

ASSET CAPITAL PARTNERS

Structured Financing – Time for Mezzanine

The 3rd annual Russian CFO Summit

Adam Smith Conferences

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- 1. Recent trends in debt financings in Russia**
- 2. Debt financings in asset based industries – natural resources, infrastructure and real estate**
- 3. Time for mezzanine financing**



Recent trends in debt financing in Russia (1)

- **Increasing competition between:**
 - **international and local banks**
 - **debt and capital markets**
 - **RUR and USD markets**
 - **developed and emerging markets**

- **As of October 2006, international banks provided to Russian borrowers USD 36bn of syndicated debt compared to USD 46bn at the end of 2005 and USD32 bn at the end of 2004:**
 - **Stable average tenor: in 2006 – 39 months vs. 42 months in 2004 and 2005)**
 - **Decreasing margins: on average 174.2 bps in 2006 vs. 204.8 bps in 2005 and 278.1 bps in 2004**
 - **Decreasing average facility size: in 2006 USD 252 m vs. USD 313 m in 2005 and USD 266 m in 2004**



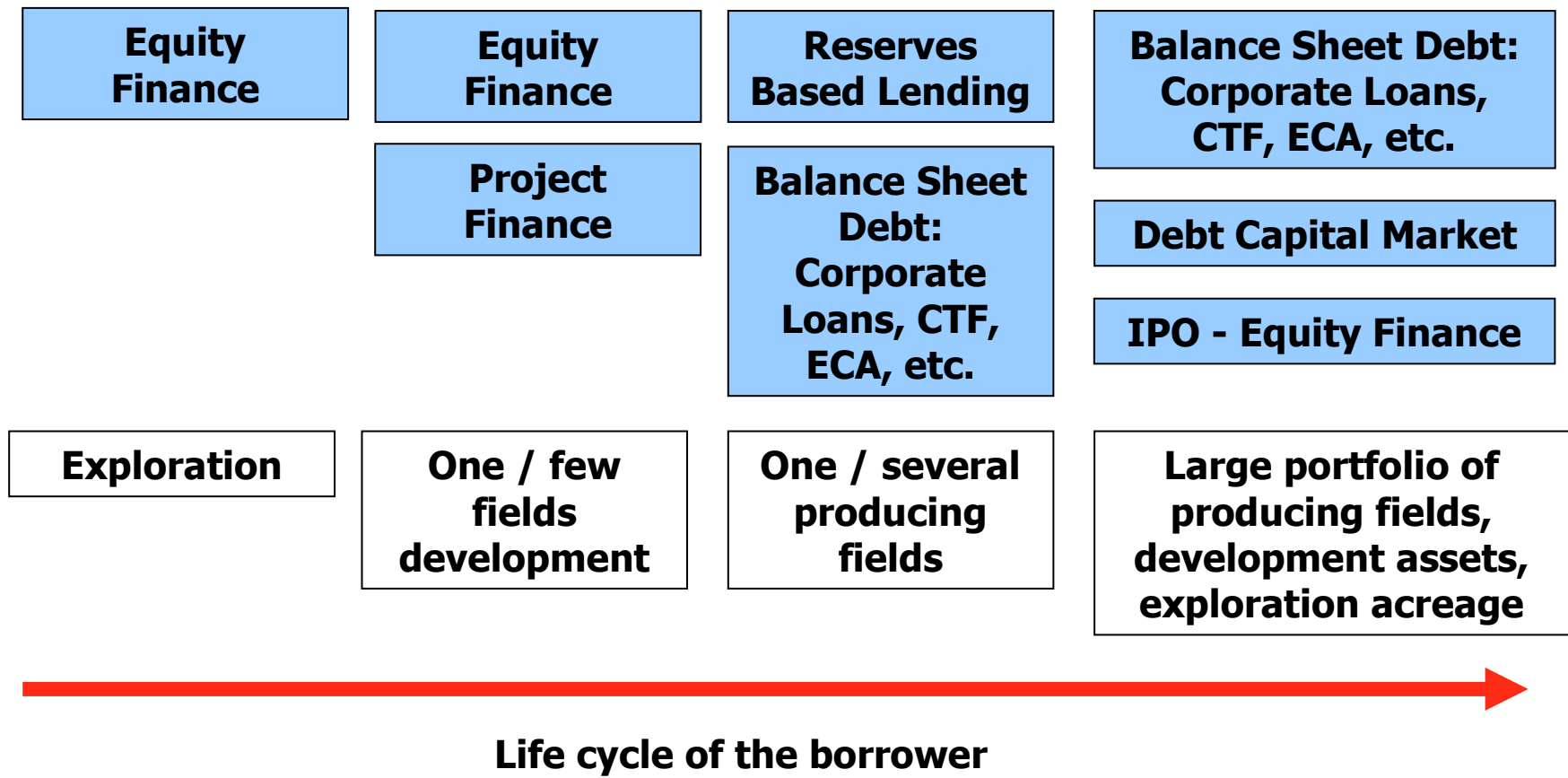
Recent trends in debt financing in Russia

- **Commercial banks face increasing competition from capital markets: debt (bonds) and equity (IPO)**
- **Average tenor: 3.5 – 5 years; maximum av. tenor in 2006 - ???**
- **Natural resources industries (especially oil and gas sector) are over-banked – decreasing margins and fees, increasing tenors**
- **Pricing dumping of yesterday turned to be a smart strategy for some banks today (improving investment profile in Russia and bullish market)**
- **Banks are forced to look at new markets or change their risk profile**



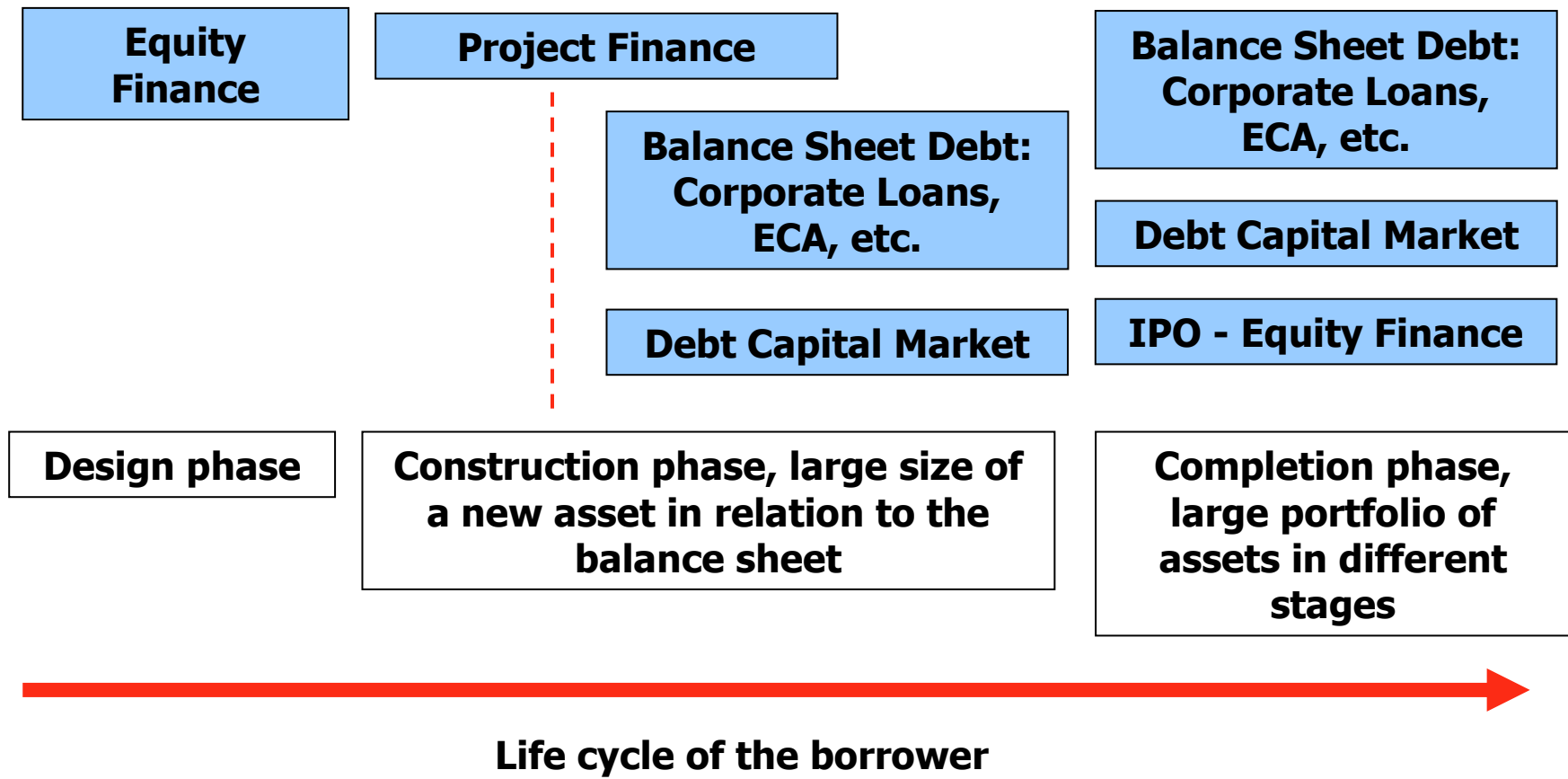
Debt financings in natural resources

- Oil and gas upstream, mining
- Pre-completion / post-completion



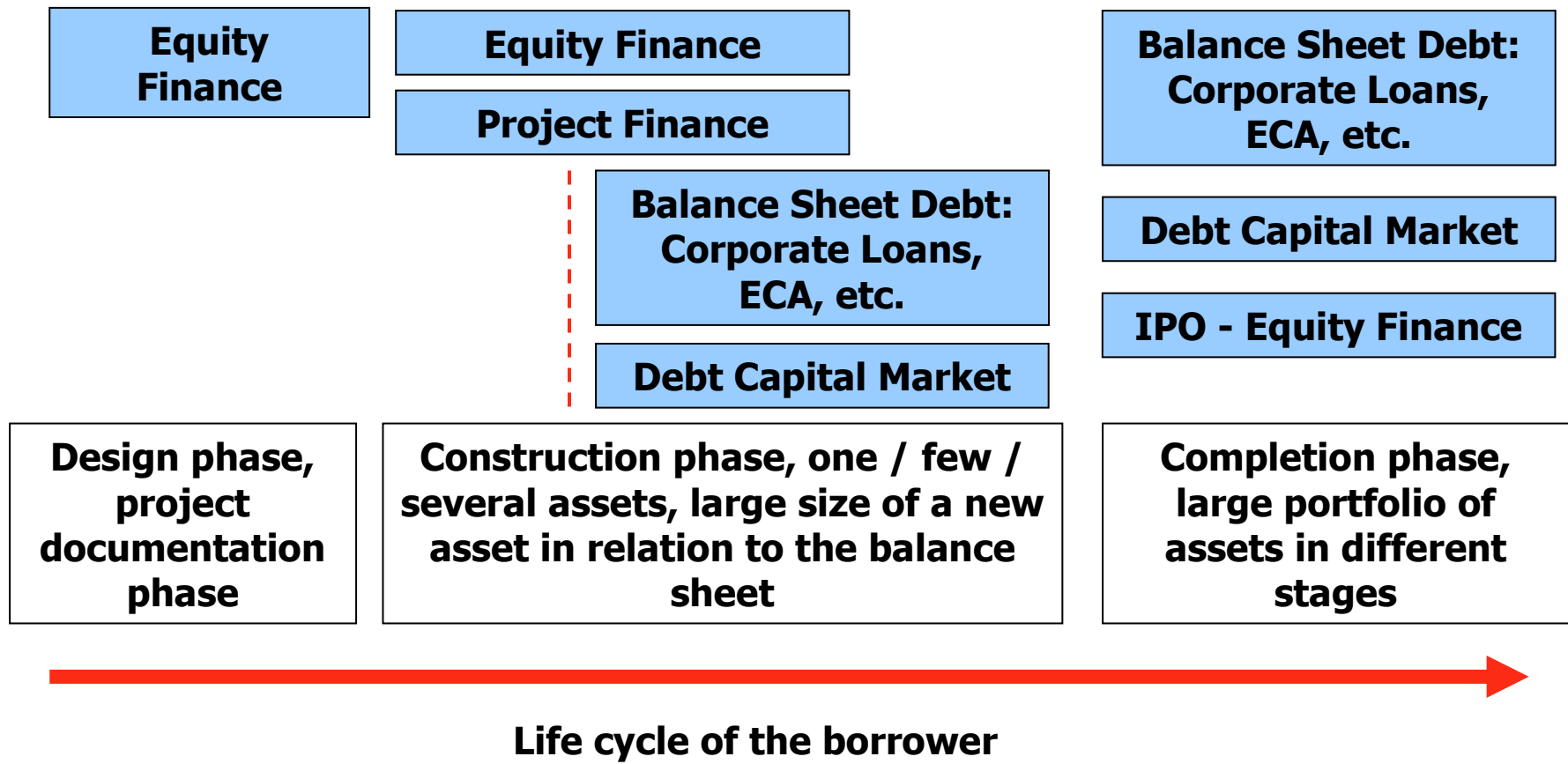
Debt financings in infrastructure

- Pipelines, airports, ports, roads, power, etc.
- Pre-completion / post-completion



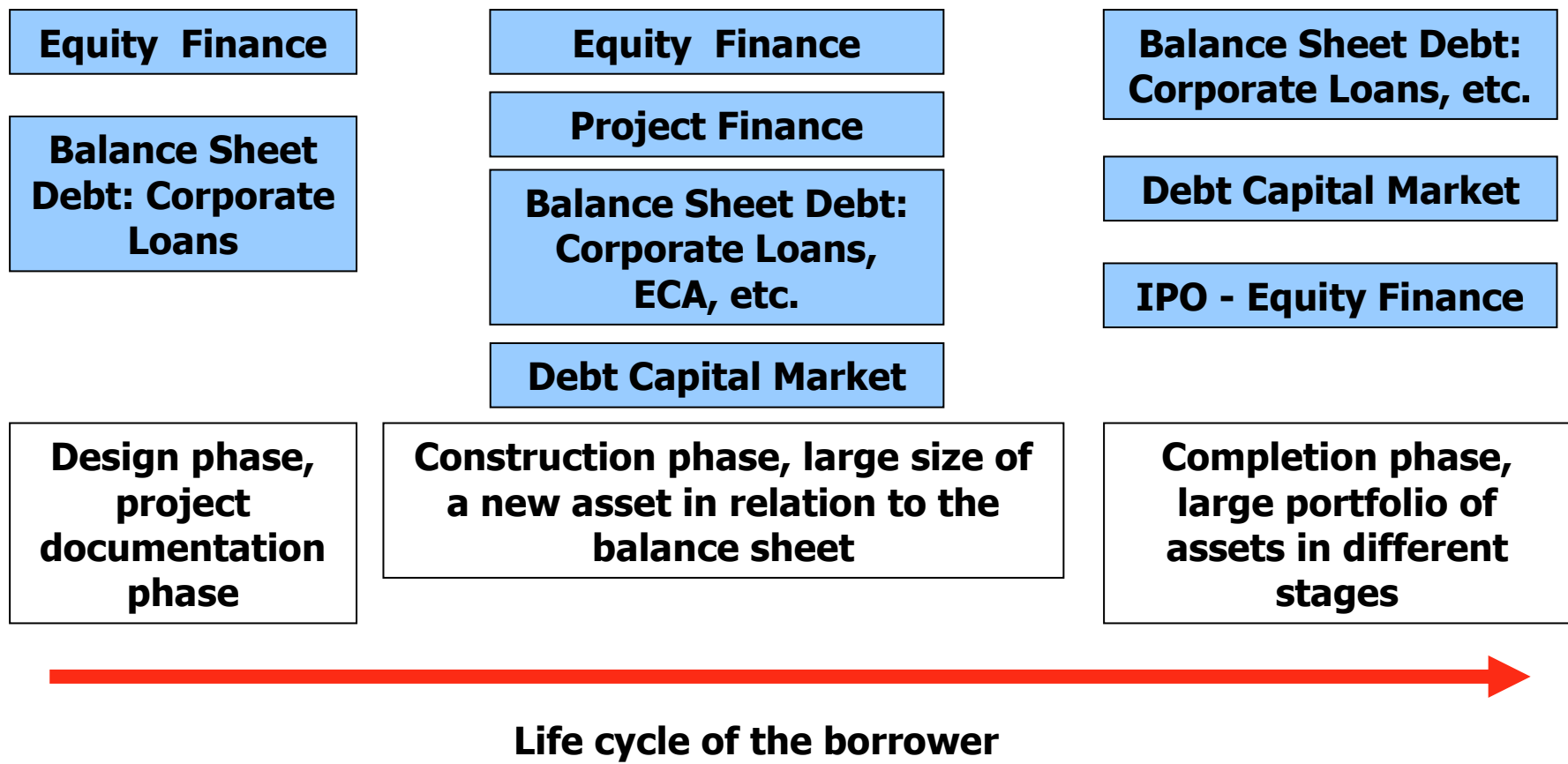
Debt financings in real estate (1)

- Commercial real estate: office buildings, retail, logistic centres, etc.
- Pre-completion / post-completion



Debt financings in real estate (2)

- Residential real estate
- Pre-completion / post-completion



Time for mezzanine financing: definition

- **Mezzanine financing is a type of hybrid junior debt financing used to fill the gap between senior debt and equity financing**
- **Due to its ranking behind the senior debt, mezzanine financing is more expensive than senior debt, however, still cheaper than equity**
- **Often longer tenor than of senior debt**
- **Often longer grace period adjusted to senior debt service**
- **Typically secondary or non-secured; however, a personal surety or corporate guarantees can be provided**



Time for mezzanine financing: application

- **Mezzanine financing can be used inter alia in**
 - **General corporate needs (restructuring, credit ratios improvement)**
 - **Acquisition financing**
 - **Project financing**
 - **Pre-IPO financing**
 - **In combination with corporate loans to medium sized companies**
 - **Private equity and venture capital investments**
 - **Securitisation**
- **No industry constrains: natural resources, infrastructure, real estate, industries, retail, etc.**



Time for mezzanine financing: borrowers

- **Benefits to borrowers:**
 - **Flexible financing instrument**
 - **Secures an adequate relation between equity and debt**
 - **Cheaper source of equity funding**
 - **Lowers the cost of senior debt**
 - **Provides stabilisation during pre-completion period: longer grace period and tenor**
 - **Unsecured**
 - **Accepts lower cash flow and more comfortable financing ratios**



Time for mezzanine financing: mezzanine providers

- **Benefits to mezzanine providers:**
 - **Higher margins**
 - **Higher ranking than equity**
 - **Profit participation**
 - **Extension of client base**
 - **Fulfilment of Basel II requirements**
 - **Better client risk management**
 - **Flexible equity distribution**



Time for mezzanine financing: mezzanine types

- **There are various types of international mezzanine financings**
 - **Mezzanine debt: junior and subordinated debt combined with equity kickers / sweeteners like equity-linked options or warrants, subordinated debt with interest payments in PIK notes or convertible bonds/notes, shareholder loans, etc.**
 - **Mezzanine equity: preference shares, convertible zero-bonds, “Preferred Pooled Shares”, etc.**
- **In Russia mezzanine debt could increase debt capacity in case of equity constrains**



Time for mezzanine financing: sources and players


- **Mezzanine financing is a newcomer in Russia**
- **Potential mezzanine providers could be:**
 - **International commercial and investment banks**
 - **Multinational financial institutions**
 - **Mezzanine funds**
 - **Private equity funds**
 - **Venture capital funds**
 - **Russian banks**
 - **Russian capital market**




Time for mezzanine financing: challenges in Russia

- **Challenges in mezzanine financings in Russia:**
 - **Product know how**
 - **Industry, financial, legal/tax knowledge**
 - **Complex financing structuring**
 - **Security structuring**
 - **Modelling skills**
 - **Transaction experience**





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