Market Intelligence

PROJECT FINANCE 2021

Global interview panel led by Milbank

LEXOLOGY® Getting The Deal Through

LEXOLOGY
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Project Finance 2021

Africa Overview

Yves Baratte is a partner based in Simmons & Simmons' Paris office where he leads the energy, natural resources and infrastructure team. Yves advises international corporate clients, governments and financial investors on complex power, water, mining and infrastructure projects, particularly those in Africa. Yves has advised on the consortium bidding for the Inga 3 hydro power project in the Democratic Republic of Congo, one of Africa's largest projects, and was ranked among the three most active lawyers working in Francophone Africa by *Jeune Afrique* magazine, 201820.

Tina Blazquez-Lopez is head of energy and infrastructure for the Middle East and Africa and is based in Simmons & Simmons Dubai office. She is also co-head of the firm's Africa practice. Tina has spent over 15 years advising governments, lenders, sponsors, borrowers and equity investors on the acquisition, development and financing of complex projects throughout the world, with a focus on emerging markets and Africa in particular. Many of her transactions have been the 'first in kind' or have been named 'Deal of the Year' by leading industry journals. Tina is a fluent Spanish speaker.

Mathilde de Brugerolles, who has been qualified in France since 2011, is a supervising managing associate working within our energy and infrastructure team in Paris. She joined the group in September 2015. Her practice focuses primarily on general corporate and commercial, project development and other matters in the energy and natural resources sectors in particular Francophone Africa. French is her first language but she also speaks English and basic Spanish.

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1 What have been the trends over the past year or so in terms of deal activity in the project finance sector in your jurisdiction?

Yves Baratte: Although the level and the pace of development are still insufficient for the needs of African countries, we have seen strong activity in the infrastructure sector in 2020 in francophone Africa – in particular in the transport sector, with progress on projects for the construction or rehabilitation of ports, airports and railway infrastructure. This has been especially widespread in West Africa with, for example, port projects in the Republic of Guinea to service the booming bauxite projects to East Africa, and the numerous port, road and railway projects in Djibouti.

The pace of development of renewable projects seems to have accelerated with the launch of new tender processes in the solar and wind sectors in a number of countries, including Morocco, Tunisia and Burkina Faso, and with full commercial operation being reached for several projects. In early 2020, the Moroccan Agency for Sustainable Energy put out a tender for the first phase of the 400MW Noor PV II solar project. Morocco plans to increase the share of renewables in its installed power generation mix to 42 per cent by next year and to 52 per cent by 2030.

In contrast, we have seen relatively low levels of activity in the oil and gas industry, despite the massive gas discoveries of the recent years, such as the Grand Tortue deep offshore project in Mauritania and Senegal, but the development of such huge projects is complex and slow.

Mathilde de Brugerolles: Almost all commodity prices saw steep declines early and mid-2020 as the covid-19 pandemic took hold. Weak economic growth also reduced the overall demand for commodities. However, according to the World Bank's October 2020 Commodity Markets Outlook, almost all commodity prices recovered in the third quarter of 2020 following the early declines. Crude oil prices had doubled since April in response to supply cuts, although they remained much lower than their pre-pandemic levels. Metal prices also recovered quickly due to a number of factors, including a faster-than-expected recovery in China. An increase in the price of copper should maintain high levels of interest for the Democratic Republic of Congo or Zambia.

In April 2020, oil fell to below zero for the first time. This followed an historic glut and a shortage in storage facilities across the world. Usually, when there is an oil surplus, demand tends to increase due to lower costs. However, as a result of covid-19 restrictions and lockdown measures, demand for oil was low. Oil prices are expected to average US$44 per barrel of oil in 2021, which is up from an estimated US$41 per barrel of oil in 2020. Metal and agricultural prices are also projected to see modest gains of 2 per cent and 1 per cent, respectively, in 2021.

Yves Baratte

Tina Blazquez-Lopez

Mathilde de Brugerolles

> "Almost all commodity prices recovered in the third quarter of 2020 following the early declines."

Tina Blazquez-Lopez: Low oil prices is of particular concern to African countries such as Nigeria, Ghana, Angola, Algeria, Gabon, Equatorial Guinea and Libya whose budgets are heavily reliant on oil. Any significant decline in income will inevitably impact government investment and spending plans for infrastructure projects.

While the outbreak of covid-19 slowed down deal activity in some sectors and jurisdictions, other deals continued to progress towards financial close. This included the US$296 million Beitbridge Border Post Upgrade public–private partnership (PPP) in Zimbabwe, which has US$222 million debt from commercial lenders and two development finance institutions. In South Africa, we also saw the conclusion of financing for some of the Round 4 Renewable Energy Independent Power Producer Procurement Programme deals. Also of note, in Kenya, Tullow Kenya, together with its Joint Venture Partners Total and Africa Oil, confirmed the end of the Early Oil Pilot Scheme contract on 2 June 2020 after two years.

Over the past year, political issues have also continued to play a part in the development of infrastructure projects. For instance, in Uganda, disagreements between the oil companies and the government have slowed the momentum built up in previous years. Likewise, political instability in South Sudan, Burundi, Mali and Somalia continue to slow infrastructure developments. There is, however, optimism in the market that the issues are not insurmountable. The development of the Grand Renaissance Dam in Ethiopia continues despite concerns raised by the Egyptian government and is now scheduled to complete in 2023. Additionally, positive political developments in the Democratic Republic of Congo have created a mood of optimism and we anticipate increased economic activity in the infrastructure sector in the immediate future.

2 In terms of project finance transactions, which industry sectors have been the most active and what have been the most significant deals to close in your jurisdiction?

YB: In terms of what is going on in the mining sector, the Republic of Guinea has continued to be very busy, including with the granting to SMB of the notorious Simandou iron ore blocks 1 and 2, but mainly with the development of many bauxite projects. A key component of the success of these projects is the infrastructure element, whether it is rail or port, and the Guinean government has been pushing hard for the development of such infrastructure. Ghana also has plans to take advantage of the country's bauxite ore and aluminium reserves and to build a fully integrated aluminium industry. Ghana Integrated Aluminium Development Corporation, in partnership with the Volta Aluminium Company Limited, is expected to establish three new bauxite mines, and at least two refineries, in addition to the existing smelter.

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MdeB: In the energy sector, a consortium led by Engie and Meridiam recently reached financial close for two solar photovoltaic projects in Senegal – 35MW Kahone and 25MW Toube – being developed under the International Finance Corporation's Scaling Solar programme, bringing to a successful close the first round of scaling solar projects in the country. Lekela has also announced that it has signed a power purchase agreement with the Egyptian Electricity Transmission Company for a 250MW wind farm project in the Gulf of Suez, expected to be operational in 2021. The European Bank for Reconstruction and Development granted a senior secured loan of up to US$89 million, which was co-financed with other parties.

TBL: We have seen increased investment by Middle Eastern investors in Africa. The development of Somaliland's Berbera port by DP World has accelerated over the past year and is expected to be inaugurated in March 2021. Infrastructure links are required to make the port viable and, in 2019, a US$400 million road project to connect the Ethiopian border town of Togochale to Berbera was launched. Saudi Aramco and Abu Dhabi National Oil Company are also reported to be planning investments in Nigeria's oil and gas sector. Also, in one of the most anticipated transactions of 2020, Qatar Airways confirmed that it had acquired a 49 per cent stake in RwandAir. The investment provides RwandAir with a solid technical and financial partner that will be able to support its development and hub strategy. This follows the acquisition by Qatar Airways of 60 per cent of the new Kigali airport in December 2019.

3 Which project sponsors have been most active in driving activity? Which banks have been most active in providing debt finance?

YB: This really depend on the industry sectors. In the power sector, the boom of renewable projects has created opportunities for a much larger spectrum of project sizes than for traditional thermal projects, from a few megawatts to large projects such as the 420MW Nachtigal hydropower project in Cameroon led by EDF. This allows the coexistence of small developers focused on one or two projects of a size sometimes limited, but which can be pioneer projects in the country where they are developed, either as the first renewable project or because it will be the first independent project to be developed there, with all the challenges it entails. You will find larger developers such as Lekela or Akuo from France developing a number of projects in parallel, as well as many infrastructure funds and major international energy groups such as EDF, Acwa Power and Engie. Interestingly, a number of the oil majors, such as Total, BP and Eni, are more and more active in that space.

As lenders, in addition to the infrastructure funds, which act both on the equity and debt sides, development finance institutions play a fundamental role. Players such as the Netherlands Development Finance Company, the Dutch entrepreneurial development bank, KfW, the German development bank, French Development Agency (AFD) and Proparco, the private sector financing arm of AFD, are key in funding projects.

MdeB: In mining, the two most active categories of players, in addition to traditional mining companies, whether major or junior, are Chinese investors – particularly in the Guinean bauxite sector or in the Democratic Republic of Congo – and mining funds, which provide quick and efficient financing solutions to mining projects, whether by way of equity, classic debt or more mining-specific streams or royalty arrangements.

TBL: Multilateral and development finance institutions remain key debt providers on the continent. The African Development Bank and the Trade Development Bank continued to play a significant role in debt provision for infrastructure projects. The World Bank has recently agreed to provide a loan of US$750 million in International Development Association financing to support the upgrade of road and other communication infrastructure in Kenya. African Export–Import Bank has also recently approved

> "Multilateral and development finance institutions remain key debt providers on the continent."

US$400 million in loans and guarantees to support the construction of a US$24 billion Mozambique LNG project.

We have also seen Africa Finance Corporation (AFC), based in Nigeria, continuing its growth during 2020. In June 2020, the AFC raised a US$700 million Reg S Eurobond. The bond was three times oversubscribed despite the challenging global economic environment, indicating strong appetite for Africa's infrastructure and other opportunities. The multilateral financial institution is said to have a current pipeline of investments in Africa worth approximately US$7 billion. In terms of sectors, the opportunities are spread across power, natural resources, transportation and logistics, heavy industries and telecommunications.

Other players such as AP Moller Capital, African Infrastructure Investment Managers and Helios Towers Africa have also been active. Commercial banks (eg, Standard Chartered Bank, Standard Bank, Intesa Sanpaolo, Credit Suisse, Rand Merchant Bank, Deutsche Bank and Société Générale) remained active in debt provision. For example, in May 2020, Standard Chartered Bank extended working capital to Beijing-based Sinohydro to fund a complex irrigation system in Zanzibar. The bank also provided working capital support to Africa Star Railway, which delivered food and

vital medical supplies to millions of people in Uganda, Rwanda and South Sudan at the height of the pandemic.

4 | What are the biggest challenges that your clients face when implementing projects in your jurisdiction?

YB: The most common and well-known challenges for the implementation of projects in Africa are political risks, the lack of sophisticated legislation in certain areas (eg, in the real estate sectors), issues in obtaining ownership over land and the frequent lengthiness of negotiation. This remains generally true.

One particular topic, which is not new, but which has become more critical, are difficulties with exchange controls. African states are working to implement their exchange control regulations more strictly, including regarding the ability for operators to open offshore bank accounts or imposing the obligation to repatriate export proceeds (in particular in the extractive industry sector). This is legitimate but sometimes clashes with the expectations of foreign investors. In project finance transactions lenders tend to maintain security over offshore bank accounts and the

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ease at which this can be done may go to the perceived bankability of the project. For example, it is said that offshore bank accounts was one of the latest issues that delayed the financial close of the Taiba Ndiaye wind project in Senegal.

MdeB: This is particularly the case in the francophone Central African Economic and Monetary Community (CEMAC) and the West African Economic and Monetary Union (UEMOA).

CEMAC was established to create an economic and monetary union among its member states (ie, Cameroon, Chad, Equatorial Guinea, Gabon, the Central African Republic and the Republic of the Congo) and, as a result of which, adopted regulation No.02/18/CEMAC/U MAC/CM on exchange control (the CEMAC Regulation). In June 2019, a number of directives (instructions) were issued by the Bank of Central African States (BEAC), which have, in particular, increased the role of the BEAC in the declaration and authorisation of transactions, the control of compliance with the foreign exchange regulations and the interpretation of the CEMAC Regulation.

Representatives of mining and oil operators from Gabon, Congo-Brazaville and Cameroon have expressed their concerns to the governor of the BEAC regarding the BEAC's new rules, which oblige miners and oil companies operating in a CEMAC state to repatriate funds obtained from abroad.

TBL: Another significant challenge on the continent is the issue of a credible offtake. Sub-Saharan Africa has a small share of global investment in infrastructure due to the low creditworthiness of some countries, their institutions and weak financial markets. This often means that investors seek credit support from the relevant government in the form of sovereign guarantees or put and call options, which many African governments are now pushing back against due to concerns about their balance sheet and accountancy treatment. Stable and secure offtake arrangements are key to a project's revenue stream and go to the heart of bankability. Designing and implementing an objective and transparent procurement process is also crucial to the success of a project. Particular attention should also be given to environmental, social and governance considerations and to ensure that these meet international standards.

5 | Are there any proposed legal or regulatory changes that may give rise to new opportunities in project development and finance? Do you believe these changes will open the market up to a broader range of participants?

YB: On 1 January 2021, a new law – the Conflict Minerals Regulation – came into full force in the European Union. The law aims to curb trade in four minerals – tantalum, tin, tungsten and gold – which sometimes finance armed conflict or are

> “Indian investors are becoming more and more evident in Africa in general.”

mined using forced labour. The regulation details the methodology and criteria to be used by a company when carrying out ‘due diligence’ on the minerals that it intends to purchase. The method set out in the text is based on that defined by the Organisation for Economic Co-operation and Development (OECD) in its dedicated guide. This would thus need to be considered by purchasers and therefore sellers of those minerals.

MdeB: Emmanuel Macron, the president of France, and the Ivorian president Alassane Ouattara announced on 21 December 2019 an agreement between UEMOA and France for an in-depth reform of the Chartered Financial Analyst franc. Used since colonial times by eight West African countries (and six Central African countries not concerned by the reform), and subject to growing criticism recently, this currency will be replaced by the ‘eco’. One major point is the end of the obligation for the countries concerned to deposit part of their foreign exchange reserves in France. Until now, BCEAO, the regional central bank of UEMOA, had to deposit half of its foreign exchange reserves with the Bank of France. France will also withdraw from the governing bodies of UEMOA, where it was present.

Despite the aforementioned major 'political' changes, in order to avoid the risks of inflation, to which African countries have historically often been subject to, the parity of the future eco with the euro is being maintained, which it is hoped will limit the impact of the reform on financings.

So far, it is hard to anticipate whether these changes will have material impacts on the investment decision-making process of foreign investors in Africa but this will certainly be a particular point of attention in the next months.

TBL: In 2019, the London Metals Exchange (LME) introduced responsible sourcing requirements for all brands listed for delivery on the LME. This followed a market-wide review derived from the OECD Due Diligence Guidance. This is an important step in the metals industry as shareholders and other stakeholders consider environmental, social and governance (ESG) issues. While the LME's inclusion of artisanal mining in its proposal to address responsible sourcing is welcome, there is a question as to whether the requirement for full engagement by 2022 and full compliance by 2023 puts the ASM sector at a disadvantage.

6 What trends have you been seeing in terms of range of project participants? What factors have influenced negotiations on commercial terms and risk allocation? Are there any particularly innovative features?

MdeB: One category of investors we have not mentioned yet are Indian investors, which are becoming more and more evident in Africa in general – particularly in the mining, energy, infrastructure and agricultural sectors. As an example, iron exploration in Guinea, which is booming, has attracted a new player, the Indian company Odhav Multi-Industries, which filed an application for the Sandenia iron project adjacent to the Forecariah iron project that was recently taken over by another Indian group, Ashapura Minechem. Odhav has been present in Guinea for several years, not in mining but in the production of concrete iron, a steel bar used to reinforce building structures.

YB: Political stability and progress in the business environment continue to play a key role when setting the key commercial terms of a project and the risk allocation, with this having a significant impact for lawyers when drafting the documentation. Unsurprisingly, the more a country gains experience and credentials in terms of complex projects, the more the commercial terms it obtains from foreign investors tend to converge with those of the most sophisticated international markets such as Europe or the Middle East. Morocco's renewable programme is a key example of that virtuous circle.

TBL: In terms of finance arrangements, we continue to see a mix of debt and equity with projects with higher demand risk having lower leverage. PPP projects with availability payments providing for stable cash flows are lower risk and tend to have higher levels of leverage. Co-financing models and blended finance structures are increasingly being considered as ways to achieve commercial feasibility and bankability of projects. While development finance institutions have traditionally been key to de-risk projects in Africa, there is now a real focus on innovative development finance structures involving true blending of commercial and concessional finance. Instruments can include debt, equity, guarantee and insurance products, risk sharing facilities or a performance-based incentive structure. This also allows for better coordination of development finance institutions and the entry of new project participants including insurance companies, pension funds, mezzanine lenders and private equity as project sponsors try to bridge the financing gap. Hybrid debt structures and models using multiple debt tranches, some of which are only available in the future and subject to certain conditions, are also being used.

7 What are the major changes in activity levels or new trends you anticipate over the next year or so?

YB: The recession that will be caused by the covid-19 pandemic is predicted to have far worse consequences than the global financial crisis. Given the significant casualties in both Europe and America, we anticipate that this will affect investment in Africa from these regions. Although China is also expected to slow down, it is very likely that Chinese investors will still take the opportunity to increase their market share in the infrastructure sector in Africa owing to the continuing urgent need.

In energy, we still expect the renewable sector to continue to rise, particularly in North and East Africa, including the hydropower sector, which has been especially active over the past few years. The development of renewables in Egypt, Tunisia and Algeria will be also worth following.

In mining, although the current oversupply of cobalt and lithium may entail a slowdown of Chinese investments in relation to these specific minerals, the anticipated increase of copper prices in 2020 should maintain a strong interest for the Democratic Republic of the Congo (DRC), Zambia and a number of other countries. The diamond sector should have another bumpy year with prices currently weak and some major African producers going through significant changes, including Angola or the Central African Republic.

MdeB: Another notable trend is the increase of innovation as a supporting tool in the mining sector. As an example, in October 2019, the World Economic Forum reached

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an agreement with seven mining companies to develop and deploy a new blockchain platform to make the supply of raw materials more responsible and sustainable. The companies include Antofagasta Minerals, Eurasian Resources Group, Glencore, De Beers, Minsure, Klockner & Co and Tata Steel. Known as the Mining and Metals Blockchain Initiative, the initiative will track and trace raw materials from the mine to end users and record carbon emissions. The goal is to improve confidence in the mining industry at a time when investors are increasingly concerned about the industry's inability to cope with the risks and uncertainties of today's world. Another example is a platform developed by the American computer giant IBM, which works with blockchain technology and has been in use since early 2019 at a cobalt mine owned by the Chinese Huayou Cobalt in DRC. The blockchain should make it possible to ensure the traceability of the metal from the extraction site, operated by Huayou's Congolese subsidiary, to the plants of the US car manufacturer Ford.

TBL: Given the increased focus on ESG and sustainability, we may see the issue of more green bonds as a tool to create more climate-resilient economies and to honour the commitments made in the Paris Climate Agreement. We have seen the examples of Acorn Holdings in Kenya, Access Bank in Nigeria and, in September 2020, the AFC also issued its inaugural 150 million Swiss francs Reg S senior unsecured benchmark green bond. Furthermore, as the low carbon transition continues, the mining sector is likely to experience a substantial boom. Many of the mineral resources required for clean energy technologies will be sourced from resource rich African countries such as the Democratic Republic of Congo and Zambia. These include iron, lithium, cobalt, nickel copper and other rare minerals, which are often used in solar panels, wind turbines and electric cars.

Despite initial concerns around the impact of covid-19 on the relationship between China and Africa, some now argue that this will strengthen the relationship in the coming years. Investment and financial corporation has continued and, in June 2020, Nigeria launched the Lekki Deep Sea Port Project, which received over US$1 billion investment from Chinese business. Chinese businesses also invested approximately US$680 million in the form of build–operate–transfer in the JKIA–Westlands Expressway project in Kenya, which has continued despite the global pandemic. China has also agreed to debt suspension arrangements with a number of African countries. The Belt and Road Initiative is also likely to increase participation by Chinese business on the continent.

There is likely to be increased investment from Russia following the recent Africa summit initiated by President Putin. The United Kingdom, in the light of Brexit, will also look to forge closer bilateral trade ties with African governments. French investors will continue increased investments in anglophone Africa. The Biden administration is also likely to increase multilateralism on the continent and is likely to work via the African Continental Free Trade Area.

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The Inside Track

What three things should a client consider when choosing counsel for a complex project financing?

Developing a project in Africa continues to require quite skills specific. You certainly need a counsel with the right sector and project financing expertise but you also need a counsel with genuine African experience. The specific challenges of developing an African infrastructure project are likely to include dealing with counterparties who are not always familiar with the requirements of international project financing (local partners, local counsel, local offtakers, local governments) even if the level of sophistication is progressing rapidly, or facing unexpected legal changes, like a last-minute new electricity law that was passed in Cameroon a few years ago just some days before the financial close of the first two independent power projects in the country.

What are the most important factors for a client to consider and address to successfully implement a project in your country?

The choice of co-investors, lenders and advisers is critical to a successful project in Africa as well as the understanding of the environment and the ability to focus on what really matters. More than anywhere else, it is possible to spend months or years focusing on details and losing sight of what really matters for you as an investor, while closing the transaction within a reasonable timetable is generally something that matters much more to you than marginal improvements to the project, which can be only achieved at great time expense. The increased involvement of infrastructure funds in African projects, as well as certain developers who have realised that the ability to close projects quickly is a key differentiating factor, is helping to move away from the thinking that closing a project in Africa has to take years.

What was the most noteworthy deal that you have worked on recently and what features were of key interest?

We have been advising the Djibouti Ports and Free Zone Authority on its negotiations with major Chinese investors to develop the largest free zone project in Africa, capitalising on Djibouti's unique positioning as the hub of East Africa. This project gathers many of the current trends of project finance in Africa: the push for infrastructure, the continued increase in Chinese investments in Africa and the efforts of African governments to move to the next level of infrastructure projects.

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Covid-19 impact
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