PUERTO RICO CONFERENCE

Entrepreneurship for Growth

2010

March 24, 2010 | Conrad San Juan Condado Plaza | 7:30 a.m. - 5:00 p.m.

Puerto Rico Chamber of Commerce

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CAMARA DE COMERCIO DE PUERTO RICO

TAKING ADVANTAGE OF THE PUBLIC PRIVATE PARTNERSHIPS (P3s)

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Manuel R. Pietrantoni (Moderator)
David Álvarez, José Arias, Benjamin Hellweg

Puerto Rico Chamber of Commerce

PUBLIC POLICY AND GOALS OF PUERTO RICO'S P3 PROGRAM

- It is the Government's public policy to favor and promote the establishment of Public-Private Partnerships in order to create projects in certain designated sectors:
  - Landfills systems and management and disposal of solid wastes and conversion of waste to energy;
  - Production of energy (alternatives to oil-fired production);
  - Mass transportation;
  - Facilities for health, security, education and correction;
  - Affordable housing projects; and
  - Others (cultural or communications facilities and high technology systems).

- The P3 Program's goals are to:
  - Encourage the development and maintenance of infrastructure facilities;
  - Share the risk of developing, operating and maintaining P3 projects between the Government and private sector participants;
  - Improve the services provided to the public; and,
  - Promote employment, socio-economic development and Puerto Rico's competitiveness.

KEY INGREDIENTS OF A SUCCESSFUL P3 PROGRAM

- A statutory and regulatory framework providing clear and uniform rules that promote transparency and consistency;
- Political commitment – strong support of program by government;
- Reasonable public support for program;
- Credible and efficient process – projects get completed;
- Develop expertise – have a dedicated agency running the program;
- Reasonable allocation of risks between public and private sectors;
- No legislative approval required for each project; and
- Standard and consistent contract documentation.

P3 EXPERIENCE ACROSS THE WORLD

- 1,109 projects valued at $509 billion (from 1985 to 2007)
- Europe: 43% of total projects, 50% of total value (Great Britain: 40% of Europe's projects)
- Asia and Australia: 24%
- North America: 16% (U.S. 9%)
- Types of Projects:
  - Roads and Bridges 35%
  - Water/Wastewater 26%
  - Building 22%
  - Rail 7%
  - Seaport 5%
  - Airport 5%
- The transportation and water systems account for 76% of dollar value of P3 projects.

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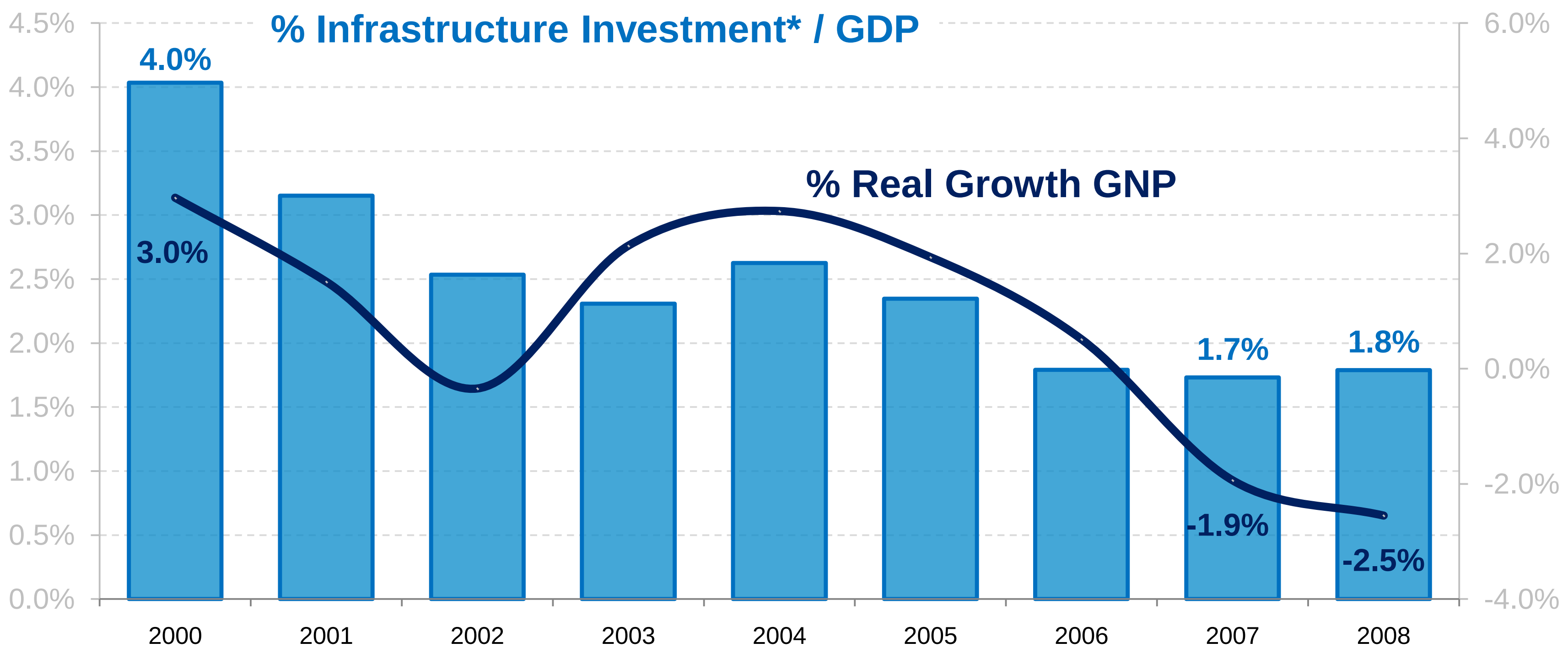
David Álvarez

Infrastructure investment is essential for economic growth

Puerto Rico needs to restore investment in infrastructure

Puerto Rico Data (Fiscal Years)



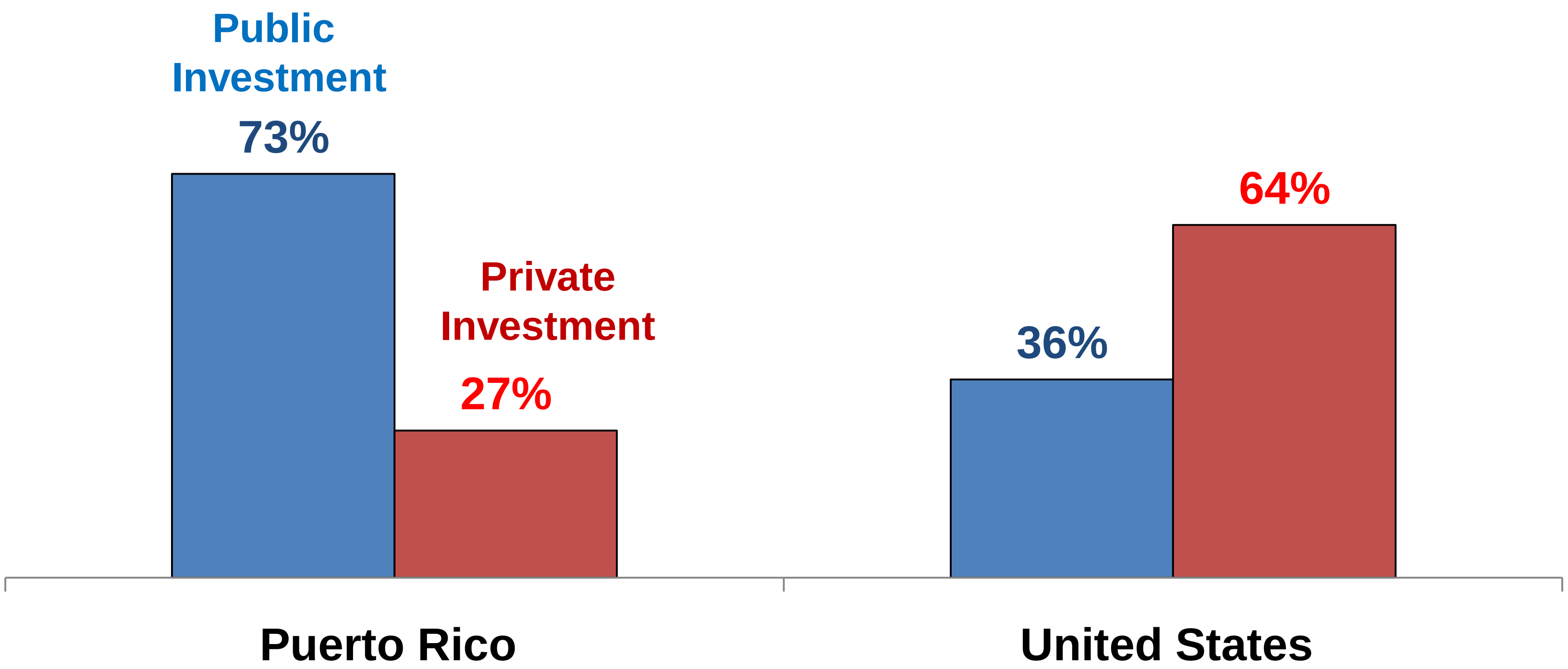
Source: Puerto Rico Planning Board.

* Selected Statistics from Construction Industry publication Table #1 (sum of Public and Private Installation Projects).

Puerto Rico remains in the past by relying on the traditional model of delivering infrastructure investment

Greater private infrastructure investment leads to higher competitiveness

Average annual composition of total infrastructure investment between 1990 to 2008

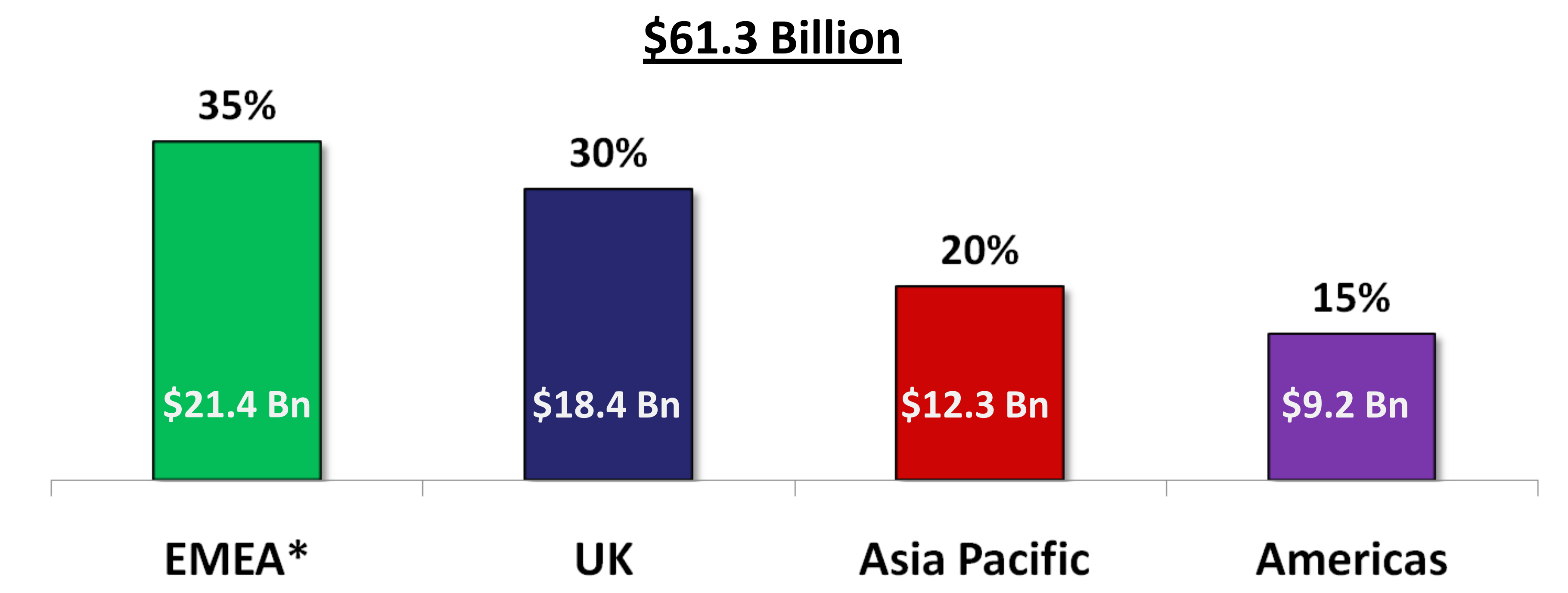


Source: Puerto Rico Planning Board & the Bureau of Economic Analysis (BEA)
* Selected Statistics from Construction Industry publication Table #1 (sum of Public and Private Installation Projects).

Highly competitive nations are leaders in P3s

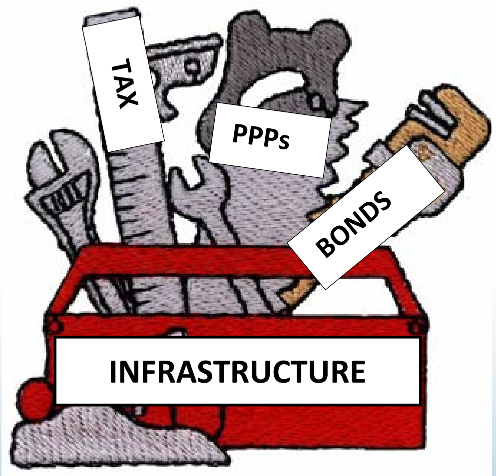
Private investment infrastructure is widely used in other parts of the world

Global P3 Market by Region



Source: Kearsarge Global Advisors, *Benefits of Private Investment in Infrastructure,* March 2010.
* Europe, the Middle East and Africa.

P3s are a needed tool to deliver infrastructure investment



PPPs are critical tool in the toolbox of infrastructure and deliver benefits for the Public and the Private Sectors

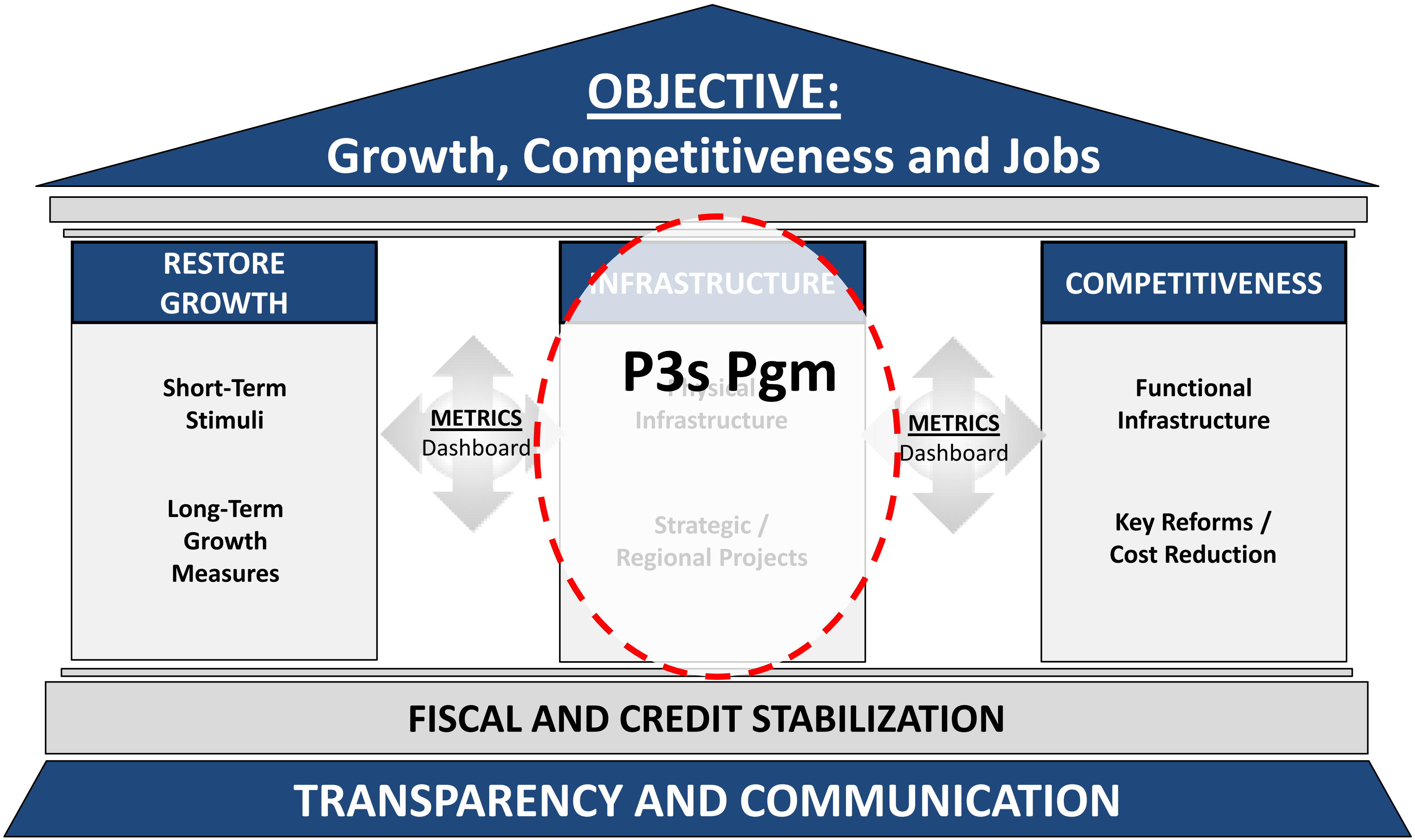
Government Perspective…

1. Retain ownership of public asset
2. Accelerate investment
3. Benefit from private sector innovation
4. Reduce risks of delivering infrastructure
5. Provide Value for Money to taxpayers

…Private Sector Perspective

1. Provides an investment opportunity
2. Complete management of project risks
3. Fosters innovation
4. Projects do not proceed if not feasible
5. Competitive process and transparency

Conceptual Framework of the Strategic Model for a New Economy (*MENE*)



P3 Opportunities across all major infrastructure areas

- **PR-22:** busiest toll road in PR
- **PR-66:** only corridor in the East
- **PR-52:** longest toll road in PR

- **Phase I NG*:** Aguirre Plants
- **Phase II NG:** SJ & Palo Seco
- **Phase III NG:** Costa Sur

- **LMM Int'l Airport:** busiest airport in the Caribbean

- **Modernization of Schools:** Design-Build-Maintenance of public schools

- **Water Metering:** improvement of water metering system

* NG = Natural Gas..

5 Infrastructure Areas = Great Opportunities

- **There is a clear need and consensus that investment in core infrastructure is needed**
- **Mix of brownfield and greenfield opportunities**
- **Favorable asset sizes**
- **Clear legal and regulatory framework**
- **Transparency through the public release of desirability studies, RFQs and RFPs.**
- **Financial markets are normalizing**

12

P3 Authority is committed to moving projects into procurement and closing in 2010

2009 Completed

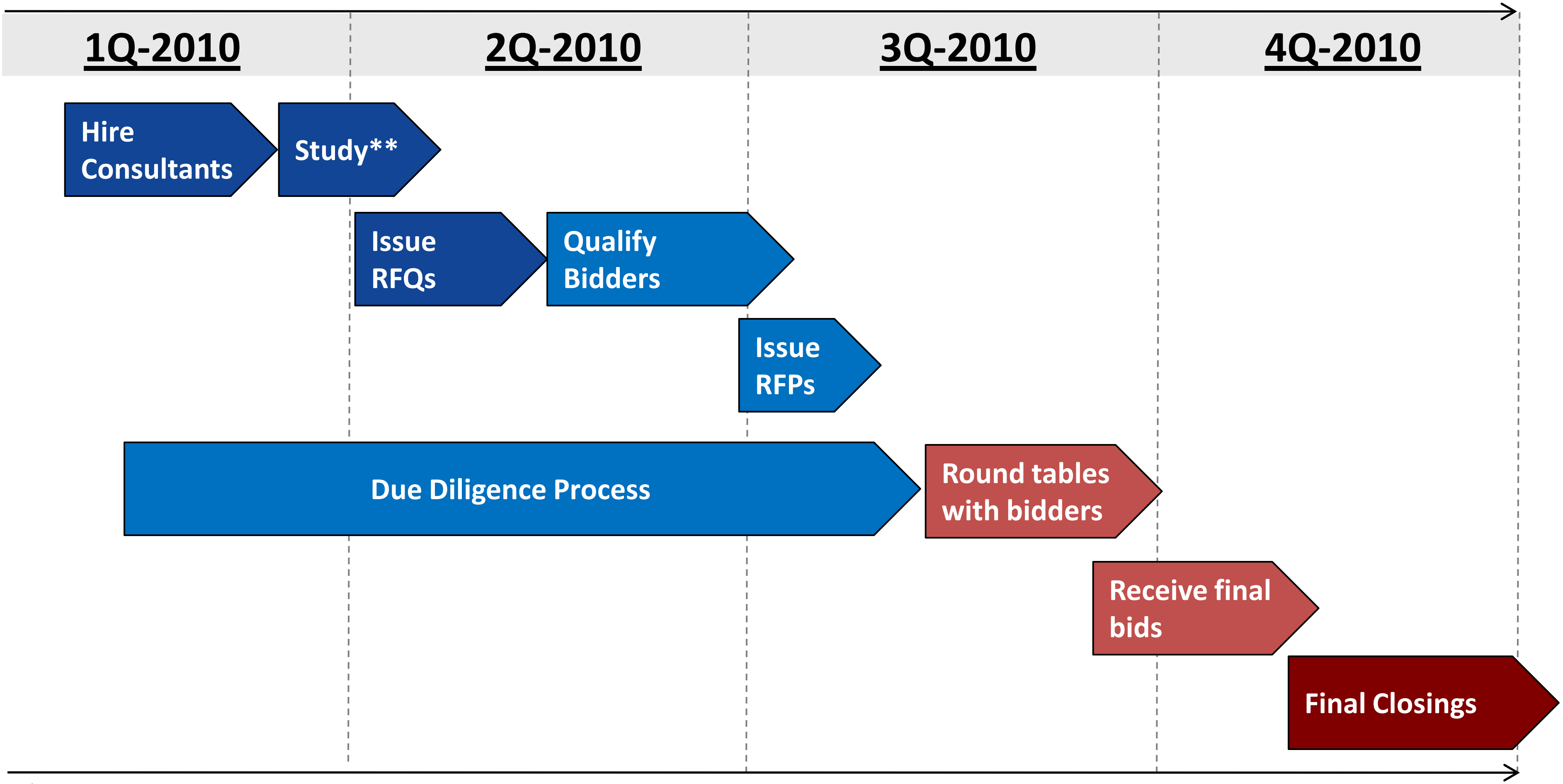
June:	Approval PPP Act ✓
Aug:	Website PPP ✓
Sept:	Board of Directors ✓
Oct:	Project Conference ✓
Dec:	8 Projects Selected and Approval of Final Regulations ✓

2010 Next Steps

1Q-2010:	Submit TIFIA Letters of Interest ✓
	Selection of Sell-side Advisors (in final phase)
	Desirability and Convenience Studies (in progress)
2Q-2010:	Website revamp (in progress)
	RFQs and initiate RFPs

General Procurement timeline for 2010

Target and Preliminary General P3 Procurement Timeline for 2010*



* Preliminary and subject to revision.
** Study refer to the required Desirability and Convenience Study.

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José Arias

Key Themes – Infrastructure M&A and P3 Market

1. Infrastructure M&A and P3 activity is making a comeback with a more robust pipeline expected in 2010
   - On-going capital markets turmoil that has produced delays and cancellations in projects has recently also resulted in divestments, private-to-private asset sales and distressed sales
   - Despite current credit market challenges, properly structured deals are still achieving financial close
2. Scarcity of certain attractive assets is still key feature of the sector
   - Investors are chasing high quality assets, but are ambivalent towards lower quality assets
3. Canada is a leader in infrastructure M&A and P3 activity in North America
   - US infrastructure M&A activity is dominated by small- to medium-sized, private-to-private transactions though the P3 market is slowly making a comeback
4. Market for P3 projects in the US is increasing
   - Several states have enacted better P3 legislation in recent times – Arizona, California, Georgia, Puerto Rico, etc.
   - There is increasing realization by states that private sector investment is fundamental to unlocking new opportunities
   - Economic crisis has resulted in a shift away from large-scale brownfield state asset P3s to greenfield P3s
   - Availability-based payment deals are now being used as well as user fee-based P3s
   - Greater role to be taken by counties and municipalities to push on with their own project pipeline

Key Themes – Infrastructure Financing

1. Capacity across most financing options continues to be constrained
   - Fewer banks in a position to lend
   - Reduced credit capacity
   - Less appetite for trees (supporting multiple bidders)
   - Bank bridges to capital markets issuance impacted by collapse of monolines and limited buyer appetite for refinancing risk
   - Exit of monolines
2. Banks unable to rely on syndication, so buy and hold only with reduced quantum
   - Deals continue to be done as “club deals” with multiple banks
3. Tight bank liquidity drove a sharp increase in pricing and tighter covenants
   - Higher margins (though LIBOR has fallen)
   - Lower debt multiples
   - Margin step-ups and cash sweeps to force early refinancings
   - Monitoring the health of the company/project through tighter banking covenants
   - Shorter-term tenors
   - Ability to refinance in capital markets
4. Bond markets have re-opened
   - Significant volume of corporate bond issuance for investment grade credits and increasingly for high yield credits
   - Pricing is not quite back to pre-crisis levels, but continues to trend that way
   - Capacity remains constrained for certain credits

Key Themes – Infrastructure Equity

1. Investor interest in the infrastructure asset class is still strong

2. Large amounts of equity capital allocated to the infrastructure sector remains uninvested (but the pool has reduced)
   - However, investors are unable or unwilling to write tickets as large as previously seen

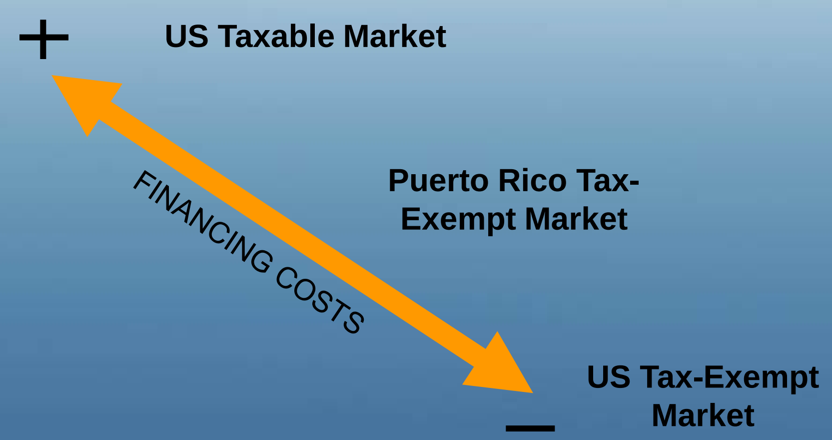
3. Director's valuations have started to come down and are now more in line with the Net Asset Values attributed by the public equity markets

4. Key challenge for the infrastructure market is the return of the finance providers
   - More challenging fund raising environment as institutional investors constrained by overall fall in portfolio valuations
   - Conservative approach to refinancing
   - Many investors unwilling to engage in the absence of proven source of financing

US and Local Capital Markets

1. The use of proceeds for public purpose will determine the market available to issue debt
   - US tax-exempt market provides the lowest costs for financing
   - If the financing doe not qualify for the US tax-exempt market, the local tax-exempt market provides lower costs than the US Taxable market

2. Credit of the Issuer is very Important in the local market
   - Investment Grade: BBB- / Baa3 or better



Local Financing Alternatives

1. Local commercial banking market
   - Large historic banking market on-island but limited history of large scale project lending
   - International lenders with a major on-island presence include:
     - BBVA
     - Santander
     - Scotia Bank
   - Many of the on-island lenders are still recovering from the credit crisis and are currently not lending but capacity may return
   - Some infrastructure lenders do not consider Puerto Rico to be the US market and will not lend to the local market
2. Issuance through Government Entities
   - Interest is tax-exempt
   - Special / Limited Purpose Obligations issued by:
     - AFICA – Industrial Development Bonds
     - Local Public Corporations
       - ✓ PR Highways and Transportation Authority
       - ✓ PR Aqueduct and Sewer Authority
       - ✓ PR Electric Power Authority

AFICA Financing

1. Advantages
   - Tax-exempt 30-year fixed rate debt provides maximum interest rate protection
   - Maximum annual debt service is usually lower than commercial loans
   - Provides for a 30-year amortization schedule
   - Financing funded at issuance for all the projects

2. Disadvantages
   - Higher interest cost than current floating rate based loans
   - Timing: potentially longer process
   - Disclosure requirements
   - Annual rating agency maintenance fees

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Benjamin Hellweg

Infrastructure Market Themes

Europe:
- Regulatory Activity (e.g. unbundling) driving utility M&A
- In Transportation, corporates are disposing non-core assets

Australia:
- Restructuring and Recapitalization of listed Funds
- Continuing privatizations of Government assets

North America:
- Weakening public sector finances are driving P3 procurements by state and local governments
  - Doyle Drive (CA);
  - Northwest Corridor Managed Lanes (GA);
  - Detroit River International Crossing (MI/ON)

Infrastructure Market Themes

More focused and disciplined investing by all types of market participants

- Listed Funds' trading levels reflect a significant discount to NAV, making acquisitions challenging
- Strategic Players narrowing targets to ensure optimal deployment of scarce capital by focussing on core geographies and projects specifications
- Private Funds and direct investors re-evaluating risk appetite and return expectations given performance of some assets during the recession

→ Smaller number of more focussed bidders for individual assets

Comparison with other jurisdictions

	Program vs. One-off	Closing/ Political Risk	Regulatory Framework	Inter-national Bidders	Local Market	OECD	Green vs. Brown-field
Puerto Rico	●	◕	●	●	◕	●	◕
Mexico	●	●	●	●	◑	●	◕
Brazil Federal	●	◑	◕	◔	◑	○	◑
Sao Paulo	●	◕	●	◔	◑	○	◑
Chile	●	●	●	●	●	◕	○
Pennsylvania	○	○	◔	●	◕	●	●
Georgia	●	◑	◕	●	◕	●	◔
Chicago	◕	◕	◑	●	◕	●	●
Indiana	○	◔	◔	●	◕	●	●
Texas	◑	◑	◔	●	◕	●	◔

What investors look for

Investors will bring their capital and resources to markets where they feel 'welcome'

- Transparent sale processes and regulatory/concession oversight
- Flexibility to listen to the investor community and adjust transactions to meet changing market conditions
- Commitment to a P3 program rather than one-off transactions
- Commercial approach to risk sharing and risk allocation

An environment where Public Private Partnerships live up to the name 'Partnership'

Global P3 Financing Market Conditions

- Debt Markets have stabilized since the credit crisis peaked late in 2008
- Lenders are more selective when extending credit, with a focus on working with relationship partners and well-structured, highly rated transactions
- Most recent bank transactions have been ‘club deals’, with limited appetite for syndication risk
- The debt capital markets have been open and active, providing a potential funding alternative for issuers
- Financing costs remain low by historical standards, as higher credit spreads are compensated by low base rates, but leverage has significantly moderated

CONCLUSIONS OF THE JANUARY 2010 REPORT PREPARED BY THE CONFERENCE BOARD OF CANADA

- **Pan-Canadian Assessment of P3s for Infrastructure Investments:**
  - The second wave of P3s initiated under the guidance of specialized infrastructure procurement agencies have to date delivered important efficiency gains relative to conventional procurement approaches. These efficiency gains take the form of cost savings and times savings.
  - These Canadian results are also broadly consistent with international evidence from the United Kingdom and Australia – the jurisdictions that have the most experience with P3s.

– Despite the successes to date, not all P3 infrastructure projects generate efficiency gains, because in some cases the gains can be more than offset by a combination of the incremental cost of private financing, any additional costs arising from transferring the risks to the private consortium (i.e., the risk premium), and the incremental transaction costs. This is why each infrastructure project requires a rigorous Value for Money assessment to ensure that a P3 procurement option delivers value relative to a conventional procurement method, as is standard practice for all second-wave P3s.

– Several factors drive the efficiency gains that arise from P3s:

- The first is the optimal risk allocation process, which is at the heart of the P3 procurement process adopted by the P3 agencies and offices across Canada. The optimal risk allocation process involves identifying and valuing project risk exposure upfront and transferring to private consortia those risks for which these firms have the requisite risk management and mitigation experience.

- Performance-based contract provisions, which specify desired outputs rather than prescribed inputs, are another driver of efficiencies in P3 contracts.
- The integration of the design, construction, operation, and maintenance phases of a project is yet another potential driver of efficiencies, because it allows private firms to adopt innovations that can reduce whole life-cycle costs, even if they involve more investment in the design or construction stages.

- Private finance is the fourth efficiency driver in P3 projects. By virtue of this feature of P3s, the public sector pays the private consortium only upon delivery of the facility (although some milestone payments are sometimes made before completion of construction). This provides a powerful incentive to ensure that the facility is built in a timely manner and in a way that meets the contractual requirements.

- We also take this opportunity to dispel a few myths about P3s in Canada:
  - First, P3s in Canada are not about the privatization of public assets. Ownership of the new infrastructure facilities either remains with the public sector or is transferred back to the public sector at the end of the contract term.
  - Second, the anecdotal evidence in this report suggests that there is little basis to the criticism that service standards suffer under a P3 relative to conventional maintenance contracts or even relative to in-house provision.

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