Project Financing

Capacity Development Program – SLAS Grade III Officers 2019

MODULE ON DEVELOPMENT-ORIENTED PROJECT FORMULATION

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Content:

- - Overview of project financing
- - Importance and role of project financing
- - Types of project financing structures (e.g., debt financing, equity financing,)
- Key stakeholders involved in project financing (e.g., lenders, investors, project sponsors)
- - Project financing process from inception to completion
- - Project appraisal and feasibility studies
- - Negotiation and structuring of financing agreements
- - Sources of project financing (e.g., commercial banks, development banks, capital markets)
- - Financial instruments used in project financing (e.g., loans, bonds, guarantees)
- - Government support and incentives for project financing
- - Challenges and considerations in project financing
- - Emerging trends and innovations in project financing

WHAT IS A PROJECT?

- A. Any task that has a beginning and an end
- (It is not a continuous process)

- B. Is a Process of carrying out works to achieve a task (Result)

- " Investment of capital in a time-bound intervention to achieve a goal/s or create productive assets"

- Effective management of projects is vital for the development of any economy because development itself is the effect of a series of successfully managed projects

Project Management - 03 things to manage –
" Investment of capital in a time-bound intervention to achieve a goal/s or create productive assets"

Performances/Scope) /to achieve a goal/s or Create productive assets



Time/
In a time-bound intervention

Cost/Budget/
Investment of capital

- Time - MUST BE ON TIME
- Cost/Budget - MUST BE UNDER BUDGET
- Performance - MUST MEET REQUIREMENTS

- To achieve the objectives of Time, Cost and Performance a project has to be properly planned, effectively implemented and professionally managed

FOR PROJECT FORMULATION AND IMPLEMENTTION : WHAT ARE THE NEEDS OR REQUIRMENTS ?

1. Well defined objectives (results)
2. Complex unique effort
3. Define time scale
4. **Cost & Resource budget**
5. **Financing Plan**
6. Temporary multi-disciplinary project team
7. Compromise between duration, cost & quality

Cost/Budget/Finances Involvement in Project Cycle

- Proposal - Study Phase
- Planning – Design Phase
- Start-up - Development Phase
- Execution – Implementation Phase and Monitoring and evaluation
- Closure – Project Completion Report

Definition of Project

- Organizations perform work continuously.
- Those include operations or projects though some works may overlap with each other.
- Projects are important elements of change. They are considered to be the leading edge of change in organization.
- A project consists of a combination of organizational resources pulled together to create something that did not previously exist and that will provide a performance capability.
- Projects support the ongoing activities of a going concern.

Projects Mainly two types

- Self Finance Project
- Sponsored / Donor Funded Projects

Finance System for Government Projects

- All government spending programs, including donor-funded projects, must be included in the central budget and have proper clearance from the DNP and the Cabinet of Ministers before funding sources are sought.
- All sums payable under agreements and guarantees are charged to the Consolidated Fund.
- Loan and grant agreements with foreign donors, are signed by the secretary of the Treasury on behalf of the government

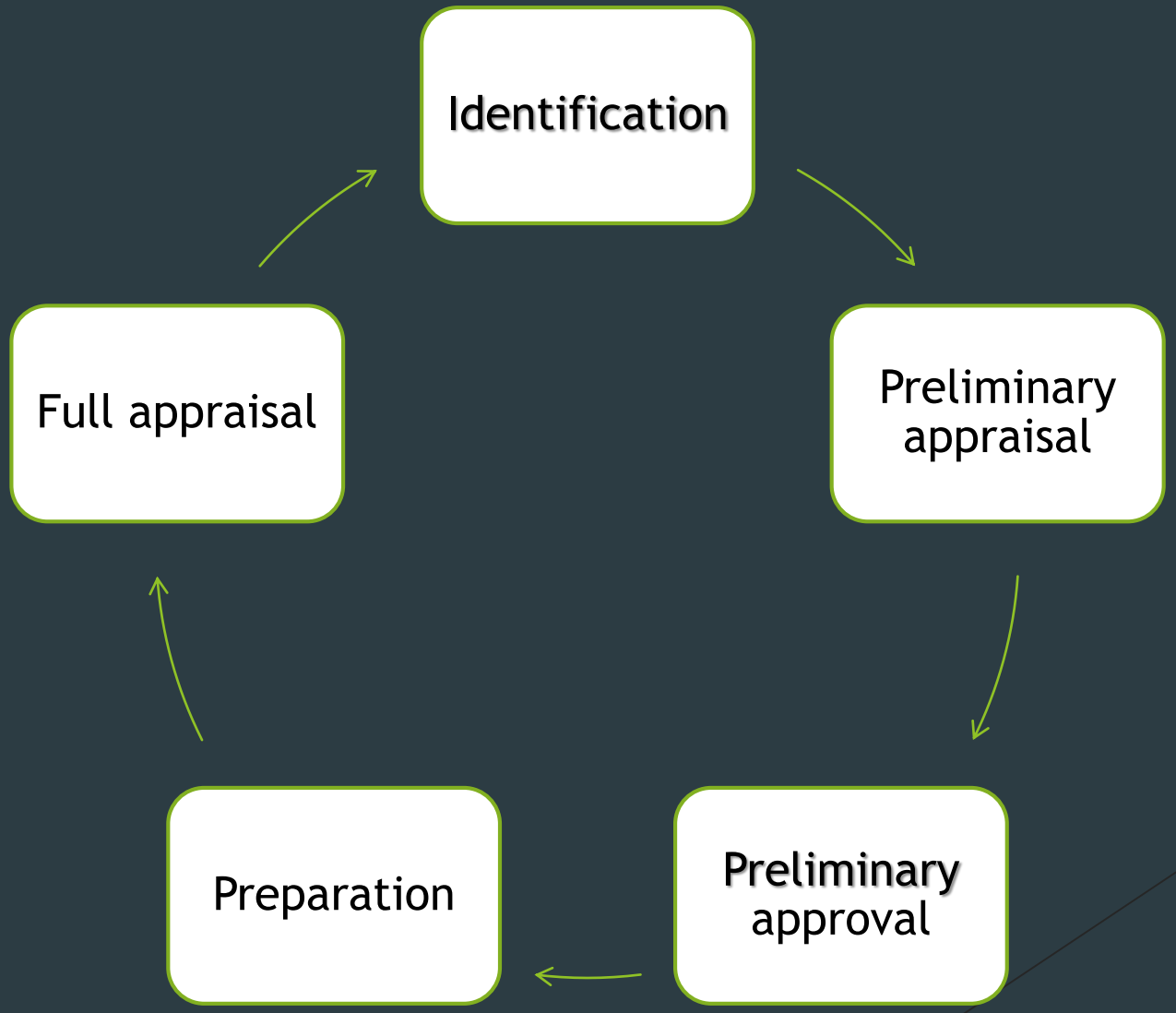
Government Project Finance System ….

- ERD is the government agency responsible for obtaining foreign assistance for development projects recommended by DNP; no other agency is authorized to deal directly with foreign donor agencies.
- The ERD channels potential projects into the lending pipeline of the various lending agencies during the annual consultations between the government and donors.
- Ministry of Finance Circular No. MoF/ERD/2014/1 notes that the assessment of foreign funding proposals for development projects is based not only on the financial terms but also on the expected use of the funds and the return on investment.

Government Project Finance System ….

- Foreign funding is to be mobilized mainly for large-scale strategic infrastructure development projects, particularly in energy, roads and highways, ports and aviation, and irrigation and water supply, to increase the return on investment
- On the other hand, official development assistance on concessionary terms will continue to be invested in soft sectors including health and education
- Foreign funds are not to be used for projects where funds can be allocated from the Consolidated Fund and where local expertise is available
- Based on Govt FR a project has to be approved following several steps

Project Planning Stages Based on Govt FR



Project Planning Stages …



Types of Foreign Aid

- Mainly Two Types:
- 1 Foreign Aid Grants
- 2 Foreign Aid Loans

- ***Classification of Foreign Aid:***
- Cash AID (Grant)
- Project Aid
- Commodity Aid
- Programme Aid
- Technical Assistances
- Balance of Payment Aid

Foreign funds classified according to funding source

- (i) foreign loans,
- (ii) foreign grants,
- (iii) reimbursable foreign loans,
- (iv) reimbursable foreign grants,
- (v) counterpart funds

Responsibility

- Any Foreign Aid comes in a form of an Agreement (Loan/Grant)
- All cash Grants should be credited to DST's Account
- All Commodity Aid should be accounted and inform the Treasury accordingly
- Provisions should be made in the annual Estimates before meeting expenditure
- Foreign Aid for any Board or Corporation should be provided under the line ministry

Why we Need a Project Budget

- The budget is the engine that drives your project's funding. It communicates to stakeholders how much money is needed and when it's needed.
- But it's not only a means to get things that your project requires. you need to pay teams, buy or rent equipment and materials, but that's only half the story.
- The other part of the importance of a project budget is that it's an instrument to control project costs. The budget is your plan, which acts as a baseline to measure your performance as you collect the actual costs once the project has been started.

Project Financing

- Project finance is analysis of the complete life-cycle of a project.
- Typically a cost-benefit analysis is used to determine if the economic benefits of a project are larger than the economic costs.
- The analysis is particularly important for long-term projects
- The first step of the analysis is to determine the Financial Structure a mixture of debt and equity , that will be used to finance the project.

What Is Project Finance?

- Project finance is the funding of long-term infrastructure, industrial projects, and public services using a non-recourse or limited recourse financial structure.
- The debt and equity used to finance the project are paid back from the cash flow generated by the project.

- Project finance is especially attractive to the private sector because companies can fund major projects off-balance sheet (OBS)

common sponsors of project finance

- **Contractor Sponsors:** These sponsors provide subordinated or unsecured debt and/or equity. They are key to the establishment and operation of business units.
- **Financial Sponsors:** These sponsors include investors and are usually in the pursuit of a big return on their investment.
- **Industrial Sponsors:** These sponsors generally believe that the project is related to their own businesses.
- **Public Sponsors:** These sponsors include governments from various levels.

The project finance structure

- The project finance structure for a build, operate, and transfer (BOT) project includes multiple key elements. Project finance for BOT projects generally includes an SPV. The company's sole activity is carrying out the project by subcontracting most aspects through construction and operations contracts. Because there is no revenue stream during the construction phase of new-build projects, debt service only occurs during the operations phase.
- For this reason, parties take significant risks during the construction phase.
- There is limited or no recourse to the project's sponsors, company shareholders are typically liable up to the extent of their shareholdings.
- The project remains off-balance-sheet for the sponsors and for the government.
- Not all infrastructure investments are funded with project finance. Many companies issue traditional debt or equity in order to undertake such projects.

Project Finance vs. Corporate Finance

- Project and corporate finance are very important concepts in the world of financing. Both of these funding methods rely on debt and equity in order to help businesses reach their financing goals. Having said that, they are very distinct.
- Project finance can be very capital-intensive and risky and relies on the project's cash flow for repayment in the future. Corporate finance, on the other hand, is focused on boosting shareholder value through various strategies like the investment of capital and taxation. Unlike project financing, shareholders receive an ownership stake in the company with corporate financing.

Risks Associated With Project Finance

- Some of the risks associated with project finance include volume, financial, and operational risk.
- Volume risk can be attributed to supply or consumption changes, competition, or changes in output prices.
- Inflation, foreign exchange, and interest rates often lead to financial risk.
- Operational risk is often defined by a company's operating performance, the cost of raw materials, and the cost of maintenance, among others.

Why Use Project Finance

- Project finance is a way for companies to fund long-term projects.
- This form of financing uses a non- or limited recourse financial structure.
- Firms with weak balance sheets are more apt to use project finance to meet their funding needs rather than trying to raise capital on their own.
- This is especially true for smaller companies and startups that have large-scale projects on the horizon.
- Companies need capital in order to begin and grow their operations. One of the ways that certain companies can do so is through project financing.
- This form of funding allows businesses that may not have a strong financial history to raise capital for larger, long-term projects.
- Sponsors, which invest in these projects, are paid using cash flows from the project. This is unlike corporate finance, which is less risky and concentrates on maximizing shareholder value.

Stages in Project Financing

- Pre Financing stage
- 1. Risk identification and minimizing
- 2. Technical and Financial feasiability
- 3. Negotiation
- Financing stage
- 1. Commitments and documentation
- 2. Disbursements
- 3. Monitoring and review
- Post financing stage
- 1. Financial closure
- 2. Project closure
- 3. Repayment and subsequent monitoring

Methods of Project Financing

- There are 3 methods
- 1. Cost share Financing or low interest loan financing
- 2. Debts Financing
- 3. Equity Financing
- The key to any project finance is to use a right mix of debt and equity. It is important that due care is taken in drafting the documents .

Project Funding / Finding Donors

Available options are;;

Grants

Partnerships

Borrowing money

Investors

Donations

Crowd funding

Growing revenue and and

Selling up

Project Funding / Finding Donors …..

A grant is a sum of money given by a government or other organization for a particular purpose.

Partnerships can help manage costs by sharing buildings, equipment, expertise and workloads.

Borrowing money can be an option if your project can repay the loan.

Investors are looking for opportunities to put their funds into, providing this private equity returns a profit.

Project Funding

"IT'S THE INVESTOR'S MONEY, NOT YOURS. DON'T GO LOOKING FOR FUNDING WITH A SENSE OF ENTITLEMENT"

Important Factors for Project Financing :

- Project's Financing Plan
- Who contributes?
- What % ?
- For What Component ?
- Total Work Plan
- Annual Work plan
- Total Budget for the Project
- Annual Budget and Action Plan

Q & A

Thank You