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Satellite Project Finance : The pivotal role of insurance

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Project Finance makes a comeback…

Satellite debt deals closed or to be closed in 2007-9

- Al-Yah Satellite Company (Project Finance)
- ABS (potential Project/Export Finance hybrid)
- O3b Networks (Project Finance)
- Globalstar (Project/Export Finance)
- New Dawn (Project Finance)
- Indosat Palapa-D (Export Finance)
- Nilesat (Export Finance)

As Corporates show increasing propensity to fail, trend towards asset-based financing grows

But what is Project Finance ?

- A form of lending which can be applied to a wide range of industries and involves the financing of a single major capital investment

- For repayment, lenders rely (either largely or exclusively) on the cash flow and assets of the project, with such debt facilities being "limited" or "non-recourse" to the shareholders

- Project finance facilities are sometimes extended to an SPV (a project company) established by the project sponsors solely to own and operate the project, although in telecoms and satellite, the corporate itself often becomes the project

- Project finance also enables <u>structured, leveraged lending</u>, with gearing (the ratio of debt to equity) ranging typically between 50:50 and 85:15, with the relative balance depending on the <u>project's economics and risk sharing</u> between shareholders and lenders

Project Finance main characteristics…

- High up front capex to fund asset that will generate strong long-term revenues once operational
- Clear understanding and mitigation of major project risks (e.g. construction, technical, regulatory /legal, and in particular, market risk)
- Typical project financing would incorporate mechanisms such as the following:
  - Financial covenants in place that remain robust even in 'downside' cases
  - Ownership covenants, no distributions to shareholders prior to first repayment and distribution 'lock-up' when financial covenants breach pre-agreed thresholds
  - Debt Service Reserve Account ("DSRA") to be funded with the next 6 months debt service, 6 months prior to first repayment.
  - "Cash-sweep" mechanism
- Typical security package, e.g., pledges over assets (tangible & intangible), project agreements, regulatory licenses, bank accounts and over shares

With no or limited recourse to shareholders, banks rely on the project alone to repay debt

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Extensive risk analysis and due diligence required…

Given project finance is limited or non-recourse lending, extensive risk analysis and due diligence is required to close a project financing.

- Sponsor / developer motivation (project's link to core business)
- Industry analysis (in market risk transactions)
- Counterparty credit analysis (e.g. contractors, customers)
- Financial analysis (cash flow analysis mostly for debt service purposes)
- Legal due diligence (international and local) covering:
    - Underlying commercial agreements
    - Drafting and negotiation of Financing Documents (loan, intercreditor agreement and security package)
- Independent Consultants' reports:
    - Industry specific (e.g. transponder demand, trends in uses of satellites, by region)
    - Technical (crucial - underlying assets), environmental (Equator Principles)
    - And last but by no means least….**INSURANCE**

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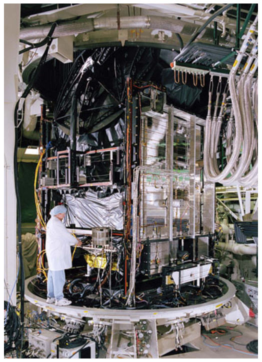
The pivotal role of Insurance

For construction



For delivery delays

For Launch failures

For in-orbit failures

Insurance and ability to access proceeds is a critical part of risk mitigation for lenders

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Typical "PF" Lenders insurance requirements

Finance documentation will typically require:

- The Borrower is the insured party, but…

- the Senior Lenders are 'additional insured'

- The Loss Payee will be the security agent, acting on behalf of the senior lenders, to ensure proceeds can flow to repay banks ahead of other creditors or shareholders

- Policies are at least 12 month in duration for most insurances

- Failure to maintain material insurances, would be an event of default, but also permit the Lenders' agent to procure the insurances on behalf of the Borrower and seek reimbursement

To ensure Lenders get want they need…

…and to facilitate securing the necessary financing, PF Borrowers should consider

- Engaging a Lenders Insurance Advisor (“LIA”) early in the process to

  - prepare a report for lenders to use to secure credit approvals
  - assist mandated banks in getting comfortable with insurance strategy of Borrower
  - Provide comfort to lenders that this strategy is ‘seamless’

- Involving the LIA in the discussions around risk mitigation and insurance strategy, together with the Borrower’s insurance broker

So… to conclude…

- PF is one of those financing products that is deliverable today
- Insurance plays a pivotal role in that deliverability
- Operators, suppliers, insurers, advisors and lenders can all work towards an optimal solution for all parties

Thank You

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