probably have a highest risk exposure as compare to base facility.

So, interest rate between these long term loans will be higher for the standby facility, so base facility the interest rate will be higher, as compare to a short term loan. Working capital will actually have the least interest rate, because it is a short term loan facility and more importantly the risk level is moderate, because of plant is in the operation stage. So, this will be the lower, lowest of the, so now, we can probably a get a general idea, in terms of why each these loans are costar in a way that, we normally see in practice.

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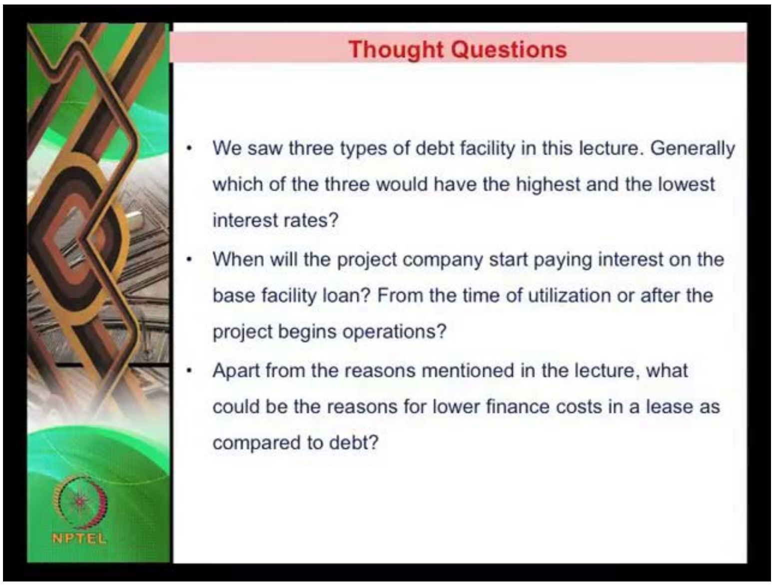

The next question that, we put forward is when will the project company start paying interest on the base facility, from the time of utilization or from the time of project begins operations.

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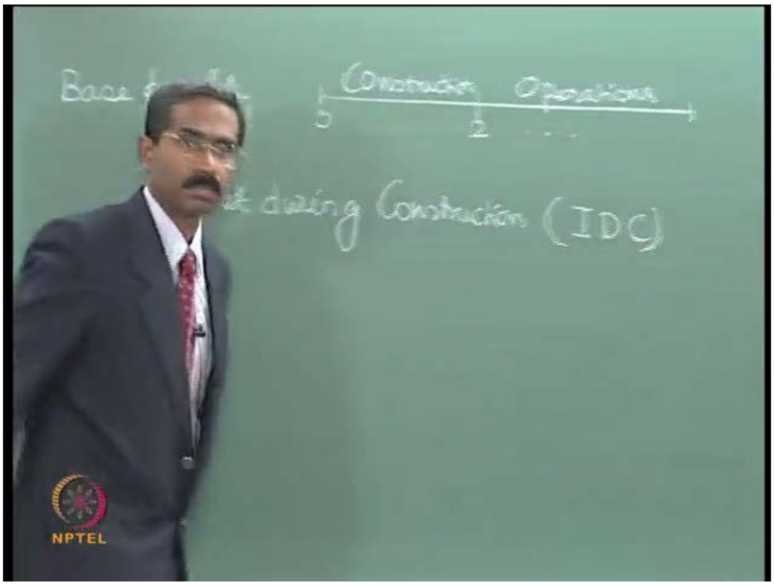

So, if you really look at it a base facility is a long term loan, but the utilization of the loan, that is the time at which the loans are withdrawn, is also not advance stage, it happens over a period of time. Let say for example, on the base facility is utilized, this is your 0, this is your 2, this is when, the project begins operations, so the withdrawal of base facility happens, let say during the project construction phase, which is let say from 0 to 2 years. Now the loan could actually, part of the loan could actually withdrawn from, time 0, you know time 0.5 years, at end of the first year and so on.

So, the interest rate technically would actually be have to be paid, from the time the loan has been withdrawn, you actually start, actually paying interest on the loan, from the time you actually take the loan. But, an important part of the project life cycle is during the construction phase, the project does not get any revenues, revenue starts accruing only when the project begins operations. So, in a base facility, the loan is actually serviced using the project cash flows, now when the project does not have any cash flows, during the construction phase, how can be interest be paid.

The project is unable to pay interest, during the construction phase, but at the same time, since the project has actually withdrawn a loan, you will have to start paying interest. So, here is what we have, a concept called, the interest during construction, we have what is called as, your interest during construction. In industry parlance, it is commonly called as IDC.

So, the interest starts actually accumulating as soon as the loan is being utilized, but the interest is not paid, the interest is not paid to the lender being pay because there are no cash flows, so the interest gets accumulated and they all the interest that actually is accrued, during the construction phase is called the interest during construction.

And this interest during construction is added to the principal that is outstanding, at the time the project begins operations and that is when, the loan starts to be repaid, to the lender. So, the interest is actually accrued, but the interest is not paid during the construction phase in a base facility.

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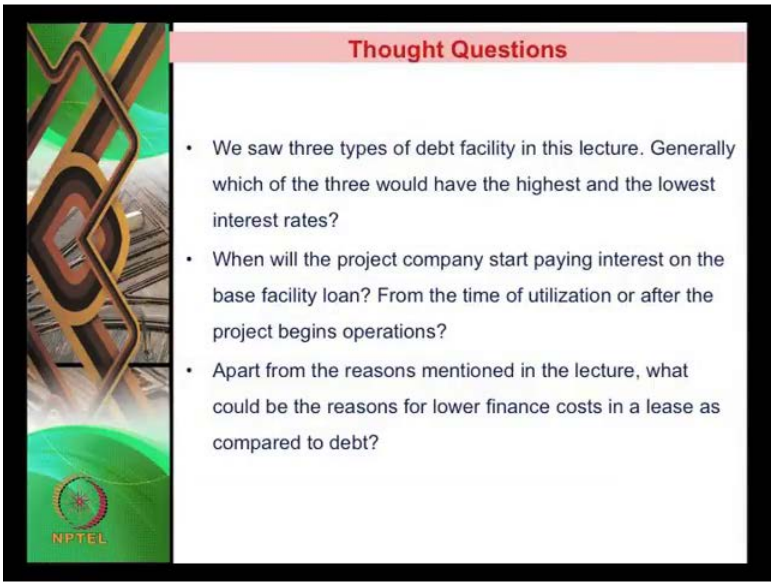

So, the third question that, we put forward us apart from the reasons mentioned in the lecture, what could be the reasons for lower finance costs in a lease, as compare to a debt. So remember, we talked about, leases as one of the alternatives of securing capital in a project finance transaction and then we looked at the various advantages of lease and one of the advantage is it actually, helps to reduce of financing costs.

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So, when we look at lease, we looked at 2 reasons, why leasing can actually result in lower finance costs, the first reason is the history and performance of the leasing company. So, the leasing company would have a longer performance history and track record as compare to the project finance company and therefore, if the project finance company borrows, it will have to probably incur a higher interest rate.

But, if leasing company borrows, on the strength of it is financial performance, it is able to borrow at the lower interest rates and the leasing company shares some of this benefit of the lower interest rate with the project finance company. So, therefore, it is able to achieve lower finance costs, so that is a reason number 1.The second reason that, we talked about was, the benefit of the depreciation tax shields, the benefit of the depreciation tax shields, so the reason here is a during a initial years the market project finance might not really have profits.

And therefore, it may not be able to enjoy or claim the tax shields from depreciation and if they are not claim within a certain amount of time then the tax cottage from the non operating losses expire, so therefore, they are not able to claim the entire tax shields. But, on the other hand, if the depreciation is claim by the leasing company, which essentially is owner of the asset, then it is able to enjoy, the tax shields from the depreciation.

And part of the depreciation tax shields can then passed on to the lessee and therefore, it results in a lower financing costs, so these are the two reasons that we actually discussed in the previous lecture. The third reason, which also, which is probably more of not mentioned is can be attributed to seniority of the payments, that is being made to the lessee, so essentially if you look at it, a project finance company has 2 alternatives.

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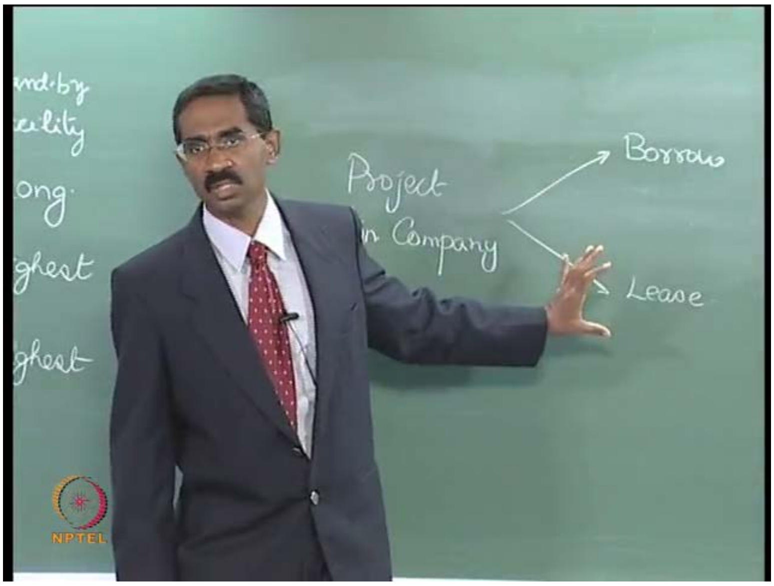

So, it can actually either borrow and acquire an asset or it can actually lease an asset, so these are the models. So, in terms of the seniority of the cash flow payments, in both this categories, you actually find that, interest payments are done, after all the operating expenses are taken care of. So, a interest payments are actually, have seniority as compare to let say dividend payments, but then expenses related to operation have seniority as compare to interest payments.

So, then if you really look at leasing, the lease rentals or essentially treated, as a part of operational expenses and not really as a part of a mess servicing the lenders. So, from that prospective lease rentals have seniority, the leaser have seniority in terms of revising payments, as compare to debtors. And because of the fact that, there is certain amount of seniority to lease rentals, one is a one is actually able to you know, use this seniority to the advantage and then claim a lower finance costs.

So, as the seniority increases the risk of payment becomes a lesser and lesser and if you really look at, it lease rental is more of obligations and it obligations as a lot more a weight, as compare to obligations toward the lenders. Because and then therefore, this seniority also provides a certain amount of advantage in terms of the lower finance costs to the project finance company.

So, this is reason that is most of in our discuss and cost advantage with seniority payments might actually not be very large, but at the same time, it may exist and we have to be aware of the fact that, the lease rentals have seniority as compare to debt service.

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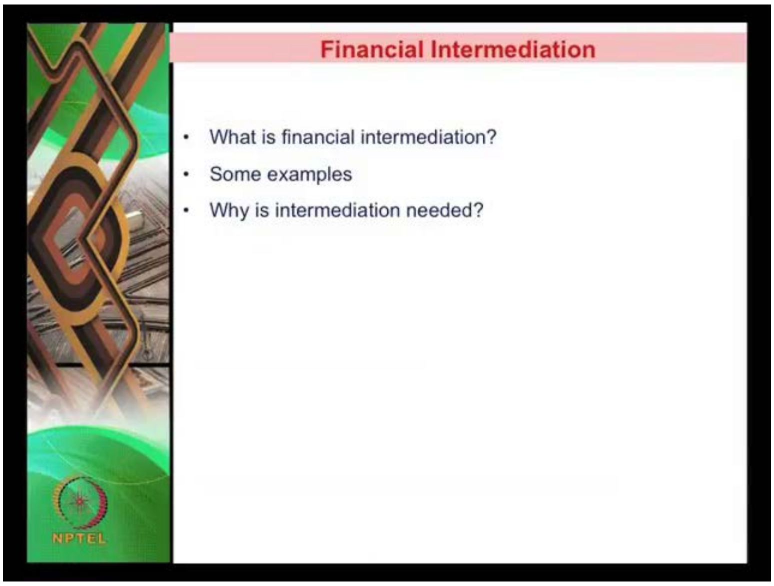

Now, we will actually get back to the topic of today's lecture, so topic of today's lecture is financial intermediation, we have to first really understand, what is the financial intermediation. So, if you really look at the financial markets, if you really look at the capital markets.

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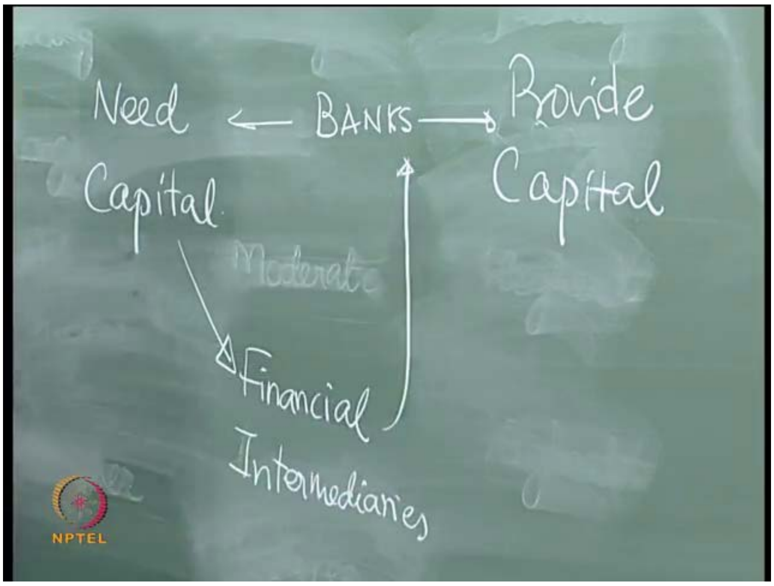

So, there are at one hand, we have what is called as a, who need a capital and then on the other hand, we have what is called as people, who are with surplus of funds they actually provide capital. So, people who need capital, they actually approach, people who provide capital and then get a money right. So, this is common across all for example, let us look at the retail level, if you are actually taking loan for your education, what you actually do, you actually go to a bank and then take a loan.

So, the bank is actually a providing a loan, for your education, but is actually the bank providing the capital, a bank is not necessarily providing the capital, what you actually do is the bank actually has, you know depositors investing their capital with the bank. And the bank uses, the deposits to actually provide your loan to some sense, if really look at it bank is a financial intermediary, in between the investors and the borrowers. So, this is a very simple case of a financial intermediation, so bank in the sense is actually provides a capital.

Now, there are different levels of intermediation, so for example, between these 2, there are banks is one level of financial, no sometimes, it is a not possible for, let say the borrowers to directly approach the banks. Because, so many reasons the borrowers might not really have the capacity to provide all the requirements, that the banks need and they may actually looks for expertise, who will actually capital information in a way that will meet the requirements of the bank, which intern might actually provide a capital.

So, what you have in some cases the borrowers can approach, what is called as a financial intermediaries, such as your investment banks and these financial intermediaries, act as a link between the borrowers and the banks. So, here we are talking about, financial intermediation of the next level, so bank itself is a financial intermediary. But, between the bank and the borrower, there is hidden another service provider, who actually helps to raise capital for the borrower, so this is the next stage of financial intermediation.

So, you actually have financial intermediation in the capital markets, it is a very, very active way, simply because of the fact that a financial intermediaries, facilitate to raise capital for the borrowers. And it helps to the financial intermediaries, over a period of time develop a lot of expertise about, the industry about, the financial institutions about, the banks and they use this expertise in order to effectively raise capital for the borrowing forms.

The question is why is intermediation needed, why cannot the borrowers directly approach the banks, let say for example, in a case of a simple thing like, an educational loan, it is possible for a individual borrowers like you, like so many others to directly approach a bank. Because, the requirements that are needed to be satisfied, to take an educational loan is not very complicated and there is no greater level of expertise, that is needed, to actually fulfill all the requirements, for taking an educational loan.

But, now let us take a issue like a project finance, so project finance is a lot more complicated, than the educational loan, it involves a larger amounts of capital, it probably also carries in term some sense, lot more uncertainties as compare to, let say a fixed product like an educational loan. So, the kind of documentation, the kind of information that needed to provided to the banks is going to be a lot more complex, it going to be a lot more time consuming and it would need a very specific expertise.

And most of the time the banks also rely a lot on the relationship that bank, for example, in intermediary, which actually has a very good relationship with the bank will be able to you know, ensure that a particular loan transaction is getting a right attention as compare to those that do not have any relationship.

So, unless until you have a good relationship with a bank, you know it is going to be a very difficult to actually, get the attention of a this, the relevant people at the bank to look at to look at it. So, the intermediaries play a very important role in that connection, so intermediaries have a relationship with several of the banks and they ensure that, because of the relationship, the deals on the operation is evaluated by the right person.

They also actually develop over a period of time expertise in terms of, how you can actually possession a particular investment opportunity to bank, so that it can meet their internal, you know credit requirements and so on. In essence they kind of understand, what are the information is bank looking for, what are the various features that will give a bank comfort, in lending to this particular project.

So, this information you know might not, you know the project finance company might not actually have the strength and the management capability to handle this, now the project finance company can actually, recruit a person with experience, in raising capital to renew to actually, you know develop a relationship with a bank and so on. But, then raising capital here in most cases is a onetime exercise, remember much of the capital is needed for construction and once a capital I raised, you do not really need the expertise doing the subsequent stage of the project.

So, therefore, recruiting in house talent to meet this kinds of a capital to meet the to meet the expertise in the capital resource is not going to be something that is going to be constantly, needed for the project finance company. So, why invest in this talent, where it is not going to be needed on a long term basis, so therefore, by using financial intermediaries, a project finance company is outsourcing the requirement, for expertise in terms that is needed for raising capital.

In many sense this could be cost effective in many sense given the fact that, the investment bankers are constantly updated in terms of the reason sense and practices, they will be able to raise loans a lot more effectively as compare to in house talent. Large corporate houses, where there is a need to constantly raise capital and to constantly maintain the relationship with the banks, might not actually rely on financial intermediaries, they may actually go ahead and raise their capital using in house talent.

But, by and large, if you look at project finance companies given the fact that a capital raising exercise is not a frequent occurrence, they probably rely on external expertise like financial intermediaries.

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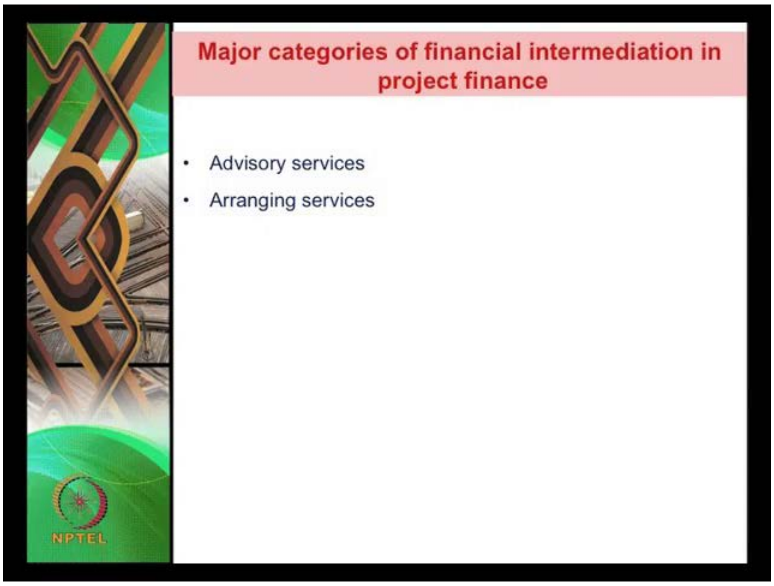

So, when you really look at financial intermediation project finance, broadly see 2 major categories, intermediaries who provide advisory services and intermediaries, who provide arranging services. Now, what are these 2 types of services, let us look at in some detail.

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Let us start with the advisory services, so what are advisory services. So, advisory services include, a whole a range of services that, that are necessary to package the project, that are necessary to prepare the project for successful fund raising, subsequently. Let say for example, a first point is a advisory services, were include studies and analysis, that are needed to make a preliminary valuation of the financial feasibility of the project.

The first thing that needed to be that, needed to be told, to the project sponsor’s is a project going to be financial feasibility, now for making that feasibility study one needs to have, a lot of information. And obviously, you know, if there is you know, no expertise available in house in terms of gathering all the information and then putting it together and analyzing it, then the project sponsors or better off handling this, using the services of an advisory services form, in making this exercises.

So, the study and analyzes that is needed to identify to predict, what is the financial feasibility of the project is a part of the advisory services. The second part is a once you identify a financial feasibility, you should also look at, what are the different project risk and the advisory services company is also help to put together, risk management framework that can address all these risks.

An advisory services, formally also expected to assists the sponsors in preparing and negotiating the major contracts, remember contract is a part of risk management framework and since a advisory services includes identifying, what are the risk management practices. They also will be assisting these sponsors in negotiating major contracts, the major contracts could be a fuel supply contract, it could be it could be a you know, a customer service, customer agreement like a power purchase agreement, it could be like a engineering procurement construction contracts and so on.

So, entire list contracts and that are needed for the project finance company and the advisory services firm can assists the sponsors in the various arrangements. And then the most importantly, before the project is actually being taken to the lenders, we need to actually have a business plan, for the project.

So, the business plan will provide details in terms of what are the expected revenues, when are the revenues expected to occur and how much are revenues expected to grow, it will also talk about, what are the expected costs going to be like and then what it is profitability of the project over the years. So, essence, it talks about the sources of revenues, it talks about the profitability, it talks about various others feature in terms of how the capital is going to be utilized and so on and so forth.

So, this business plan is very important document and the advisory services firm will play very important role in putting together the business plan. So, obviously, the advisory services firm cannot work independently, they will have to work closely with the sponsors and in some cases, in if the business plan is been prepared by the sponsors, then the advisory services firm can review the business plan prepared by the sponsors. In cases, where the sponsors are unable to prepare a business plan, then the advisory services firm will have take the responsibility of a preparing the business plan.

And an importantly the advisory services firm will also have to act as a sounding board for the sponsors, no sponsors you know will probably understand the business opportunity well, but then it is possible that the sponsors probably have their own, what is called as your, a black you know blank spots. So, the advisory services firm will have to actually, highlight the problems that the sponsors have not considered, the sponsors are probably overlooked.

And it is important that, they actually resolve some of the issues before, they can actually take the project to the lenders. So, this problems that, the sponsors have not considered or overlooked have to be resolved, for the deal success.

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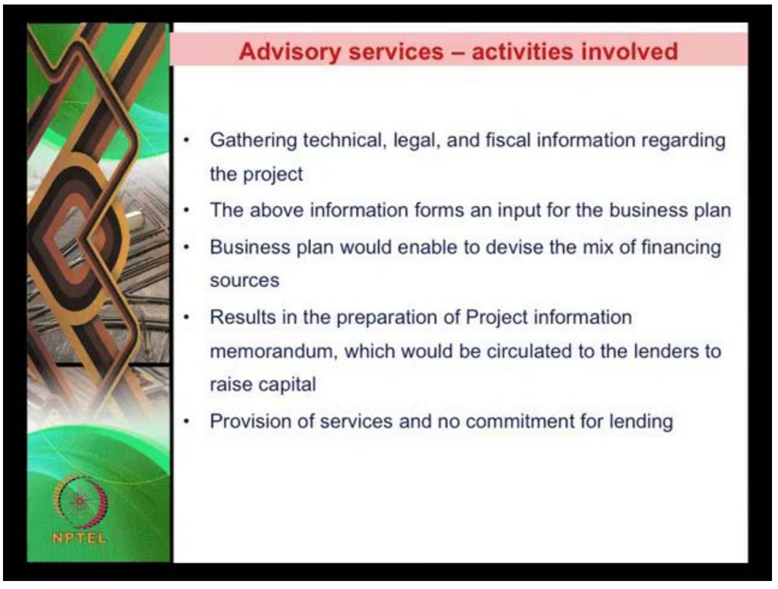

So, we look at the main features of a you know components of advisory services, but what are the activities that are involved in advisory services, let say how does an advisory services spend, it is time and what are the different activities. Now as soon as an advisory firm gets a mandate from the project company that, they have been mandated as an advisor, they will have to do whole lot of activities.

Let us look at some of the main activities that, they have to spend their time on and the first thing is they will have to start gathering a lot of technical legal and physical information regarding the project. For example, you know, how long is going to be, how long it is the road is going to be, if it is a road project, what is a kind of a trend that, we are looking at, what is a kind of technology that is needed, what is a kind of engineering that is needed to develop the road project and so on right.

So, if it is going to be a power project it talks about, what is going to be the kind of technology use for generating power, it is going to be thermal or is that going to be C C G T, what is going to be the capacity of the plant, what is going to be the fuel quality based on which you know, the cost of the, you know equipment is going to be decided and so on right. So, that is what of the second is a the legal, what are the clearances that are needed, for the project right and who are the agencies, that are responsible for getting the clearances.

Who should be a approach for getting legal clear for getting environmental clearances, who should be approach for getting clearances related to other approvals like ride off way and so on. So, this information needs to be obtain and we also need information, in terms of you know broader economy right, how is demand expected to be for the services and what is going to be price that, the consumers can be able to pay for the services of so on. So, the lot of information gathering, that are needed at the beginning and the advisory services formally expected to spend lot of time in getting.

Now, what next, so once you gather all the information, this information have to be put together, you know business plan, so obviously, business plan will have to depend on the initial information gathering exercise. So, therefore, the soundness of business plan will strongly depend upon, how exhaustive has the information being gathered, how accurate the information has been and how complete is a information has been. So, a business plan development is also, you know very, very exhaustive exercise and a sound knowledge of the ground reality are needed, for preparing the a business plan.

So, a business plan will also have to be, it also be getting lot of information from the project sponsors, now after developing the business plan what next. So, after developing the business plan the next would be to find out, how do we actually finance this business plan. And what will be the sources of capital, how much will be the debt, how much will be the equity and who are going to be the sources of debt, how we are going to source equity.

So, that is going to be the next step, in terms of what will be the sources of capital at, we will approach for funding this a business plan. Once we have cross that stage, the next would be to prepare, what is called as your project information memorandum, project information memorandum will talk about the entire project details essentially, this is memorandum that is circulated to the lenders. So, the targeted readers would be the potential lenders, who are going to invest in this project and the information that, would be of interest to the lenders will be put together in the project information memorandum.

Essentially at the end it, if you see the some and substance of an advisory services firm actually to provide a lot of services related activities to the project sponsors or to the project company and which will help which is actually help a the project finance company to successfully raise capital. The advisory services firm has no commitment for providing, capital to the a project finance firm, they may be interested, but as of as an advisory services activity, they do not have to provide any commitment, for lending to the project company.

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Now, who are this firms, who provide the advisory services, so you actually have consulting companies, whoever or largely are active in the infrastructure space, they have a services that, to provide for this kind of services. The next category would be let say, you know auditing firm, so you have unsung ((Refer Time: 33:35)) price water house.

So, these are all major a global audit firms and the corporate financing divisions of this global audit firms, they take a advisory services in a very active way. And then you have a commercial banks, who also do lending and as a part of the every project finance activity commercial banks, also have advisory services for example, commercial banks like, ABN AMRO bank society general Deutsche bank. Some of this large banks, they also have provide advisory services.

And then you have the investment banks, the investment bank are largely responsible for raising capital for the project finance company in some cases along with their arranging services they also provide advisory services. So, there are different categories of firms, who actually provide a advisory services, depending on the need, depending on the kind of advisory arrangement, to the project finance companies have, they can approach any of these firms to provide this to get this advisory services.

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So, the next we have what is called as a arranging services, arranging services are provided by firms and they are responsible for raising, capital for the project. Remember advisory services actually provide all the relevant information, which will help to raise capital. but arranging services are actually responsible for raising capital, so that is a difference. So, normally arranging people do actually provide arranging services, they have relationship with large number of banks, who make investment in this kinds of projects.

And once they get a mandate from the project company that, they have been appointed as arranger for the project then they will actually get in touch with the banks, who they have relationship with whom they think will be interested in investing such a project. And then circulate the project information memorandum, they will actually invite the banks to participate in the deal.

So, whenever, they invite they will also have to be circulated the project information memorandum. So, that is a that is a first activity that the arranging services provided do and once we have a group of investors, who are invest, who are interested in investing in the project. They actually represent all the lenders, who are going to be investing in the project remember, for a project finance company interacting with each and every investors is going to be very difficult.

Given the fact that, a most of the project finance investments are going to be very large, it is a very unlikely that, the entire capital will be provided by a single lender, you have what is actually called as a group of lenders coming together and then providing capital for the project. So, this group is commonly known as the syndication, most of the project financing, loans are actually syndication loans, in the sense that, you have more than one investor investing in the project.

And therefore, when you have such a group of investors coming together, you need to have one representative, who will interact with the project finance company. So, that representative is a company that, provide the arranging services, if you look at the types of arranging, they can be broadly classified under 2 categories. The first is a best efforts basis, so the best efforts basis providing arranging services means, that the firm will actually do it is best provide will put a best efforts in terms of arranging capital. But, it does not give any guarantee that the capital will be raised.

So, there is a lot of uncertainty in this type of a arrangement, if there is any sudden change in the external environment, if there is some new information that can cost. Let say that can provide a some adverse information on the project, then the arranging firm can actually, you know withdraw and say that is not able to actually raise a capital that is need for the project. So, the best efforts basis is a certain amount of uncertainty, for the project finance company, because the arranging services can always come back and express its inability to raise capital for a project.

The next is a the guarantee basis, so guarantee basis indicates that, if the arranging firm is not able to raise capital from other lenders then it will be in a position to invest, it is own capital for the project. So, the arranging services the arranging the arrange the arrangement is on guarantee basis, they guarantee to raise capital for the project. So, whenever we are talking about this guarantee basis, obviously, only firms that are having a substantial amount of capital will be able to provide this kind of guarantee.

Remember a firm, which is not having the financial capital, but then provides the guarantee that, it will be able to raise capital is having is going to get serious problems, if there are no interest from the side of lenders. So, therefore, normally you actually find firms providing arranging services, also have the financial capital to invest in the project. Unlike the case of advisory services, in the case of advisory services the firm might not be able to bringing the capital to invest in the project.

But, in those who actually provide arranging services will be able to get their own financial capital to invest in the project, so that is a another difference between an arranger and an advisor. How does one select an arranger, so to if you kind of look at the industry, there is what is called as a league tables, a league tables indicate a ranking of the arrangers a based on, how successful they have been able to arouse capital. So, the ranking in a league table is a very, very important indicator of the expertise success and the experience of the arrangers.

So, people look at the ranking the league table, as one of the important criteria, to actually provide, to actually select the arranger. So, there are the other inputs, such as experience a reputation the flexibility of the arranging firm, in terms of meeting the needs of the project finance company can also play a very important role. Sometimes you have an arranger, who has a excellent reputation a lot of experience.

But, if he is not able to provide a flexible service that meets the project finance a company then you know they may not be able to they may not be able to get the a mandate. It also the cost of financing also plays an important role in the selection process, which of the arrangers are able to provide a financing at the lowest cost, for example, there is an arranging fee that is involved and which of the arranger is able to arrange a capital at the lowest arranging fee, that is that is a cost of financing.

The cost of financing also includes the cost of debt, so the arranging fee, as well as a cost of debt is jointly refer to is called as a cost of financing. So, which of the arrangers are able to arrange capital at the lowest cost is going to play an important role and also important thing, the relationship is also an important, if an organization has had a very successful a relationship, with an arranger in the past.

It is very likely that, relationship might continue in the future as well provided the arranger is able to provide a competitive arranging deal. So, the past relationship in addition to experience reputation flexibility and cost of financing also plays an important role in the selection of arranger.

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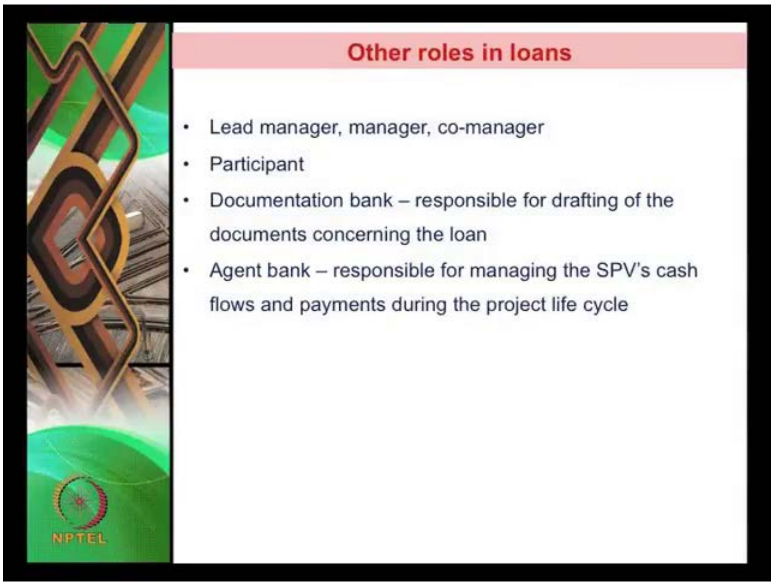

There are also other loans in a typical project finance loan structure, let us quickly look at some of them. So, you have what is called as your lead manager, co manager, so these are titles that are given to the lender depending on the commitment that, they make to the investment, let us say for example.

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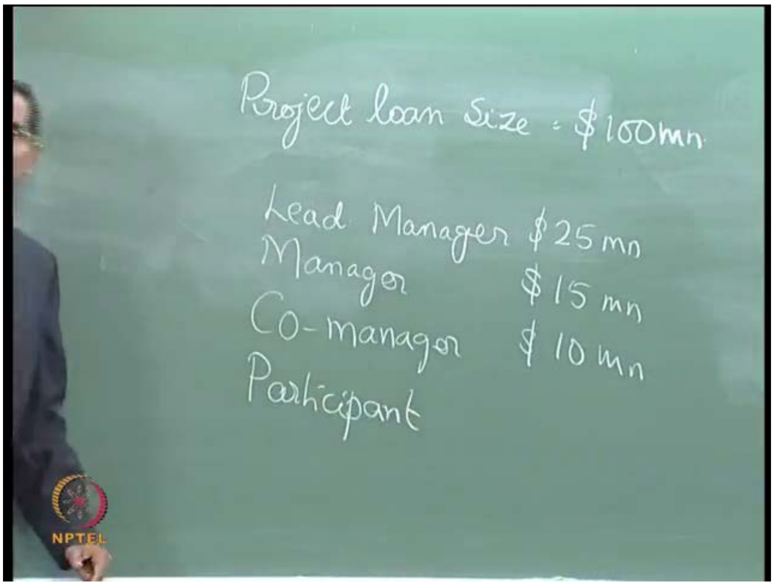

The project loan size is a 100 million dollars right, now depending on the commitment the investors make, they are given let say specific title, if an investor is able to invest a 25 million dollars then he will probably given a title of lead manager right. And if an investor is able to make a commitment for 15 million dollars then he is given a title of a manager and co manager title is probably, let say for 10 million.

So, this title reflects the amount of commitment that, the investors are made in the particular project, more the commitment a higher the title that, you will be able to get. Now, why are this titles important, this titles are important, because the titles decide a your reputation in the project finance market. So, if you are a lead manager for, large number of transaction then you are probably going to get a lot more weight age as compare to a manager title, this actually decides the commitment and also provides sentence your reputation

Then we have what is called as your participate, a participate in a deal provides, what is called as your the lowest investment amount, so participate can actually provide, what is called as your family right. So, then we have what is called as documentation bank.

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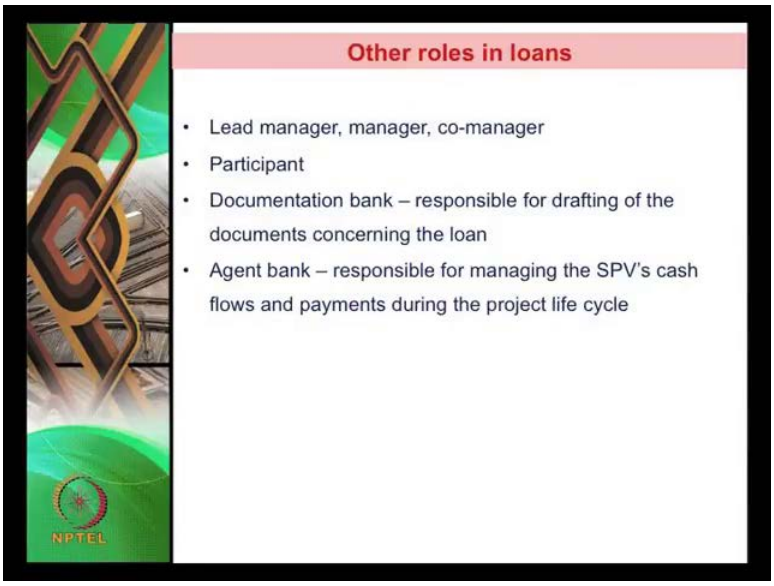

Documentation bank is responsible for drafting, the document concerning the loan, so you need to actually, a draft a loan agreement that, has to signed by all the people, who lend for the project all the investors in the project. So, there is a specific bank, which actually given a responsibility, for drafting this loan agreement and that is called as your documentation bank, then you also find, what is called as agent bank.

An agent bank is responsible for managing the SPV's cash flows, remember this loans are fierily for a long duration and there has to somebody, who will be responsible for ensuring that, the lenders are paid on time, the loans are being serviced on time. So, for that, we need to actually ensure that the cash flows are being managed properly, so there is a particular bank, which is refer to the agent bank, which made the SPV's cash flows and ensure manages a payments during the loan life cycle. So, in addition to all the other you know players that, we have seen, we have like say for example, we have the arranger firm and then we have the advisory firm these roles also play important role in the project finance transaction.

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Now; obviously, for all the services, they will have to be compensated, for an advisory services firm, they are let say what is called as different types of fee structure, we have what is called as retainer fee. Retainer fee is provided to the advisory firm to take care of the expenses that are incurred in the efforts that, the advisory services firm will have to put it. And then we have what is called as success fee, if the project has been able to successfully raise capital then the advisory services firm gets a success fee.

A success fee is a proportion of size of the deal and then there is what is called as your out of pocket expenses, if there is any expenses related to travel and other expenses, then the advisory services firm reimburse, those expenses. For the arranging services firm there is something called as the arranging fee and then the upfront management fee, the arranging fee is a fee to is a fee to compensate for the services in arranging the, to compensate for the effort in arranging the loan.

For example, the arranging services firm will have to contact the various banks and the circulate the project information memorandum will have to probably address various quarries that, might actually raise and in essence help the different banks to manage the internal credit approval process. So, the services the several services, that is needed and the effort, you know the arranging fee is to compensate for the effort that, the services firm provided.

And then we have what is called as upfront management fee, the upfront management fee also called as a commitment fee in many instances is actually fee that are provided to the different investors to compensate, for the efforts that they will have to do for you know evaluating the a particular investment opportunity. So, whenever the different investors get a project information memorandum, they will have to spend time they will have to understand a the project.

So, there is a lot of effort involve in terms of evaluating and processing the a investment opportunity, so this upfront management fee is provided to a various, all the lenders on the basis of the commitment that they make.

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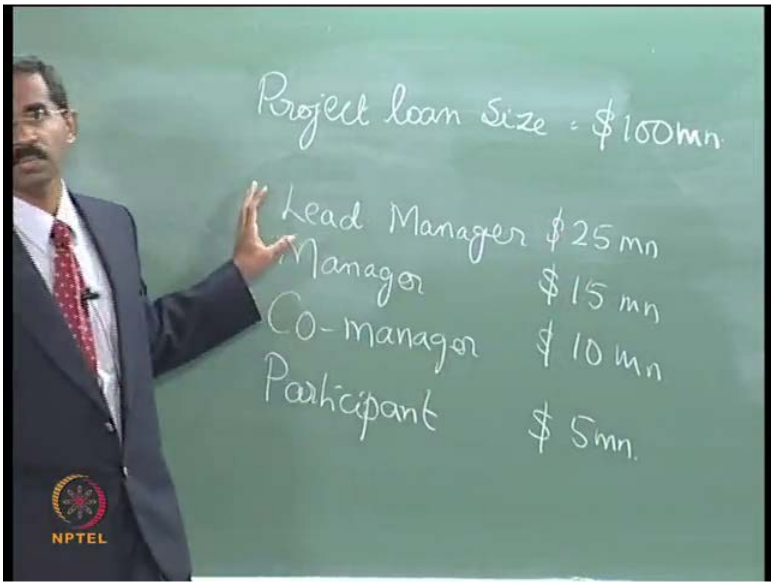

So, for example, if the lead manager makes a commitment of 25 million then the upfront management fee is a part of this, it could be let us say a point 2 percent a 0.2 percent of a commitment amount. So, that is how the usually upfront management fee is a calculated.

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So, if an investor is able to invest a lot of money, then the upfront management fee will also be higher.

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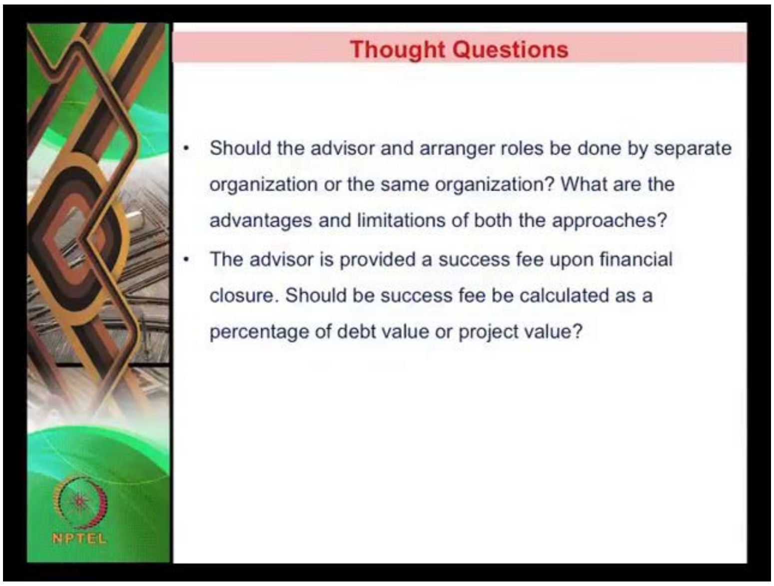

Now, we will come to thought questions for a today's lecture, so we talked about, 2 major categories of you know intermediaries, we have advisory services firms and then we have arranging firms. So, the question is should the advisor and the arranger roles be done by separate organization or the same organization, today we also have organization should provide both advisory and arranging services. So, the question is what is appropriate should both the services be provided by the same organization or should it be different organizations, what are the advantages and limitations of both the approaches.

So, second question is usually the advisory firms are provided a success fee, upon financial closure, now should the success fee calculated as a percentage of debt value or as a percentage of project value. Let me repeat the question should the success fee paid to the advisory services firm, be calculated as a percentage of debt value or as a percentage of project value. So, think about these questions and we will discuss in the next session.