Supporting the development of infrastructure

## Research & Analysis

# IJ first half review: Equator Principles financing

17 August 2006

**A study conducted by IJ Research & Analysis reveals that Equator Principle banks have underwritten US$10bn in project financing debt in non-and-low-income OECD countries (emerging markets), representing 34 per cent market share - write Vander Caceres and Simon Ellis.**

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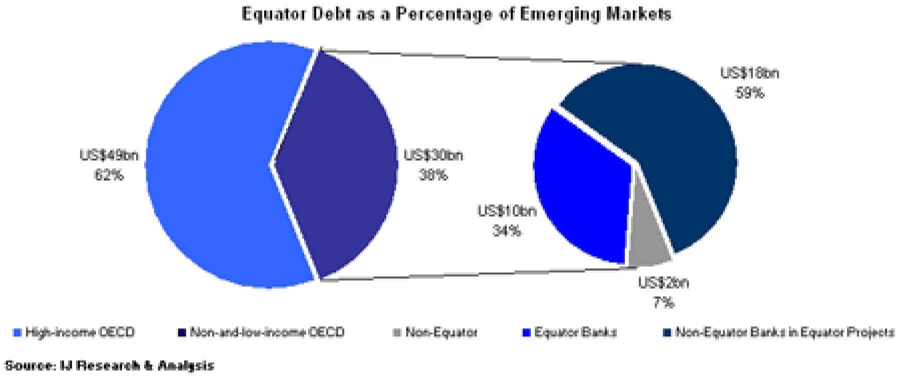



The research demonstrates that Equator banks have achieved a substantial leveraging effect by co-financing projects with non-signatories.

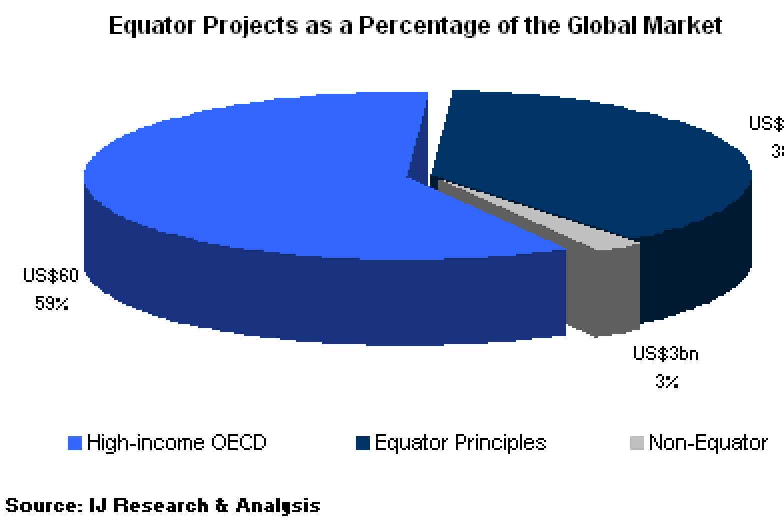
'The Equator banks have leveraged financing for emerging markets by US$18 billion from non-Equator banks' says Jon Williams Head of Group Sustainable Development at HSBC.

The report shows that non-signatories underwrote 59 per cent of emerging markets project finance within Equator-compliant deals, while a further seven per cent of debt was raised in non-compliant projects.

The total debt amount for Equator Principle debt financing in emerging markets was US$28 billion or 93 per cent of the market.

As Maria Cull, a consultant with Hebert Smith's environmental law practice, puts it 'most of the project financing is being carried out in some form or another under Equator bank Principles'.

Overall, Equator Principle-compliant projects in emerging markets accounted for 38% of global project finance with US$38bn.  Only 3 per cent of projects were non-compliant.




### Methodology - Changes to the conventional wisdom

Our figures show that Equator banks have underwritten US$10 billion worth of debt or 34 per cent of project finance debt as opposed to the 80 per cent figure widely quoted.

The difference is that our figures were based on emerging market debt and not on global project value.

Jon Williams from HSBC says that our research 'has been conducted in accordance to the Principles'.

Non-Equator banks arranged US$18 billion in debt for Equator-compliant projects (where at least one mandated lead arranger is an Equator bank).

Therefore the total debt amount for Equator Principles debt financing in emerging markets was US$28 billion or 93 per cent of the market.

In conclusion, most of the project financing is being carried out in some form or another under Equator bank Principles.

IJ Research & Analysis has compiled data for Equator Principle-compliant projects and debt financing based on submissions sent by banks, advisers and sponsors and from our own research.

Only projects financed by loans and/or bonds structured on a limited or non-recourse project finance basis were eligible.

We split our global project finance database into two regions: High Income OECD and Non-and-Low Income OECD (emerging markets).

Then we applied the Principles to emerging markets in compliance with the Statement of Principles signed on 4 June 2003. A summary of the Principle is provided below:

- Only projects with a total capital cost of US$50 million or more are eligible.
- Project risk is categorised in accordance to IFC environmental and social criteria. Category A, B or C.
- The borrower or issuer has completed an Environmental Assessment (EA) for all Category A and Category B projects.
- The EA has addressed compliance with applicable host country laws, regulations and permits required by the project.
- As necessary, lenders have appointed an independent environmental expert to provide additional monitoring and reporting services.

Deals involving state-owned banks and/or multilaterals were also eligible only if the project was co-financed by at least one Equator bank.

We excluded deals in trade & export finance, agriculture, aviation financing, real estate, manufacturing and shipping.

## Top Equator Principles MLAs

Twenty-two of the 41 Equator banks closed 99 project finance debt tranches in the first half of 2006 and Citigroup was the top arranger with US$1.2 billion worth of debt capturing 12.2 per cent of the market.

HSBC followed closely with US$1.02 billion and a market share of 10.1 per cent. The bank adopted the principles in September 2003 and quickly positioned itself as one of the most influential institutions.

'We have trained hundreds of our staff in the project & export finance department on the Equator Principles' says Jon Williams Head of Group Sustainable Development at HSBC.

With more than 11,000 correspondent banks worldwide the potential for influencing others institutions to adopt the principles and the room for market growth are there.

**Top Project Finance Equator Banks H1 2006**

| Rank | Bank | Underwritten Debt US$m | No of Deals | Market Share % |
|---|---|---|---|---|
| 1 | Citigroup | 1,227.95 | 10 | 12.18 |
| 2 | HSBC | 1,018.49 | 9 | 10.10 |
| 3 | WestLB | 847.73 | 8 | 8.41 |
| 4 | ING | 794.13 | 8 | 7.88 |
| 5 | Standard Chartered Bank | 788.52 | 8 | 7.82 |
| 6 | Mizuho Financial Group | 756.11 | 7 | 7.50 |
| 7 | SMBC | 746.66 | 7 | 7.40 |
| 8 | Calyon | 643.58 | 9 | 6.38 |
| 9 | Royal Bank of Scotland | 545.81 | 5 | 5.41 |
| 10 | BOTM | 527.20 | 5 | 5.23 |
| 11 | BBVA | 481.78 | 6 | 4.78 |
| 12 | Credit Suisse | 400.00 | 2 | 3.97 |
| 13 | ABN Amro | 316.39 | 4 | 3.14 |
| 14 | Dexia Group | 256.00 | 1 | 2.54 |
| 15 | European Investment Bank | 242.00 | 1 | 2.40 |
| 16 | Fortis Bank | 174.28 | 2 | 1.73 |
| 17 | KBC Bank | 76.00 | 1 | 0.75 |
| 18 | Banca Intesa | 68.75 | 1 | 0.68 |
| 19 | Gruppo Sanpaolo IMI | 68.75 | 1 | 0.68 |
| 20 | International Finance Corp | 62.50 | 2 | 0.62 |
| 21 | Nedbank Capital | 23.66 | 1 | 0.23 |
| 22 | Unibanco | 17.84 | 1 | 0.18 |
| | Total | 10,084.13 | 99 | 100.00 |

Source: IJ Research & Analysis

Individually banks have launched a number of alternative ways of meeting environmental and social objectives.

Citigroup has independently enacted a reporting scheme for its thermal power projects, Goldman Sachs has launched a comprehensive environmental policy and several banks including HSBC, RBS and ABN AMRO have set up separate Sustainable Development desks.

The Equator banks were most active in the Petrochemicals sector, where they arranged US$3.7 billion worth of debt in a total of 38 tranches.

PetroRabigh was the largest Petrochemical deal valued at US$9.8 billion. A mixed-syndicate of 25 Equator and non-Equator banks lead arranged a total debt package of US$ 5.8 billion.

Power was the second largest sector with US$2.2 billion and 22 tranches, followed by Transport and Oil & Gas with US$1.9 billion and US$1.5 billion respectively.

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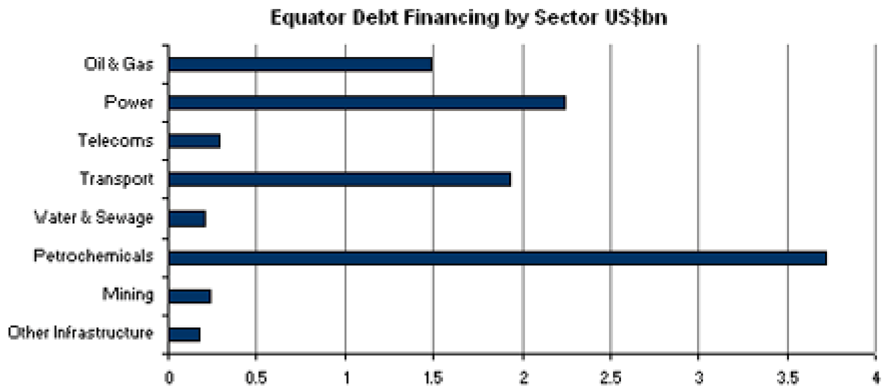


Source: IJ Reasearch & Analysis

Non-Equator banks which co-financed Equator-compliant projects underwrote 57 per cent more than the Equator banks.

JBIC came on the top of the table with seven tranches worth US$4.7 billion. The bank closed deals mainly in Asia but also in the Middle East and South America.

Along with most multilaterals and ECAs, the bank has its own environmental and social guidelines which are widely regarded as comparable to the IFC and Equator standards.

Masashi Watanabe from JBIC's Planning and Coordination Division expects more cooperation with Equator banks in the future and by applying the bank's own environmental guidelines in parallel to the Equator Principles, they hope to bring added value to projects.

Saudi Arabia's Public Investment Fund was the second largest non-Equator bank with a combined total debt of US$2.6 billion for the SHARQ, Yansab and PetroRabigh petrochemical complexes.

| Top Non-Equator Banks in Equator Projects H1 2006 | | | | |
|---|---|---|---|---|
| Rank | Bank | Underwritten Debt US$m | No of Deals | Market Share % |
| 1 | JBIC | 4,735.00 | 7 | 26.87 |
| 2 | Public Investment Fund | 2,547.00 | 3 | 14.45 |
| 3 | BNP Paribas | 890.95 | 7 | 5.06 |
| 4 | Societe Generale | 877.22 | 9 | 4.98 |
| 5 | Gulf International Bank | 696.58 | 7 | 3.95 |
| 6 | Saudi Hollandi Bank | 646.53 | 3 | 3.67 |
| 7 | Islamic Development Bank | 605.53 | 3 | 3.44 |
| 8 | Apicorp | 521.28 | 5 | 2.96 |
| 9 | Saudi British Bank | 404.91 | 4 | 2.30 |
| 10 | Grupo Santander | 309.79 | 6 | 1.76 |
| 11 | KfW | 263.58 | 2 | 1.50 |
| 12 | Bank of China | 253.78 | 2 | 1.44 |
| 13 | Banque Saudi Fransi | 224.38 | 2 | 1.27 |
| 14 | Saudi American Bank | 213.91 | 2 | 1.21 |
| 15 | Qatar National Bank | 205.22 | 3 | 1.16 |
| 16 | China Development Bank | 205.00 | 1 | 1.16 |
| 17 | China Exim Bank | 200.00 | 1 | 1.13 |
| 18 | Eximbank of Korea | 200.00 | 1 | 1.13 |
| 19 | Riyad Bank | 191.00 | 2 | 1.08 |
| 20 | DZ Bank | 179.86 | 2 | 1.02 |
| 21 | DBS Bank | 178.78 | 1 | 1.01 |
| 22 | HKSAR Government | 178.78 | 1 | 1.01 |
| 23 | Dubai Islamic Bank | 166.66 | 2 | 0.95 |
| 24 | Morgan Stanley | 162.00 | 1 | 0.92 |
| 25 | Natexis Banques Populaires | 159.75 | 2 | 0.91 |
| 26 | BayernLB | 144.75 | 2 | 0.82 |
| 27 | China Construction Bank | 144.00 | 1 | 0.82 |
| 28 | Arab Bank | 124.30 | 2 | 0.71 |
| 29 | Mashreqbank | 124.30 | 2 | 0.71 |
| 30 | Sumitomo Trust & Banking | 116.00 | 1 | 0.66 |
| 31 | DnB Norbank | 113.75 | 1 | 0.65 |
| 32 | Krung Bank | 111.20 | 1 | 0.63 |
| 33 | Depfa Bank | 111.11 | 1 | 0.63 |
| 34 | Deutsche Bank | 111.11 | 1 | 0.63 |
| 35 | Development Bank of Singapo | 111.11 | 1 | 0.63 |
| 36 | Arab Banking Corp | 105.53 | 1 | 0.60 |
| 37 | Comercial Bank of Qatar | 80.92 | 1 | 0.46 |
| 38 | Agriculture Bank of China | 76.00 | 1 | 0.43 |
| 39 | Bank Albilad | 75.00 | 1 | 0.43 |
| 40 | ABC International Bank | 68.75 | 1 | 0.39 |
| 41 | Banca Nazionale del Lavoro | 68.75 | 1 | 0.39 |
| 42 | EDC | 68.75 | 1 | 0.39 |
| 43 | Hypo-bank | 68.75 | 1 | 0.39 |
| 44 | National Bank of Greece | 68.75 | 1 | 0.39 |
| 45 | National Bank of Kuwait | 68.75 | 1 | 0.39 |
| 46 | SG Warburg | 68.75 | 1 | 0.39 |
| 47 | Vakifbank | 68.64 | 1 | 0.39 |
| 48 | Bangkok Bank | 55.60 | 1 | 0.32 |
| 49 | Bank of Bahrain & Kuwait | 55.55 | 1 | 0.32 |
| 50 | Emirates Bank International | 55.55 | 1 | 0.32 |
| 51 | Commercial International Banl | 35.00 | 1 | 0.20 |
| 52 | National Bank of Egypt | 35.00 | 1 | 0.20 |
| 53 | BNDES | 31.00 | 1 | 0.18 |
| 54 | Standard Bank | 23.66 | 1 | 0.13 |
| 55 | Caixa Banco de Investimento | 15.00 | 1 | 0.09 |
| | Total | 17,622.82 | 112 | 100.00 |
| Source: IJ Research & Analysis | | | | |

## The view from the NGOs

Despite the wide coverage of Equator Principles in emerging markets, NGOs which monitor the Equator Banks continue to raise criticisms about the transparency of the process and the deals receiving finance.

Johan Frijns of monitoring body Banktrack claims, 'It has not yet been proven on a generalised basis that the EPs are making a difference to communities on the ground. Today, EP banks still are involved in environmentally and socially harmful projects.'

Frijns cites the pulp mill project in Uruguay proposed by Finnish developer Botnia, where Equator signatories Calyon and BBVA are MLAs. ING withdrew from its advisory and MLA role in the deal in April - without citing the Principles.

'The Botnia deal is clearly in violation of some of the principles,' says Frijns, 'No consultation took place with stakeholders in the communities down river of the pulp mill in Uruguay and Argentina.'

Frijns also believes the Sakhalin II project to be in breach of the Equator Principles' environmental guidelines, although bankers stress the cost and delays accrued by the Shell consortium in the rerouting of a pipeline route to avoid damaging the habitat of the endangered Western Grey Whale.

Lucie Giraud, spokesperson for environmental and social issues at the IFC rejects the idea that it is possible to gauge the success of the Principles by looking at individual projects.

'The purpose of IFC's standards and the Equator Principles is not to avoid difficult projects' she says, 'but rather to enable client companies to successfully tackle the environmental and social issues arising from these projects.'

## Conclusion

IJ research reveals that EP banks' involvement in the emerging markets is creating a sizeable umbrella which is covering the lending activities of non-Equator lenders.

Equator principles have taken some time to be incorporated into the banks' internal practices, hence the slow uptake of the principles by regional and local banks. In this regard Equator banks are playing a key in bringing these institutions as correspondent and relationship banks.

Before serious discussion can start about Equator Principles III, banks are focusing on implementing Equator Principles II which according to one banker will take at least 24 months. In the meantime there is likely to be more convergence of environmental and social standards between signatory and non-signatory banks.

In the longer term, there is hope that as project financing grows in geographical and sectorial spread Equator Principles will follow suit.

According to Charles July, a project finance partner at Freshfields, 'The hybridisation of infrastructure financing is likely to mean that the Equator Principles move beyond project finance into other asset classes'.

Wider uptake of the principles is unlikely to silence the NGOs which focus on accountability, but there is now a broader platform for discussion.

Another challenge will be to secure agreement and standardisation of procedures among an ever growing membership.

As one banker said, 'It was a smoother decision making process when we were just 10 banks, now that are we are 41 it is much more challenging.'