Auckland Light Rail

DRAFT FOR DISCUSSION

IBC Phase financing discussion document

Auckland LIGHT RAIL
Bringing us closer

Process & progress

Process / financing workstream through IBC phase

By its nature, the financing workstream is led by development of delivery entity, funding and procurement workstreams. Specific focus has been on narrowing to potential approaches to financing to support the IBC and advice to Ministers. Further articulation and development of financing options to a preferred financing structure will only be possible during DBC phase

Workshop: Discussion of evaluation criteria and financing options

IBC work product development

Further discussions (if required) & DBC next steps

Development of long list

The long list will cover the full range of potential options.

The focus of the options will be on project specific financing options.

Where possible, international and domestic precedent will be identified and leveraged.

Consider financing sources and options for different phases of the project.

Consider whether (and to what extent) Crown support is provided for financing or finance-related risks.

Development of evaluation framework

A multi-criteria evaluation framework is proposed, covering the core financing objectives & implications.

Update of evaluation criteria & development of funding options

High level evaluation of each of the financing options and approaches against the multi-criteria to obtain a short list.

Further detail on Crown vs Delivery Entity financing

Build out further detail on Crown vs Delivery Entity financing structures and undertake indicative assessment for the purposes of the IBC.

Assessment based on a qualitative judgement against each factor (e.g. high, medium, low).

Considerations & implications

Articulation and development of financing options only possible during DBC phase, with further development of delivery entity, funding and procurement workstreams.

We note that the financing options outlined in this pack are not binary and the preferred financing structure for the Project could incorporate elements of options presented

Indicative evaluation criteria (following initial workshop)

Criteria	Description (red highlights are minor updates to the criteria suggested in the workshop)
Implementation and deliverability	The extent to which the financing options could be easily implemented and delivered, with minimal execution risk and maximum financing certainty. Factors such as potential to be impacted by the then state of financial markets will be considered
Value for money	Assessment of the extent the financing options provide value for money. This criteria will include minimising the cost of capital to drive value but will also consider how value of funding sources is maximised
Flexibility	The extent to which the financing options are sufficiently flexible to allow different technical options, decisions, phases of the project, responses to market liquidity/illiquidity, market changes (e.g. sector reform). A key consideration under this criteria will be the flexibility of options to respond to future project requirements (e.g. if further augmentations or extensions to the ALR project were undertaken)
Impact on Crown partners	The extent to which the financing options impacts the Crown partners. Key considerations under this criteria will include impact on the Crown partners balance sheet, fiscal indicators, the amount of Crown support required and how costs are able to be spread over a period of time so as to reduce any up-front burden on the Crown (including the NLTF)
Risk transfer	The extent to which the financing option mitigates both project and financing risks
Wider considerations e.g., ability to access sustainable or ESG finance options	The wider considerations and impacts of each option will also be considered, including ability to leverage different sources of capital or to further leverage funding streams

Narrowing of financing options since initial workshop

Key actions, information and outcomes since initial workshop

- We have undertaken a high-level evaluation of a Crown vs Delivery Entity financed approach for the purposes of the IBC
- Based on the initial options assessment and the preliminary, IBC phase, evaluation shown on slide 8, a financing structure that utilises Crown financing through the DMO is currently preferred over a structure whereby the Delivery Entity raises financing from the capital markets
- However, further assessment and development of the options, and deciding on a preferred financing solution, will occur during the DBC phase and will be heavily influenced by a range of factors, including the preferred transport solution, Delivery Entity scope and governance structure, procurement strategy, funding solution and the urban development approach, which all feed into the key question of 'what' is being financed
- It is important to note that the financing options outlined in this pack are not binary and the preferred financing structure for the Project could incorporate elements of both options, if optimal
- Financing workstream will be heavily influenced by the funding solution. The funding workstream has been undertaking a narrowing and estimate of the quantum of funding options. Two key pieces of advice are being produced:
  - Detailed funding advice: detailed overview of the capacity for different Crown and Council organisations to contribute to the project, potential levers available to each organisation to fund a contribution, balance sheet considerations and policy / wider trade-offs and considerations.
  - Value Capture Advice: detailed overview of a select range of value capture tools, including the potential application to the project, impact on beneficiaries, and key trade-offs. A couple of case studies will be included, which focus on the practical application of the selected tools.
- Financing strategy also continues to depend on a number of market facing aspects e.g., market conditions, appetite, cost of debt, tenor, volume, credit rating, risk transfer etc. We will seek input from the market during the DBC phase on those

Key factors used to assess options at DBC stage

Funding solution – the financing approach will be directly impacted by what we consider are the major funding sources, including the nature and extent of Crown funding and in relation to any funding or cost sharing arrangements between Crown, Auckland Council and others

Market appetite and conditions – financing strategy will depend on a number of different aspects e.g., market conditions, cost of debt, tenor, volume, credit rating, risk transfer etc. We believe there will be appetite from the debt capital markets for a Delivery Entity financed solution. However, it is too early to engage with market in IBC phase given the level of project and commercial detail

Crown involvement – Crown appetite for the provision of financing or support in respect of Crown or Delivery Entity financed approach. To be assessed in the context of the preferred funding approach

Procurement approach - Procurement, packaging and contractual terms will impact on the preferred financing approach. We would expect the financing workstream to provide further input as to the suitability of a privately financed package

Delivery Entity and decisions on scope – delivery entity form, scope, governance and powers, including in relation to the urban development approach will impact on the financing approach. The approach to urban development and how those aspects are either funded and/or financed separately or are integrated with the delivery of the core transport infrastructure

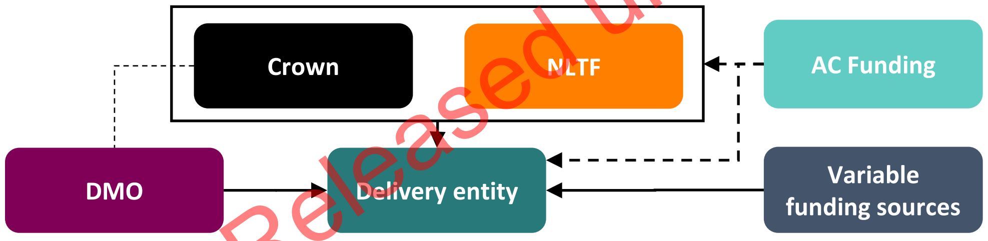
Financing options

Options for financing ALR

There are two main financing approaches that could be utilised for the financing of the ALR project

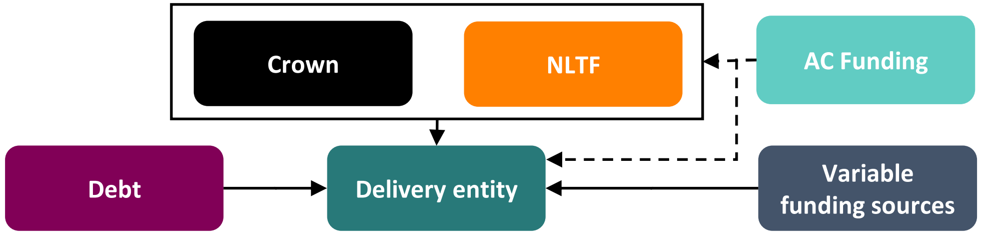
Crown financing

- Financing raised by the Crown with DMO providing the debt in accordance with a pre-determined schedule
- A variant could involve NLTF raising debt from either DMO or commercial lenders directly. However, this feels unnecessarily duplicative vs direct-DMO option and commercial lenders would likely require Crown support given the nature of the NLTF and competing demands on it given projects envisaged
- The Crown would be responsible for servicing the debt with no direct obligation of the Delivery Entity. However, we note that the arrangement could be structured as a loan with a repayment obligation
- Flexibility of DMO-based solution from a timing perspective will dictate whether DMO-raised finance will need to be supplemented with a commercial revolving credit facility (RCF) to manage timing of project payments. Early indications are that a Crown/DMO solution could provide sufficient flexibility
- The Crown (and potentially AC) would also fund development/early stage/transition costs and ongoing operating costs, with variable funding sources potentially leveraged to offset any Crown, NLTF and AC funding requirements
- No explicit Crown support for financing required but Crown effectively takes risks that cannot be passed through procurement



Delivery Entity financing

- Debt financing is raised by Delivery Entity based on future revenue stream. This allows the entity to borrow as required and leverage off future committed revenues. This could be commercial debt.
- Delivery Entity has a high level of autonomy in structuring its financing arrangements, utilising the best combination of debt capital market products, dependent upon funding and procurement approach
- The Delivery Entity would receive ongoing funding during construction from the Crown, NLTF and AC. Funding would be used to meet debt servicing and operating costs
- Variable funding sources retained (and potentially leveraged) to offset the financing and any Crown, NLTF and AC funding requirements
- Crown, NLTF and AC financing options could be used to supplement a Delivery Entity led financing solution
- Crown equity, either actual or uncalled, will be required (assuming that introduction of private equity will not be favoured on policy grounds)
- Crown support e.g., for construction tail and finance related risks will likely be required to secure a cost of capital finance that is competitive relative to the Base Case

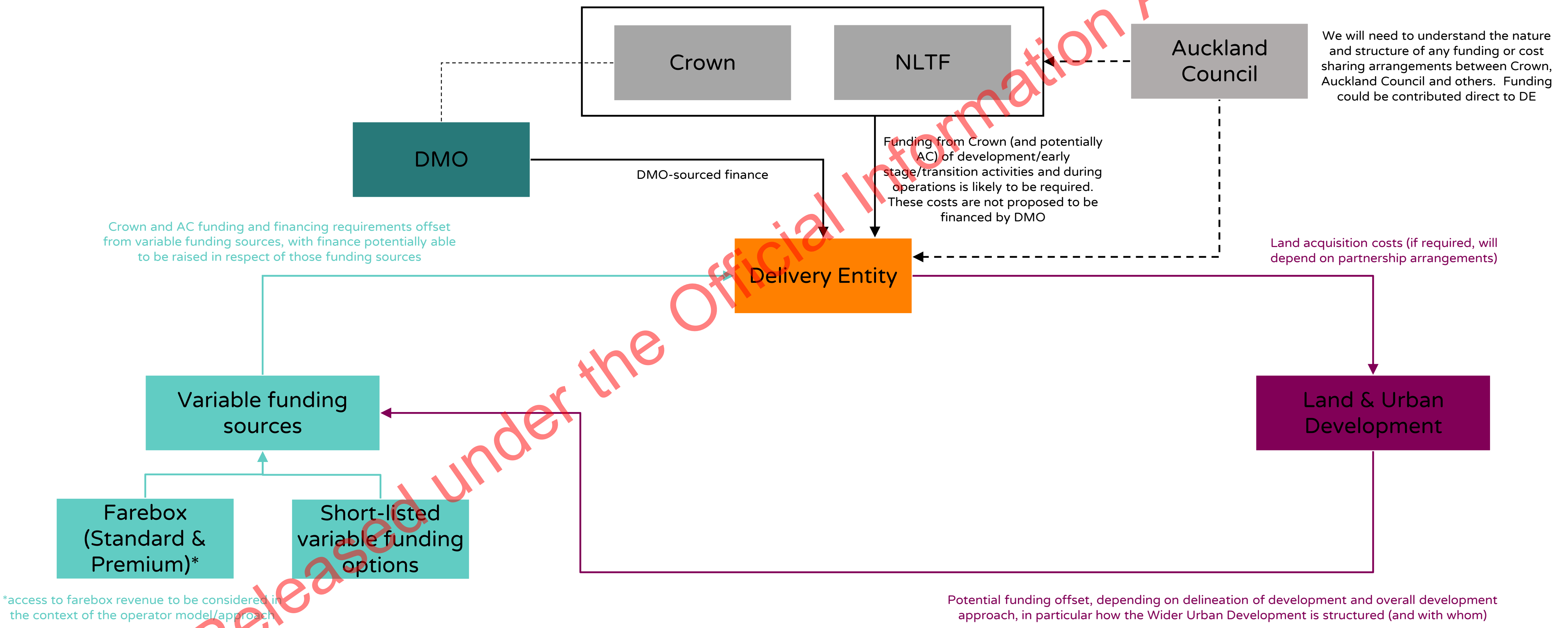


Indicative evaluation criteria (following initial workshop)

Criteria	Description	Crown financing	Delivery Entity financing
Implementation and deliverability	The extent to which the financing options could be easily implemented and delivered, with minimal execution risk and maximum financing certainty. Factors such as potential to be impacted by the then state of financial markets will be considered	If a DMO-based solution is supported from a policy perspective, then it is likely to be able to implemented quicker than a Delivery Entity financed solution.	If a DMO-based solution is supported from a policy perspective, then it is likely to be able to implemented quicker than a Delivery Entity financed solution.
Value for money	Assessment of the extent the financing options provide value for money. This criteria will include minimising the cost of capital to drive value but will also consider how value of funding sources is maximised	DMO-based solution will likely provide a lower WACC than a Delivery Entity financed solution.	A Delivery Entity financed solution will have a higher cost of capital than a Crown/DMO-based solution. A more definitive estimation of the delta will only be possible during the DBC phase
Flexibility	The extent to which the financing options are sufficiently flexible to allow different technical options, decisions, phases of the project, responses to market liquidity/illiquidity, market changes (e.g. sector reform). A key consideration under this criteria will be the flexibility of options to respond to future project requirements (e.g. if further augmentations or extensions to the ALR project were undertaken)	Flexibility of DMO-based solution from a timing perspective will dictate whether DMO-raised finance will need to be supplemented with a commercial RCF to manage timing of project payments but working assumption is that requisite flexibility can be structured and/or an RCF can be structured alongside a Crown financed solution that would not materially impact the cost of capital advantage noted above.	Delivery Entity has a high level of autonomy in structuring its financing arrangements, utilising the best combination of debt capital market products, dependent upon funding and procurement approach. A Delivery Entity financed solution is unlikely to have as much flexibility to respond to project requirements e.g. if further augmentations or extensions to the ALR project were undertaken.
Impact on Crown partners	The extent to which the financing options impacts the Crown partners. Key considerations under this criteria will include impact on the Crown partners balance sheet, fiscal indicators, the amount of Crown support required and how costs are able to be spread over a period of time so as to reduce any up-front burden on the Crown (including the NLTF)	DMO financing will be treated as Core Crown Debt and will be factored into credit rating agency assessments of the NZ Sovereign rating. We do note that the current assessment of credit ratings agencies of the NZ Sovereign is positive at (AAA: S&P and Fitch; Aaa: Moody's). Recent engagement on reform processes have indicated that amounts comparable to the potential ALR cost would not negatively impact that positive assessment. However, this will need to be confirmed with ratings agencies in the DBC phase.	A Delivery Entity financing structure may be able to be structured so that debt would not be included in the Crown debt burden
Risk transfer	The extent to which the financing option mitigates both project and financing risks	Crown has direct obligation to repay the finance so no further Crown support required. Crown effectively takes risks that cannot be passed through procurement. Aside from comment in relation to use of private finance, risk transfer position is very similar between the two options with risks not transferred having to be back-stopped by Crown in either case	Financing will not drive additional transfer unless private finance is utilised in the structure. Will work in tandem with procurement workstream in next phase to see whether risk transfer vs increased cost of capital is sufficient to justify Crown support e.g., for construction tail and finance related risks, will likely be required to secure a cost of capital that is competitive with the Base Case
Wider considerations	The wider considerations and impacts of each option will also be considered, including ability to leverage different sources of capital or to further leverage funding streams	Crown will need to consider the precedent nature of a Crown financed solution in terms of other, large scale, procurements and projects in NZ. No distinguishable difference between the two different options in terms of the ability to utilise or leverage different sources of capital.	No distinguishable difference between the two different options in terms of the ability to utilise or leverage different sources of capital.

Crown-based financing structure

Noting further assessment of options is required in the DBC phase, a financing structure that utilises Crown financing through the DMO, with funding and financing offsets from variable sources, is currently preferred over a structure whereby the Delivery Entity raises financing from the capital markets



Next steps & action items

Timeline for development of financing solution

Development and agreement of the preferred ALR financing will lag the funding solution and is expected to be landed during the DBC phase, in advance of DBC submission

IBC submitted

IBC approval

DBC submitted

DBC approval

Award of major contracts & FC / availability of finance*

IBC development → Gateway 1: IBC Approval

DBC development → Gateway 2: DBC Approval

Consultation & Consenting, Delivery Strategy & Procurement → Gateway 3: Major contract award

Initial development of funding solution in IBC phase

Development and agreement of ALR funding approach and mix

Funding of early stage activities → implementation of funding solution

Initial development of financing solution in IBC phase

Development and agreement of preferred ALR financing approach → Financial Close / availability of finance

- Further assessment and development of the options, and deciding on a preferred financing solution, will occur during the DBC phase and will be heavily influenced by the preferred transport solution, Delivery Entity and governance structure, procurement strategy and funding solution and the urban development approach
- Development and agreement of the preferred ALR financing will lag the funding solution and is expected to be landed during the DBC phase, in advance of DBC submission

* Actual timing of all of major contract award(s), contractual close and financial close will vary depending on the procurement approach and ultimate funding and financing solution

Next steps / action items for DBC phase

Though a Crown financed solution that utilises the DMO is likely to be preferred, development and agreement of the preferred financing solution will only be arrived at during the DBC phase

- Detailed assessment of Crown and Delivery Entity financed approaches, in particular the optimal financing structure for the Delivery Entity financed approach (utilising the long list of financing options previously discussed)
- It is important to note that the financing options outlined in this pack are not binary and the preferred financing structure for the Project could incorporate elements of both options, if optimal
- DBC will allow financing workstream to further understand:
  - Preferred technical option
  - Quantum and timing of project costs during construction and operating phases
  - Delivery entity form, scope, governance and powers
  - Funding options, in particular quantum, structure, timing, certainty of funding stream to inform likely quantum of finance able to be raised and to ensure that any costs to service financing are factored into the sufficiency of funding sources
  - The nature and structure of any funding or cost sharing arrangements between Crown, AC and others
  - Preferred procurement approach (with the financing workstream providing input as to the suitability of a privately financed package)
  - Crown appetite for the provision of support in respect of a Delivery Entity financed approach and whether such support is VfM
- The above all feed into the key question of 'what' is being financed
- We will need to undertake detailed market sounding during DBC with debt capital market participants to inform assessment of relative merits
  - Financing strategy continues to depend on several factors e.g., market conditions, cost of debt, tenor, volume, credit rating, Crown support, risk transfer etc.
  - Engagement with credit rating agencies to understand implications of Crown vs Delivery Entity financed options and impact on Crown/Sovereign rating (if any)
- A financial model will be developed during the DBC that will allow a more direct and specific comparison between both Crown financed and Delivery Entity financed options
- Retest, compare and contrast a Crown financed vs preferred/optimal Delivery Entity financed approach to identify the preferred financing option for the purposes of the DBC