AIL Structured Finance

We bridge the gap

Newsletter July 2010

Brazil / Stadler – Successful Closing, AIL advises Stadler Rail on the export of the world's biggest and most powerful rack-and-pinion locomotive

At the end of February 2010, AIL closed a structured payment security finance rolling stock transaction in Brazil for MRS Logística S.A. AIL acted as financial advisor to the reputable Swiss railway manufacturer Stadler Rail.

In this transaction Stadler Rail is building the world's biggest and most powerful ever rack-and-pinion locomotive for the Brazilian cargo company MRS. MRS has ordered seven of these locomotives from Stadler, worth about CHF 60 million, for the freight line from São Paulo to the docks in Santos. An option for three further locomotives has also been agreed. The vehicles will be built in Bussnang and delivered in 2012/2013.

MRS is one of the largest cargo transportation companies in Brazil. MRS is a concessionary that controls, operates and monitors the Southeastern Federal Railroad Network. The company has been in operation in cargo railway transportation since 1996. It interconnects the states of Rio de Janeiro, Minas Gerais and São Paulo. The company has 1,643 km of railways that make the transportation process easier in a region in which approximately 65% of Brazil's gross domestic product is concentrated and which is home to the largest industries in the country. Through MRS' railways you can also reach the ports of Sepetiba and Santos (the most important in Latin America).

MRS' activities focus on general rail cargo transportation, such as ore, steel products, cement, bauxite, agricultural products, coke and containers; and on integrated logistics, which involves in-planning, multi-modality and defined transit time. MRS ordered the seven rack-and-pinion freight locomotives from Stadler Rail mainly for use with heavy trains carrying iron ore. Each Stadler locomotive has a maximum power of 5,000 kW and a length of almost 18 metres per vehicle.

AIL advised Stadler Rail on risk management issues and structured a security package, covered by the Swiss Export Agency SERV. This security package comprises a cover of export risks during the manufacturing period, as well as a payment security in a private sector environment.

Interview with Mr. Herbert Wight, Director Swiss Export Agency SERV*

The Swiss export industry has to some extent been hit hard by the financial and economic crisis. Beside the fact that many Swiss exporters have been confronted with a sharp fall in orders, some of them have also faced liquidity shortfalls. Despite the steadily recovering situation on the international markets, tight liquidity is still an issue.

In order to support Swiss exporters in this difficult situation, Swiss Export Risk Insurance SERV has introduced four new products within phase II of federal stabilization measures. The purpose of these products is to facilitate access to financing for exporters and to maintain their liquidity. In addition, the maximum cover ratio for private buyer risks under supplier credit insurance has been increased to 95 percent (in line with the cover ratio for political risks). By law, these new products are available only until the end of June 2011.

AIL Structured Finance had the opportunity to talk to Mr. Herbert Wight, Director of SERV, about the important role of the national export credit agencies in the current international financing markets.

AIL: The credit crunch's impact in Switzerland is a subject that has recently been discussed a lot. Have you been able to identify any signals evidencing such a crunch, how is SERV managing this situation and what kind of support can SERV offer?

Herbert Wight is the Director of SERV since December 2009

HW: What we see again and again is that some companies are struggling with liquidity shortfalls. These shortfalls are usually due to the poor order situation in 2009 which caused a drop in revenues. The financial condition of the companies has worsened and banks have become more cautious in granting additional limits for loans or guarantees. In order to receive loans or guarantees, companies often have to provide additional securities, e.g. cash deposits. This constrains their liquidity even more. We support affected companies with the new products introduced within the framework of phase II of federal stabilization measures. In particular, our working capital insurance and counter guarantees support companies facing tight liquidity situations. Both products protect the bank granting the loan or guarantee from default of payment on the part of the exporter. Thus, they enable banks to grant new loans or guarantees without fully charging them to the credit limits of exporters. In this way, exporters are able to preserve their liquidity and have the necessary leeway for further transactions.

AIL: Which products have your customers particularly been requesting during the last 24 months? Do you see any trends?

HW: We see a substantial increase in the demand for insurance of private buyer risks. At the same time, the demand for cover of transactions with bank guarantees and with public buyers is decreasing. This development has been accentuated by the crisis. The financial crisis made it more difficult and more expensive for foreign importers to obtain guarantees from local banks. As a consequence, Swiss exporters are forced to assume buyer risks. But since they are often not able to bear these risks themselves, they need SERV cover.

In addition, we observe an increasing demand for insurances with medium- and long-term credit periods. This is an indicator that banks have grown more cautious about financing transactions with longer terms and request SERV insurance as a pre-condition. This has also been a contributory factor in SERV insuring more transactions in OECD countries such as Germany, France, Greece, Spain and Italy as compared to previous years.

Moreover, demand for the newly launched products, especially working capital insurance and counter guarantees, has been high, right from the start. We anticipate that the demand for these two products will increase even more.

AIL: We see that potential and also current customers of Swiss exporters increasingly ask for tailor-made financial solutions. This means that besides an attractive product, the exporter also needs to offer customized financing solutions. What is the role of SERV in this respect and how flexibly can your insurance be structured?

HW: In general, our products protect exporters from default of payment. Among other things, we cover credits which exporters grant their customers. For example, SERV insurance makes it easier for exporters to assign a supplier credit to a bank. As a consequence, exporters can offer financing to their customers but receive payment immediately. In most cases, this is a win-win situation for the exporter and the buyer.

As an institution under public law, our actions are governed by Swiss legislation, specifically the Swiss Export Risk Insurance Act (SERVG), as well as by international agreements (i.e. OECD and Berne Union). For example, Swiss Export Risk Insurance Act requires that an export transaction must include a certain proportion of Swiss value added, in order to be eligible for cover. The OECD rules, among other things, define international standards on credit periods and minimum insurance premiums for state-covered export transactions. In order to operate flexibly within the framework of these rules, it is important that exporters contact us as early as possible, ideally even before signing a delivery contract. We are then able to advise exporters how

to structure an export transaction, so that they can benefit from our products in the best possible way.

AIL: Is it fair to say that many export transactions could not be executed without the support of SERV?

HW: The feedback we get from our customers again and again is that they could not realize some of their export transactions without our support. The risks of the transactions would be too big for the exporters. Many exporters cannot afford default of payment in the current economic situation. They depend on reliably and quickly receiving their money. SERV insurances make this possible. Moreover, our new products make sure that exports do not fail due to the exporter's lack of liquidity. Last but not least SERV ensures that Swiss exporters are on a level playing field with their foreign competitors. Since most industrialized countries have their own national export credit agency, Swiss exporters would be significantly disadvantaged in international competition without the support of SERV and would not be able to carry out some of their transactions.

AIL: Has SERV's cover practice changed since the start of the financial crisis?

HW: As already mentioned, we launched new products to counteract the negative effects of the crisis and to systematically support Swiss exporters. Moreover, we increased the cover ratio for private buyer risks under supplier credit insurance from 85 to 95 percent. This helps Swiss exporters in carrying out higher risk export transactions. Aside from this, SERV's cover practice has not changed.

AIL: How do you see the future trends in respect of the market's demand for the various SERV products?

HW: As already stated above, we think that the demand for working capital insurance and counter guarantees will further increase. We are convinced that there will be a need for these products even after 2011. Although the global economic situation is gradually recovering, we still see many Swiss exporters struggling with liquidity shortfalls. Moreover, many countries are continuing privatization and so more and more current and potential customers of Swiss exporters will be private companies. This is why we expect that demand for insurance of private buyer risk will further increase.

AIL: The OECD sets the rules and treaties to define common credit standards in international trade. It does this mainly to avoid distortions of competition. How do you think this will develop in the next years, considering the signals of increasing protectionism of industrial countries and the increasingly dominant role which the BRIC-countries, especially China, are playing in the global economy?

HW: A close cooperation within the OECD is very important. Its rules ensure uniform and fair conditions for its members. It is necessary to continue working on the standards, to modernize and revise them in order to keep them up to date. At the same time, we have to try to bring the BRIC-states closer to the OECD regulations. Otherwise we will be disadvantaged compared to the BRIC-countries.

Many thanks for the interesting information!

* About SERV: As a Swiss government institution under public law, Swiss Export Risk Insurance (SERV) covers export transactions of Swiss companies. SERV helps exporters to accept foreign orders when receipt of payment is at risk due to political or economic instability. Most industrialized nations offer exporters public export risk insurance. For this reason, SERV is an important instrument of the Confederation's economic policy. It ensures the competitiveness of Swiss companies that compete on international markets.

EEII (Eastern Energy & Infrastructure Invest) AG – No major changes expected in the Ukraine

The investment objective of EEII is to maximize long-term returns to shareholders through investments in strategically selected companies active in the energy and infrastructure sectors, with a special focus on emerging markets and in particular the former Soviet Union. The Company is currently invested in ten Ukrainian utility companies, Ukrnafta, the premier Ukrainian oil company and Russian Gazprom, the world's biggest gas company.

AIL in its role as investment manager of EEII AG, an investment company listed on the Swiss Exchange SIX, is pleased with the portfolio performance for the year 2010. EEII's net asset value ("NAV") increased in a challenging investment environment by 13.3% from CHF 13.75 to CHF 15.58 per share. The increase in the net asset value was mainly attributable to a strong performance of one of the main stock holdings, Ukrnafta, which represents almost 59% of the portfolio.

The economy of Ukraine showed some signs of recovery. The country's GDP grew 4.8% yoy in the first quarter of 2010. However, it is expected that the state budget for 2010 might still show a fiscal deficit of 7-8% of GDP. Ukraine's economy and financial markets so far proved to be fairly resilient to the turmoil in the Eurozone. This is mainly thanks to the strong export performance and the comparably low intensity of short-term capital flows. S&P recently raised the country's sovereign credit ratings to B/B (foreign currency) and B+/B (local currency) citing "improved policy coordination, the stabilization in Ukraine's external liquidity position and our expectations of an increase in useable foreign exchange reserves relative to short-term debt, and a relatively moderate general government debt burden" as the main reasons for the upgrade. Obviously, the political stabilization played an instrumental role in the improvement of the external accounts as capital inflows accelerated and tapering off depreciation expectations turned balance of payments positive in March 2010.

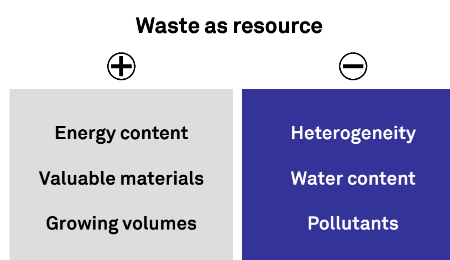
On June 2, President Viktor Yanukovych presented his reform program for 2010, which probably is too cautious to bring about a major change. The

program contains a set of reforms that have been discussed over a long period but have not been implemented due to a lack of political will. They mainly follow what may be called "Ukraine's liberal agenda" – a set of policy directions pronounced in proposals from international financial organizations and think tanks. This agenda envisages privatization, liberalization, fiscal decentralization, public services reforms, targeted social benefits, etc. Experts have assessed the program critically saying that it avoids answering some "uneasy questions". For 2010, mostly three main tasks are on the agenda: First to complete banks' recapitalization by the end of 2010, second to reduce the quorum for shareholder meetings from 60% to a 50% + 1 share and third to eliminate discounts on prices for gas, electricity and transport services for industrial companies.

Carnot Capital Ltd.: Waste to energy – highly attractive in theory, highly complex in practice

Carnot Capital AG is an asset management company, established in July 2007, which manages an investment fund open to qualified investors. The fund pursues a value approach and concentrates on companies within the energy sector. Specifically the fund invests in listed companies that create value by enabling a more efficient use of energy. Carnot Capital AG is an associated company of AIL Structured Finance Ltd. For further Information: www.carnotcapital.com

Waste to energy – highly attractive in theory, highly complex in practice: In May, an expert on waste treatment from the Canton of Zurich gave a presentation for Carnot Capital. In particular, the eligibility of waste as an energy source and its attractiveness as an investment topic was debated. Currently only about a fifth of waste is used for recycling or energy extraction, four fifths is shipped to landfills. As a matter of fact, waste could replace a very substantial amount of fossil fuel: The available and technically usable energy from waste is equivalent to 3,000 mn barrel oil per year, i.e. over one month's global oil consumption! The pulp and cement industries are clearly the furthest advanced in using waste as energy and raw material source. While the pulp industry burns wood waste (branches, bark, trunks), the cement industry burns various types of waste in the so-called co-processing, be it old tires, chemicals or plastics. A lot of work is undertaken to develop new technologies which can extract the energy from waste or direct valuable waste substances back into the value chain. It seems that the technical challenges often are underestimated, particularly in the initial separation of heterogeneous waste.



Up to now, quite a few plants had to be mothballed due to persistent technical problems. Besides the technical operation the economics of using waste as an energy resource are a challenge, too. Using fossil fuels and dumping waste is often still the less costly alternative. The waste to energy market will become more attractive to institutional investors when the external costs of burning fossil fuels and disposing waste in landfills are internalized, i.e. when emitting greenhouse gas will be subject to greater taxes and dumping waste becomes more expensive or prohibited.

Opportunity for Investors

AIL in its role as financial advisor currently is looking for:

⇒ Lead-Investor for a **99MW wind park in Bulgaria**. The project is fully developed and will be fully permitted in summer 2010; two independent wind studies are available. Start of construction is scheduled for spring 2011. The project is being developed by an experienced German wind development company with an impressive track record. The project developer seeks a lead investor to finance the construction of the plant. Requested equity amount for the completion of the project is between € 50-57 Mio. For any further information please contact Mr. Andres Heusser, +41 43 299 62 11, andres.heusser@ailsf.ch

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