Lessons of the Chad-Cameroon Pipeline Financing

A Case Study in Project Financing and Political Risk Mitigation

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Abstract

Major corporations with strong balance sheets use project financing for different reasons. Typically they are less interested in leveraged returns or stretching their debt capacity. Instead, project financing is used to fund joint ventures without over-financing weaker partners; at other times it becomes a risk management tool. This latter motivation is most often evident when an otherwise attractive project is located in a politically risky nation.

The Chad-Cameroon Pipeline Financing is perhaps the premier example of project financing undertaken to mitigate political risk. The long history of the project – it took some thirty years to commercialize oil found in the 1970‟s – testifies to the sponsors' aversion towards the project's political risks. Their ultimate solution was unique; a host of Export Credit and Multilateral Agencies were involved in the financing, topped off by the participation of the World Bank. The sponsors sought the Bank's involvement for its "deterrent" effects on the host governments of Chad and Cameroon.

As its price for participating, the World Bank insisted that Chad adopt a "Revenue Management Plan" (RMP). The RMP's purpose was to assure that government income from the project would be invested in bona fide development projects. The financing was completed and the project started up in late 2003. Thereafter, Chad and the World Bank had several confrontations over the RMP‟s operations. Ultimately, the Bank asked Chad to repay its loans and allow it to withdraw from the project. The private sponsors, however, weathered the 2008 oil price peak with their deal terms essentially intact.

This case study involves another company considering a resource project in another undeveloped country. The project involves LNG, not oil. Members of the finance team debate whether project financing with ECAs will be sufficient to protect the sponsor's terms from government pressure tactics. One member of the team forcefully argues that only the presence of an Agency like the World Bank can protect the deal's fiscal terms. The team's leader is not convinced that the added protection will be worth the costs and complications that the World Bank brings. She asks that the "Lessons of the Chad-Cameroon financing" be carefully examined before deciding.

The case thus asks students to examine whether this LNG project is as exposed as was the Chad oil venture, whether the World Bank's involvement would bring significant incremental protection, and to value that protection versus the risks of added costs and of

project delay.