

Japan: the centre of a new growth phase

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After several years of drought, there appears to be a revival of project finance activities in Japan, even though the projects are mostly outside the country.

The opportunities for project finance legal and advisory services in Japan were few and far between in the 1990s, as the country struggled with a decade-long recession, non-performing loans, restructurings and ailing trading companies. What little project finance activity existed centered on Japanese leveraged leases and a few outbound projects in Asia and Latin America. As the new millennium dawned, international project finance legal work almost ground to a halt in the world's second largest economy.

But times are changing. Over the last five years, with large project restructurings being completed in the emerging markets, the level of project finance activity has been steadily increasing. Some observers believe we are now entering a new growth phase in international project financing and that Japanese players are taking the center stage.

The main focus is on the emerging markets, with two driving trends: (i) finding and financing energy and natural resource projects; and (ii) acquiring and financing existing project assets that are still for sale.

The existence of several attractive acquisition targets, combined with renewed financial strength of Japanese trading companies and gas and electric utilities, has resulted in an increased interest in acquiring existing overseas assets – primarily in power. A handful of transactions have already been successfully completed, in some cases with the financing support of the Japan Bank of International Cooperation (JBIC). Mitsui, Sumitomo, J-Power and Tokyo Electric have been leading the charge to buy, in addition to building, overseas, tapping into JBIC's untied mezzanine loan programme, which creates a great competitive advantage for Japanese buyers. Although a limited number of attractive assets remain unsold, we expect there to be several more large acquisitions in the region involving Japanese buyers, including assets in Singapore and the Philippines.

Meanwhile, as a result of what is finally believed to be – after a few false starts – a recovery of the Japanese economy and successful restructuring of the banking sector, Japanese trading companies, gas and electric utilities, and banks are investing in and lending to new greenfield projects abroad. This is not limited to or even concentrated in Asia; the footprint of Japanese players is global. The money is starting to flow again into new projects in Asia, the Middle East and Latin America. The deals involve, for example, oil in Venezuela, mining and toll roads in Peru, water and power plants in the Middle East and mining, energy and power in China and Southeast Asia.

The demand for legal services supporting the investment revival is sure to keep busy the foreign law firms that have maintained their presence in Japan during the down years, and is likely to attract more legal professionals to the Tokyo marketplace.

While most of the project finance activity in Japan has been outbound, the project prospects supporting domestic project finance should not be ignored. Since the late 1990s, there has been serious talk of PFI (private finance initiative) in Japan, and since then, there has been a trickle of public infrastructure projects that have been financed with private funds. Unfortunately, the slow liberalization of the power sector and reduced demand from a shrinking population has dampened hopes for power sector activity.

However, most expect the flow of domestic projects to increase. A few marquee projects, such as the Haneda Airport expansion, are billed to be project financed; but these projects have not yet required international law firm involvement. Perhaps the most popular projects for domestic PFI are the financing for construction and ownership of government office buildings, jails and hospitals, which are then leased back on long-term contracts to government tenants. Project finance is also being used in Japan to finance large-scale private investment in theme parks and telecommunications. As a result, large Japanese law firms have all built small teams dedicated to the Japanese PFI market, but limited experience (domestically and abroad) by these firms means there is likely to be an important role for international project finance law firms for some time.

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