KOCHI R-LNG PROJECT

Syndicated Project Finance Deal for Petronet LNG Ltd.

LNG

Liquefied Natural Gas ("LNG") is a convenient and cost effective option for transporting gas over distances greater than 2000 km offshore and 4000 km onshore. It is therefore emerging as one of the most rapidly growing fuel options and today accounts for more than 25% of the gas trade worldwide. Over the next 10 years or so, while the US and the European markets are expected to be saturated with the piped natural gas supplies from Canada, Russia and North Africa, the Asia Pacific region is likely to emerge as major demand hub for LNG. Additionally, its strategic location between the two major LNG producing hubs viz the Middle East and Australia would enable the Asia Pacific region to tap a sizeable chunk of the LNG trade flows.

As per various estimates, by the year 2012, the domestic demand for gas in India is expected to be around 280 mmscmd while the supply would be around 180 – 200 mmscmd. Thus, there would be a significant demand-supply gap, which has to be met through imports and a sizeable chunk of these imports would be in the form of LNG. Thus the Indian market offers a strong business rationale for building new LNG import infrastructure. The Kochi LNG Terminal of Petronet LNG Ltd ("PLL") will be the first LNG terminal in southern India and the fourth LNG terminal of country (after Dahej, Dabhol and Hazira).

Petronet LNG Ltd

PLL is a public limited company promoted by four public sector 'Navratna' oil and gas companies of India viz. Bharat Petroleum Corporation Limited ("BPCL"), GAIL (India) Ltd. ("GAIL"), Indian Oil Corporation Limited ("IOCL"), and Oil and Natural Gas Corporation Limited ("ONGC"). Each of the aforesaid promoter companies holds 12.5% of the issued equity share capital in the Company. Gaz de France ("GDF"), a strategic investor, holds 10% of the issued equity share capital in PLL through its investment arm, GDF International. The Asian Development Bank ("ADB") holds 5.2% of the equity of PLL while the balance 34.8% is held collectively by the public investors, FIIs, mutual funds etc. PLL was the pioneer in the field of LNG in India and is currently the largest domestic importer of LNG in the country.

Current Operations of Company

The Company owns and operates an LNG Regasification terminal of 5 MMTPA capacity located at Dahej, Gujarat which is being expanded to 10 MMTPA capacity ("Dahej Projects"). The use of strong vendors coupled with the strong experience of the

Sponsors in executing large projects enabled PLL to successfully complete Phase-I of Dahej Projects (i.e. the Greenfield R-LNG terminal) on time and within the estimated budget. The Company is also on course to commission the Phase-II of Dahej Projects (i.e. the R-LNG terminal expansion) well within the scheduled time and cost. The Dahej Projects have been structured in a manner that allocates critical risks to external parties best suited to handle them by entering into back-to-back contracts with counterparties. The Asian Development Bank ("ADB") has provided a term loan facility of Rs 675 crore equivalent to PLL to refinance part of its existing domestic rupee debt for Phase-II of Dahej Projects, thereby reducing the effective cost of funding to the Company

Phase-I of Dahej Projects commenced commercial operations in April 2004 and the Company made cash profit in the very first year. The tram line model adopted by the Company with back to back LNG & RLNG sale and purchase agreements provides a stable cash flow to the Company. The profitability of the Company is showing continuous growth on account of (i) superior management of the operations resulting in savings in operating costs; and (ii) additional revenues from spot gas regasification. In FY 2007-08, the Company reported a net profit of Rs. 4746.5 million and had a cash surplus of Rs 8846.8 million as on 31st Mar 08 to meet the equity requirement for the Kochi Project.

PLL has established and developed the Spot market in India and has established business relationships with almost all the renowned LNG suppliers in the world. The LNG cargoes have been procured at very competitive prices. PLL has been selling most of the LNG sourced from the Spot markets for use in the power sector and fertiliser sector which have huge demand for gas to feed gas fired power plants and also to replace Fuel Oil/Naphtha.

The Kochi Project

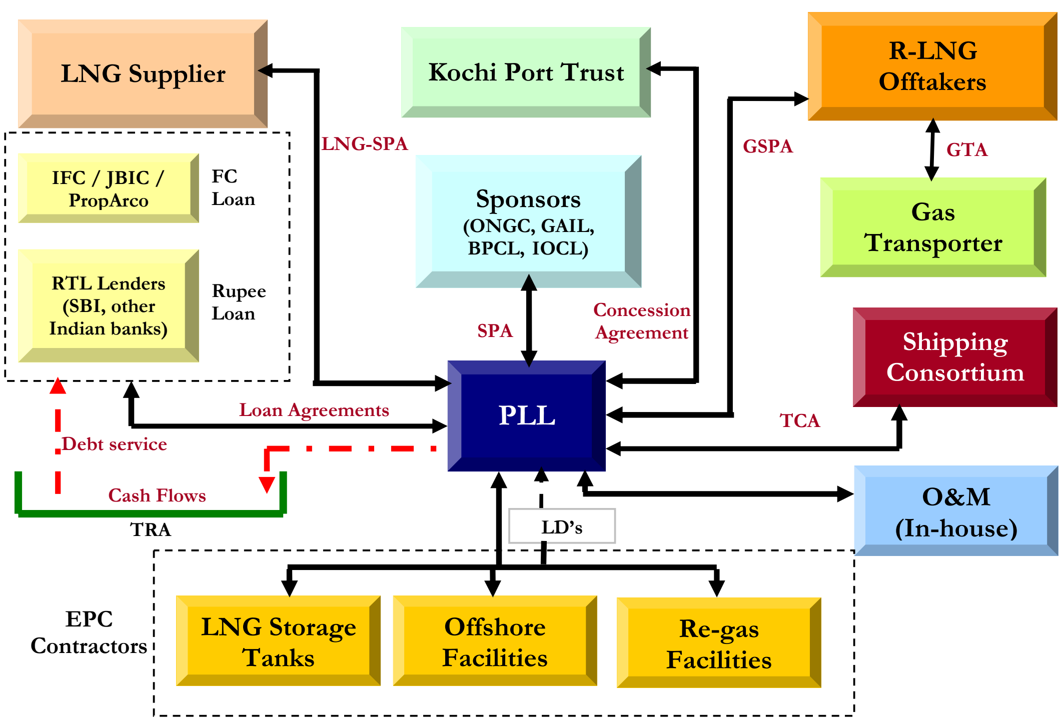
The Kochi Project is a Greenfield LNG Regasification terminal to be set at Puthuvypeen Special Economic Zone (SEZ) at Kochi, Kerala on land allotted by the Kochi Port Trust. The Project involves setting up of (i) 2 LNG Storage Tanks, each of 160,000 m^3 storage capacity of full containment type for storing LNG and allied facilities / equipment for boil-off gas recovery, gas vapourisation, transmission & unloading of LNG ; (ii) Send out and Regasification Facilities suitable for handling 2.5 MMTPA of LNG along with the associated facilities; (iii) Marine or Offshore facilities including the jetty, berthing / unberthing and mooring / unmooring of LNG Tankers and other associated facilities required for all weather operations of LNG ships of nominal capacities ranging from 65,000 to 216,000 m^3; and (iv) a captive Power Plant.

In order to optimize the cost of the Project and also taking into consideration the different timelines for LNG Tanks, Off-shore Facilities and Regasification Unit, the Company is implementing the project through three separate EPC contracts for construction of (i) the LNG Storage Tanks, (ii) the Off-shore Marine facilities and (iii) the Regasification Facilities. LNG Tanks are highly specialized and long lead items and take about 4 years to be completed, accordingly the Company has already awarded EPC contract for two LNG storage Tanks on fixed and firm lump sum turnkey basis to M/s IHI Corporation, Japan, who were the EPC contractor for Dahej Projects of PLL also, in March 2008. The Company is following global competitive bidding process for award of other two EPC contracts.

The as-built cost for the Kochi Project is estimated at Rs. 34,265.5 million which includes a foreign cost component of USD 231.5 million. The construction works have already begun at site and will take 4 years to complete. The terminal is expected to commence commercial operations from 1st April 2012 and will fulfill consumer demand primarily in southern India.

Proposed Contractual Structure for Kochi Project

The figure below depicts the proposed Contractual Structure for Kochi Project



SPA – Share Purchase Agreement
LNG SPA – LNG Sale Purchase Agreement
TRA – Trust and Retention Account
GTA – Gas Transport Agreement
TCA – Time Charter Agreement
GSPA – Gas Sale Purchase Agreement

The contractual structure for Kochi Project would also be similar to the tram line model followed for the Dahej Projects. The Company proposes to source LNG from the Gorgon Project in Australia, which is promoted by Chevron (50%), Exxon Mobil (25%) and Shell (25%). The TCA, GSPA and GTA will be executed on back-to-back basis with the LNG SPA. PLL will also be hiring two LNG vessels under long term charter and has also acquired 3% equity stake in the special purpose company formed to own and operate LNG tankers that would be utilized to transport LNG to the Kochi Project.

Financing Arrangement for Kochi Project

SBI Capital Markets Limited ("SBICAP"), India's premier and leading Investment Bank, which is also ranked by PFI as Globally No.2 and Asia Pacific's No. 1 Mandated Lead Arranger for H1 2008 was the Sole Financial Advisor & Mandated Lead Arranger for the Rupee Term Loan and LC facilities for PLL. SBICAP has been associated with PLL throughout the transaction right from inception by carrying out the financial appraisal of the Project till the time of financial closure and the signing of the loan agreements for the rupee loans on 24th October 2008.

The Kochi Project shall be funded through debt and equity in the ratio 70:30. The financing structure for the Kochi Project summarized as under:

Project Cost	Rs 34265.5 million
Means of Finance	Debt & Equity in the ratio of 2.33:1
Total Equity	Rs 10265.5 million, to be funded out the internal generations of PLL (i.e. cash flows from Dahej Projects)
Total Debt	Rs 24000 million
Foreign Debt	USD 250 million, provided by IFC (Washington)
Rupee Debt	Rs 14000 million, lead arranged by SBICAP

PLL has tied up US$ 150 million loan (Tranche A Loan) direct loan for International Finance Corporation IFC (W) for a 13.5 year door to door tenor, besides they have the option to avail further US$ 150 million 'B' loan which may be sold down by IFC (W). Additionally, the Company has firm offers from JBIC of Japan for a facility of upto US$ 500 million and from Proparco Bank of France for a facility of upto US$ 100 million. PLL may avail the above facilities at a later stage under the IFC (W) 'B' loan or independently.

Rupee Term Loan Facility Lead Arranged by SBICAP

A Consortium of 10 Indian Lenders led by the State Bank of India have, on 24th October, 2008, committed a 13-year project finance term loan aggregating Rs 14000 million (equivalent to US$ 280 mn) to PLL, for setting up the Kochi Project. The transaction is a unique Syndicated Project Finance deal and the Lenders to the Project are Canara Bank (Rs 2500 mn), J&K Bank (Rs 950 mn), Oriental Bank of Commerce (Rs 950 mn), State Bank of Hyderabad (Rs 950 mn), State Bank of India (Rs 4000 mn), State Bank of Indore (Rs 700 mn) , State Bank of Patiala (Rs 500 mn), State Bank of Travancore (Rs 950 mn), Syndicate Bank (Rs 2000 mn) and The Federal Bank (Rs 500 mn).

M/s Amarchand Mangaldas Suresh A Shroff & Co was the Lender's Legal Counsel while M/s Phoenix Legal advised the Company on the transaction.

The key terms of the INR debt are as under:

Key Terms of Rupee Debt	
Tenor	13 years (4 years construction + 1 year grace + 8 years repayment)
Pricing	Floating, negative spread of 125 bps to the State Bank Advances Rate ("SBAR")
Reset of Pricing	o With every change in SBAR till the earlier of (i) COD or (ii) 48 months from Agreement signing date o Annually Thereafter o Negative spread of 125 bps will remain fixed throughout loan tenor
Upfront Fee	10 bps of the commitment amount
Repayment	32 quarterly instalments commencing after one year from the earlier of (i) COD or (ii) 48 months from the date of agreement signing

Uniqueness of the Financing Structure

The transaction has been structured to allow PLL the flexibility to change the financing mix during the construction period to suit the requirements of the Project. SBICAP has helped PLL negotiate with the rupee lenders for an option that will enable PLL to replace upto Rs 6000 million of the Rupee loan by raising further loans from Export

Credit Agencies (ECA), External Commercial Borrowings (ECB) and / or Multilateral agencies without payment of any charges / penalties in addition to INR 10000 million.

The other salient features of the Kochi Project financing are highlighted below:

- Project finance loan of 13 year tenor without recourse to the Sponsors.
- Participation of multilateral funding agencies like the IFC (W) for the foreign currency portion of the debt which reflects the inherent strength of the Project and robustness of the contractual arrangements proposed to be implemented in the Kochi Project.
- As many as 10 domestic lenders participated in the rupee debt with State Bank of India (SBI) being the Lead Bank
- Flexibility to the Borrower to reduce / refinance part of the rupee loan through further INR 6000 million borrowings from ECA /ECB/ Multilateral Agencies without any penalty, in order to reduce the effective cost of funding.
- The pricing of the Rupee loan is structured in such a way that it protects the interest of both the Borrower and the Lenders through linkage to the SBAR which is a well accepted benchmark and reflective of the credit situation prevailing in the economy. The Interest Rate is fully floating during construction period which means that any change in SBAR will change the pricing of RTL. In fact, post signing the SBAR has been reduced by 75 bps and PLL will have the advantage of the same. The interest rate post construction will be reset annually based on the SBAR prevailing at the time of reset.
- The structure also gives the Borrower the flexibility to pre-pay whole or part of the loan, post COD, without any penalty (i) at any time, out of its internal accruals; or (ii) on any of the interest reset dates; by giving a 60-day notice to the Borrower. This gives the Borrower the avenue to leverage its strong cash flows from operations and / or replace its rupee loan with cheaper borrowings, once the construction risk is over.
- The risk borne by the Lenders of the Kochi Project is significantly mitigated by (i) the robust contractual structure which allocates most of the risks to external competent counter-parties; & (ii) the gradually increasing share of spot / short-term sale arrangements which provide additional flexibility to operations.
- The Domestic Lenders Consortium has also sanctioned DSCR LC facility of INR 1200 million, Stand by LNG LC facility of US$ 120 million and Working Capital Facility of INR 2000 million for the Kochi Project.

Key Challenges Faced in the Financing Structure / Process and How They Were Overcome

❖ ***Increase in Project Cost***

The deal was originally launched for syndication in July 2007 at a lower Project cost of Rs 25940 million, based on the in-house estimates of the company. Subsequently when the EPC contract for the two LNG Storage Tanks was awarded by the Company, there was a substantial increase in the EPC cost on account of (i) requirement of higher piling work for the tanks due to soft soil conditions at site; (ii) substantial increase in prices of steel, cement and other materials required for construction; & (iii) tight order book position of EPC contractors the world over. As a result, there was an increase of around Rs 8325 million in the Kochi Project cost. The proposal was then re-launched in March 2008 with the revised project cost; this led to a series of meetings / interactions with Lenders for demonstrating to them the financial viability of the proposal in the revised costs scenario.

❖ ***Volatility in the interest rate scenario and liquidity conditions in the domestic economy***

The transaction was launched for syndication in July 2007 with an interest rate at negative spread of 225 bps to the SBAR and full funding for the project was tied up at that pricing. However, due to revision in the project cost, the approval of lenders was sought in March 2008 with revised project cost and means of finance. During this period, the macro economic scenario changed. There was a significant growth in credit off take and the Reserve Bank of India (RBI) raised its Cash Reserve Ratio (the proportion of deposits that banks have to keep with the RBI) from 7.50% to 9.00%. This resulted in considerably tightening of liquidity in the banking system and consequently the lending rates peaked.

Despite tight liquidity position and significant rise in interest rates in the domestic market, the pricing was revised upward only by 100 BPS through effective negotiation with the Lenders.

Further, PLL will bring 50% of the equity first and also use the ECB facility so that initial draw down from domestic lenders takes place in Q1 FY 2010; this was done to ensure that the present tight liquidity situation of Banks is not stretched further.

While, on the one hand, the floating rate of interest during the construction period provided comfort to the Lenders, it also gave the Borrower the opportunity to avail the benefit of expected fall in domestic interest rates before the commencement of the draw down. With the unfolding of the present global financial crisis, the domestic economy is also slowing down. The RBI has already taken a slew of measures to infuse additional liquidity into the Banking system including cutting the CRR and the policy interest rates. Following these measures, the interest rates in the banking system have also moved southward with the SBAR being cut by 75 bps to 13%. Correspondingly the effective loan pricing to PLL has reduced by 75 bps.

Thus the structuring of the deal has protected the interest of both the Lenders and the Borrower.

❖ ***Financial Closure Achieved Prior to Firm Back to Back Gas Supply Agreement***

PLL is presently in an advance stage of negotiations with Exxon Mobil to source LNG from the latter's 25% share in the Gorgon gas fields of Australia and is hopeful of signing the LNG SPA in the near future. The financial closure of Kochi Project has been achieved prior to the execution of the said LNG SPA. This was made possible by structuring the deal in a manner wherein the cash flows for debt servicing in the initial years are primarily met from the spot operations and subsequently from long-term contracted gas sales. This also demonstrates the faith that the Lenders have reposed in PLL's ability to source long-term LNG.

2008

PETRONET LNG LIMITED

Petronet LNG Ltd

2.5 MMTPA Greenfield R-LNG Terminal at Kochi, Kerala

SBI Capital Markets Limited

Sole Financial Advisor and Funds Arranger

Rs 14000 million