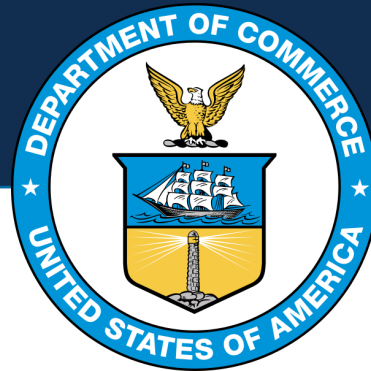


# The Commercial Law Development Program *Presents* *Public-Private Partnership Webinar Series*



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# Foreign Exchange (FX) Risks



# Today's Presenters



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# About Arnold & Porter

**100+** Years of business acumen with a practical forward-looking, results-driven approach

**14** Offices in the US, UK, Europe and Asia

**123** Attorneys ranked in *Chambers USA, UK, Global, Europe, Latin America, and Asia-Pacific*

## What We Offer

- Nearly 1,000 lawyers with an unyielding commitment to excellence and professionalism
- Exceptional depth of talent across the litigation, regulatory and transactional spectrum
- Leading multidisciplinary practices in the life sciences and financial services industries
- Broad reach across geographic, cultural, commercial and ideological borders
- One of the world's leading pro bono programs, with our attorneys performing more than 98,000 hours of pro bono work in 2021

## Recognition Across a Broad Spectrum

- *The American Lawyer's "A-List" recognized the firm 11 times since 2003*
- *Chambers USA 2022 ranked 106 attorneys as "Leading Individuals"*
- *Chambers UK 2022 ranked 12 attorneys as "Leading Individuals"*
- *Chambers Global 2022 ranked 35 attorneys*
- *Chambers Latin America 2022 ranked five attorneys*
- *Chambers Asia-Pacific 2022 ranked three attorneys*
- *Legal 500 US, UK, Europe, Latin America, and Asia ranked 64 practices and recognized 182 attorneys*

## Our Services

- Antitrust & Competition
- Appellate & Supreme Court
- Bankruptcy & Restructuring
- Complex Litigation
- Corporate & Finance
- Environmental
- Financial Services Regulatory
- Government Contracts
- Intellectual Property
- International Arbitration
- International Trade
- Labor & Employment
- Legislative
- Life Sciences & Healthcare Regulatory
- Mergers & Acquisitions
- Product Liability & Mass Tort
- Real Estate
- Securities Enforcement & Litigation
- Tax
- White Collar Defense

# Today's Agenda

- Project Finance Risks Overview
- Types of Investors in Projects
- Foreign Exchange Issues
  - Governmental/Regulatory Issues
  - Commercial Issues
- Mitigants
  - Project-level Mitigants
  - Structural Mitigants
  - Governmental Mitigants

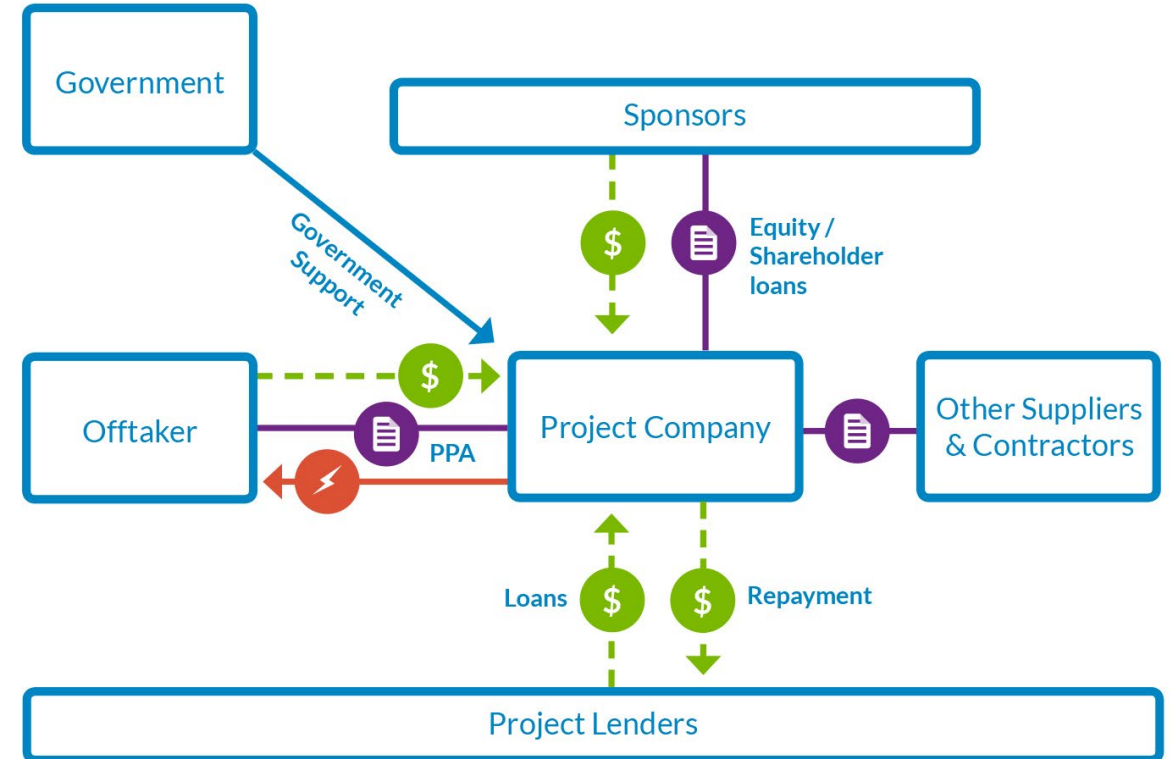


# Project Finance Risks Overview



# Project Structure & Risks

- Capital intensive projects often require funding from foreign investors
- Currency mismatches may occur
- Construction risks
- Operating/cash flow risks
- Total investment issues
- Uncovered shift in currency could turn a good project bad



# Types of Investors in Projects





# Types of Investors

Banks  
(International  
and local)

Global  
Corporations

Smaller  
International  
Companies

Local  
Companies

Equity Funds



# Foreign Exchange Issues



# Commercial FX Issues

- Rate variability
- Foreign denominated construction (usually a mix of foreign and local currency)
- Operating phase: local currency revenue, but often foreign expenses (financing, equipment, services)
- Foreign-denominated debt from banks (may carry lower interest rates, and access to larger amounts/resources)
- Return on investment for foreign investors



# Governmental/Regulatory FX Issues

FX Rate (if not free float); even if pegged, currency risk remains as investors cannot be sure that the peg will be maintained (or could be movement within bands)

Convertibility and transferability; moratoria



# Mitigants



# Project-level Mitigants

- Only finance in domestic currency
- “Natural” hedge (matching of currencies for sources and uses, revenue and payments)
  - USD (or other int’l currency) denominated exports
  - USD (or other int’l currency) denominated contracts for local market
    - May be directly priced in such currency, or otherwise indexed to the currency
- Commercial hedge (typically limited term, and cost increases dramatically for longer periods)



# Project-level Mitigants cont.

- Structuring of financing
  - Overcollateralization -- secure the debt obligations with cash flows and/or other assets with a significant buffer to give comfort to banks that even with a currency shift sufficient funds will remain for repaying the debt
    - But by its nature this means that the project company will need to reduce its leverage, which may reduce the return of the investor, making the project less attractive
  - Reserve accounts for currency buffers
    - But to be effective requires a relatively stable currency -- this is not practical to address potentially large shifts in value
- Termination payments linked to debt size
- Case study – Early Termination Guarantee



# Structural Mitigants

- Linking Tariffs to investment currencies (% in local currency/% in foreign currency)
  - Can be implemented as part of a tender structure, with bidders proposing balance of %s between local/foreign currency, potentially up to a cap
  - May lead to a multi-sourced financing (part local, part international)
  - But can cause tariffs for end-users to increase in the event of currency shifts
- Tariff adjustments linked to currency shifts
  - Rather than linking to investment/construction inputs, tariff has a built-in adjustment mechanism such that will increase in some percentage to offset currency swings (may not fully address the FX exposure, but lessen the exposure)
  - May be done through direct adjustment of tariff, or for example building up a reserve fund which is released upon currency shift triggers





# Structural Mitigants cont.

- Removing legal/regulatory bars requiring contracts to be in local currency
- “Rebalancing” of contracts, as provided in civil law jurisdictions
  - Usually not a feature under common law
- Government foreign currency indexed payments in PPPs
  
- Case study – Early Termination Guarantee



# Governmental Mitigants

- Fundamental questions, but can generally be addressed through diligence and regulatory framework (will depend jurisdiction by jurisdiction)
- Political risk insurance
- Bilateral Investment Treaties also give comfort on a macro level
- Location of accounts
- “Preferred creditor” status for multilaterals
- If government concession, may include a stabilization agreement or investment agreement
  
- Case study – Currency Inconvertibility Insurance



# Support for Local Institutions

- Support for local capital markets
  - Provide guarantees of infrastructure bonds in order to broaden the scope of potential investors, and can reduce the overall cost of the financing
  - Can be through gov't guarantees, or multilateral agencies, or export credit agencies
- Support from local government (development) banks
- Financing for local commercial banks from IFIs
  - Gives additional credit support to local institutions for on-lending (whether directly tied to the loan or not)
- Case study – Deductions of Adverse Impact of FX Variation



# Conclusion

