

# **Chapter 1 - Introduction**

## **1.1 Overview and objectives of study**

Malaysia intends to transform into a fully developed nation by the year 2020. The Malaysian Government has been gearing up aggressive development policies to realise the country's ambition. Acceleration of the privatisation programme under the Seventh Malaysia Plan can only mean that more infrastructure projects are in the pipeline. More often than not these projects require huge amounts of funding and involve high risks and a range of parties with different priorities or interests vested in the project, legal political or economical. As such the techniques of project finance are applied as the appropriate financial vehicle.

Project finance is a specialised field of financing applicable to a wide range of projects or ventures particularly capital intensive and large scale infrastructure projects. Hence, with the Malaysian Government pressing for Vision 2020, our country is poised to be a potential growth area for project finance. In fact it has been said that Asia particularly Eastern, Central and

South East Asia, Central and Eastern Europe are the growth areas for project finance in the future.

Appendix A provide some tables with data or forecasts on investment resources requirement for infrastructure development for Asian region, comparisons between Malaysia and some similar size countries on various infrastructure aspects etc.

In view of the growing importance of project finance, the main objective of this research or study is to analyse the methods or techniques practised by local bankers in accomplishing successful project financings, so as to obtain a better understanding of this field of financing and its application. It is hope that this study will advance the knowledge on project finance in view of the scarcity of local literature in this sector of finance.

However, in view of some limitations (see Section 1.2) this study did not comprehensively review or research the entire framework of project finance. Nevertheless this report will be useful as it will provide readers with some basic understanding of what "project finance" is. It should serve to provide a conceptual starting point for the further development of the reader's ideas on project finance.

More importantly perhaps, it will provide readers, who are yet to be exposed to project finance, with some knowledge and understanding of the

basic evaluation process or techniques of project finance practised in this country. It is the writer's opinion that the same techniques are applicable to cross-border projects with some necessary adjustments in view of the different legal and political connotations.

This report comprises two main parts. The beginning part, namely Chapter 2, aims to highlight some of the characteristic features of project finance as an introduction to the reader to the field of project finance. The Chapter reports the findings on the characteristics of project financings in this country covering aspects such as the common or basic elements, the types of projects, the contractual structure of the projects, the parties involved and the stages of project finance.

The second or final part of this report, namely Chapter 3, deals more directly with the concerns of the lenders namely evaluation of the project to determine its feasibility for financing. Specifically covered are methods such as project risks analysis and financial analysis.

## 1.2 Methodology

Most of the information or data collected in this study is through secondary sources. Primary data are also used, that is, from non-random and unstructured interviews and discussions with local bankers involved in the field of project finance. The sample size comprises 15 bank officers and project analysts from four local financial institutions, namely, a commercial bank, a merchant bank, a discount house and a financial advisory firm. Some of the relevant issues and questions asked in the interviews are presented in Appendix B attached.

The sources of the secondary data includes the following :

- a. Written material and papers from seminars and courses relating to project financing conducted by private firms;
- b. Published and unpublished articles, newspapers, journals, legal contracts, information memorandum, feasibility reports on project evaluation etc.;
- c. Financial magazines and publications such as Project Finance International by IFR Publishing Ltd, Asiamoney by Euromoney Publications PLC, Malaysia Infrastructure, etc.

The method of this study is to analyse the data collected for information relating to the characteristics of project financing practised in this country covering aspects such as the common or basic elements of such financings, types of projects financed, the contractual structures the projects, the parties involved and the stages of the financing. An important aspect of this study is to analyse the evaluation process undertaken or practised by local bankers to establish a project's feasibility for financing. Specifically analysed are the methods and techniques used such as project risks analysis and financial analysis. Project details are also analysed to provide for illustrations in this report.

This study intends to cover as much as possible about the practice of project finance. However, initial attempts to obtain material especially local ones on the subject prove to be difficult as no references were found in the library of University of Malaya. The writer was fortunate to have the assistance of some local bankers who provided some relevant publications and material. In addition, they have provided the most valuable data, namely, their opinions, knowledge and experience on the subject matter as well as insights on actual project evaluation process. However, for confidentiality reasons and in view of the restrictions imposed by the Banking and Financial Institutions Act 1989, only certain information regarding the projects that have been evaluated could be disclosed, that is, information which have already been made to the public.

In view of the above, this study did not comprehensively review the entire framework of project finance. As the data obtained are limited, the opinions and conclusions expressed in this report should not be taken as the authority on project finance.