

Negotiating With Chinese Lenders

by Magnus Rodrigues, in London

Chinese lenders are emerging as a major source of funding in international project finance transactions.

Developers in various sectors in Asia, Africa, Australasia, the Middle East, Europe and the Americas now routinely consider the option of using Chinese equipment with financing from Chinese lenders.

The most active Chinese lenders in financing projects outside China historically have been the Export-Import Bank of China and China Development Bank. In 2009 and 2010, these two institutions lent at least US\$110 billion to developing countries, which was more than the World Bank. Both are state-owned policy banks indirectly focused on funding projects outside China. Policy banks were established to pursue macro policies of the Chinese government. However, China Development Bank is in the process of changing from a policy bank to a commercial bank.

Various other Chinese commercial banks have financed or considered financing international projects. The four largest Chinese commercial banks — the Bank of China, Industrial and Commercial Bank of China, China Construction Bank and Agricultural Bank of China — are now four of the seven largest banks in the world by market capitalization.

Although the structure of Chinese banking is evolving and each Chinese lender has its own traits, there remains a high degree of uniformity in the approach of Chinese lenders.

Practical Considerations

Due to the very large size of Chinese lenders and because their networks are spread over a considerable area even within China, work on project finance transactions is conducted by various branches of each Chinese lender. Where a Chinese lender is providing an export credit facility to facilitate sale of Chinese goods in a project finance transaction, the branch of the Chinese lender involved will typically be the one that works most closely with the relevant Chinese vendor that is supplying the goods. This has the advantage that the branch will understand the relevant sector in which the Chinese vendor operates very well, but there is no one central team within the larger institution that acts as an experienced project finance desk.

The branch may be more familiar with financing of projects within China where some practices are very different. For instance, it is not unusual for Chinese lenders to require a completion guarantee for financings in China. More time may have to be spent with Chinese lenders — including time on the ground in China — educating them than with other international lenders.

The approval process for Chinese lenders can be more time consuming and structured than for other international commercial lenders. For instance, the Export-Import Bank of China and China Development Bank are usually only able to complete their final approval processes when all the contracts have been agreed. This means that the financing agreements will not be able to be signed as soon as they are agreed. Chinese lenders will usually have the benefit of a Sinasure insurance policy in international projects where Chinese lenders are financing the purchase of equipment or other goods from Chinese manufacturers. Sinasure, which is short for China Export & Credit Insurance Corporation, is China's policy-oriented insurance company specializing in export credit insurance.

Larger Sinasure transactions require the approval of the State Council, which is the executive arm of the Chinese government. This can potentially take a number of months.

The policies of the Chinese central bank — called the People's Bank of China — remain of central importance for Chinese lenders. This is not necessarily a negative influence at present. The People's Bank of China remains supportive of Chinese lenders lending overseas. The policies of central banks in many developed countries, such as implementation of Basel III, are forcing many western banks to reduce their lending.

Types of Projects Financed

Since the 1990s, projects have been financed within China across a range of sectors. The sectors include power, transportation, and mining and metals projects.

The first wave of Chinese lending outside China by Chinese policy institutions — the Export-Import Bank of China and China Development Bank — reflected Chinese government policy of using economic assistance as a / continued page 2

Chinese Lenders

continued from page 1

key foreign policy tool. For instance, during 2009, China EXIM and China Development Bank provided US\$60 billion facilities for oil to Kazakhstan, Turkmenistan, Russia and Venezuela that furthered the Chinese government's aim of securing supplies of vital natural resources for the resource-hungry Chinese economy.

With Chinese lender entrance into the broader project finance market, Chinese lenders have been prepared to consider financing projects in developed countries as well as emerging market countries, including India, The Philippines, Oman, Botswana, Saudi Arabia, Turkey and Guyana.

Chinese lenders are prepared to lend much higher amounts to a wider range of countries than other international lenders: this difference is most marked with regard to various emerging markets.

For instance, China Minsheng Banking Corporation, which is a large commercial Chinese bank, earlier this year offered to provide a project finance facility for the development of a US\$600 million alumina facility in Laos. This alumina facility is being developed by a joint venture of Orde River Resources of Australia and Non-Ferrous Metal Industry's Foreign Engineering & Construction of China.

The project finance structures in which Chinese lenders are prepared to lend has significantly evolved during the last few years. Initially and for many years, Chinese lenders focused on lending to projects in China where the sponsors and other parties would be all Chinese or a mixture of Chinese and non-Chinese parties.

When Chinese lenders started to lend outside China, their initial focus was financing projects where most of the key parties were Chinese, but this has since evolved so they will now lend to projects where even only one party is Chinese (for example, where equipment is supplied by a Chinese vendor or there is a Chinese investor).

More recently, they have been prepared to contemplate lending to projects where none of the parties is Chinese. For instance, the Nakilat Phase III LNG project sponsored by Qatar Gas Transport required US\$949 million in debt facilities for construction of 25 ocean vessels specially designed to transport LNG from Qatar's North Field. Bank of China and China EXIM each provided a US\$200 million facility as part of the US\$949 million facilities. There are no Chinese sponsors, vendors or offtakers (although, like many others, Chinese parties do purchase LNG from Qatar).

However, it will remain an anomaly to see Chinese banks

financing deals in which there is no other tie to China. For instance, at the end of 2010, CLP successfully refinanced US\$288 million of the debt for the 1,320-megawatt Jhajjar coal-fired power project in India. This involved replacing some of the debt that was to be provided by Indian lenders with a Sinosure-backed export credit facility provided by China EXIM and China Development Bank together with another facility provided by other international commercial lenders. In this project, the construction contractor is the Chinese company, Shandong Electric.

Diligence by Chinese lenders can take longer than for other lenders if the Chinese lenders have limited experience with the type of project.

Financing Terms

The availability of project finance facilities from international commercial lenders remains different from what it was before the financial crisis in the fall 2008.

In contrast, Chinese lenders continue to have the ability to provide very large facilities and are, therefore, able to fund deals alone or with a very small number of other lenders. This is a very important advantage in dealing with them, and avoids the protracted and often difficult nature of a club or syndicated financing.

When lending outside China, Chinese lenders will generally expect their facility agreements to be governed by English law and the terms, and conditions of such facility agreements usually follow market practice within the London banking market.

One benchmark with which Chinese lenders are comfortable is the template financing agreements prepared by the Loan Market Association in London. These forms of agreements have been prepared taking into account the views of key parties involved in the London banking market in a manner that is meant to balance the interests of borrowers and lenders.

Chinese lenders are subject to the policies of the People's Bank of China as well as, to a degree, those of other parts of Chinese government. Compared to controls on international lenders in Europe and the United States, those in China are stronger overall. Indeed they may be more analogous to those in other emerging markets. For example, the Reserve Bank of India imposes various controls on the operation of Indian banks. To provide an illustration of such policies, recently the People's Bank of China has started to promote lending in renminbi outside China, and this practice is likely to become more important as the ongoing re-evaluation of / *continued page 3*

Chinese Lenders

continued from page 2

the US dollar and other major currencies continues.

Where the financing is linked to a Chinese equipment supply or other contracts, the terms of the financing will usually include certain terms that reflect this position. For instance, these terms may include a cap tied to the percentage of the Chinese goods that will be financed with the loan facility.

Chinese lenders often have a different risk perspective from other international lenders when considering projects. As a result, they can be more open to accepting solutions that would be more difficult for other international lenders to

accept. For instance, on a recent bid for a North African power project, the European sponsors spent many months making limited progress negotiating with European banks, which were concerned about certain of the commercial aspects of the project. Finally the sponsors gave up and turned to Chinese lenders that agreed to provide financing in a matter of weeks, thereby enabling the sponsors to submit a bid in time. ☺

November 2011