Step-up Loan for Infrastructure Projects

Highlights

Step-up Loan (SuL):

- *Offers a lower price during the project's implementation phase*
- *Clients can lock in savings if they prepay the loan after 8 years from the project approval*
- *Frees up client's borrowing headroom for IBRD projects to allow new lending*
- *At no additional cost compared to a regular IBRD Flexible Loan*

The Step-up Loan (SuL) feature in IBRD Flexible Loan (IFL) allows public sector clients to advance infrastructure projects by providing an initial pricing incentive during the high-risk implementation phase and enabling refinancing in private capital markets afterward.

Benefits of the SuL

- Lowers initial pricing during higher-risk project implementation period
- Potential for further savings if refinanced
- Mitigates the risk of a borrower's inability to refinance by allowing the IBRD loan to be held to maturity
- Frees up IBRD headroom for new lending with the same capital
- Allows for a faster recycling of the sovereign guarantee for sub-sovereign clients

Repayment Terms

The IFL with SuL is a 20-year average repayment maturity (ARM) loan. As any IFL, the SuL allows clients to customize the amortization profile to meet debt management or project needs.

Pricing

The pricing structure operates in two phases:

During the initial project implementation period (called the "incentive period"), clients pay only the IBRD base interest rate from the lower average maturity pricing bucket, with the maturity premium of the Variable Spread reduced or removed. After the incentive period expires, the interest rate returns to regular IFL pricing plus an additional spread designed to recover the earlier incentive. This step-up is calibrated so that clients who hold the loan to maturity pay the same NPV cost as a standard IFL for a comparable maturity (Figure 1).

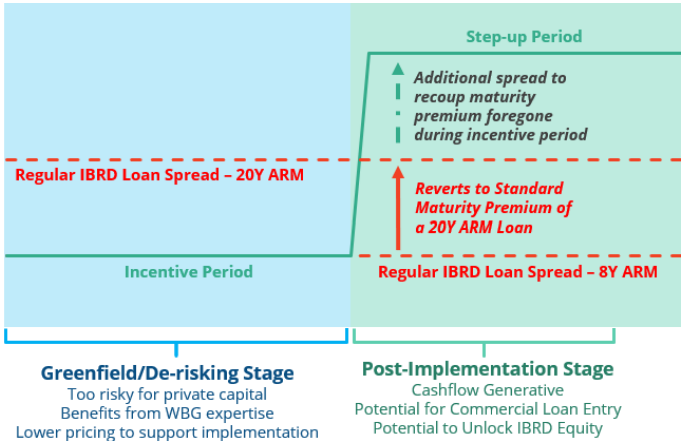

Figure 1

The price of the SuL adheres to the IFL principles, based on IBRD's triple-A credit rating. The pricing components include the interest rate and the standard IFL fees (refer to the next page for details).

Refinancing Options

The World Bank Group actively supports the refinancing process through technical assistance for market readiness and credit enhancement solutions in coordination with other World Bank Group entities, such as the International Finance Corporation (IFC) or the Multilateral Investment Guarantee Agency (MIGA).

Eligibility

For eligibility criteria refer to the table on the next page. SuL feature is also available with IDA non-concessional credits (as such credits are offered on IFL terms).

Country Example: Indonesia

Project Eligibility	The SuL targets infrastructure projects over $100 million for IPF and PforR instruments, with clear refinancing potential. On an exceptional basis, World Bank management may offer the SuL for non-infrastructure projects provided they demonstrate strong potential to generate revenues and meet the other SuL eligibility criteria. Additionally, the project must demonstrate a clear pathway to potential refinancing, defined as follows: (i) the project has clear potential to generate revenues, or (ii) the client has strong capital market access or access to commercial lending at a cost that provides an incentive to refinance, and (iii) the client has strong debt management capacity, and (iv) the project has a strong prospect of being completed within the incentive period.
Incentive Period	For the 8-year incentive period (from the World Bank approval of the loan), the SuL is discounted by the adjustment of the maturity premium to align with the pricing of an 8-year ARM IBRD Loan (0 maturity premium charged for Groups A, B, and C; 5bp maturity premium for Group D).
Step-up Period	At the time of step-up, i.e., after the 8-year incentive period, the maturity premium returns to the applicable level charged for regular IFL's, plus an adjustment spread to ensure the SuL is NPV neutral with a regular IFL of comparable maturity terms. The adjustment spread is calculated such that the NPV of all projected debt service payments of the SuL is equivalent to a regular IFL of the same maturity. The adjustment spread is set in the loan agreement as fixed additional spread. When calculating the NPV of these debt service payments, the World Bank uses market conditions on the day of loan negotiations.
Lending Rate	The main lending rate consists of a variable reference rate plus a variable spread. subject to variations during the incentive and step-up periods (see above). The lending rate is reset on each interest payment date (based on World Bank quarterly resets – see below) and applies to interest periods beginning on those dates. The reference rate is the value of the applicable market rate for a six-month interest rate period (SOFR for USD, TONA for JPY, SONIA for GBP, and EURIBOR for EUR). The loan interest rate charge can be capitalized. The variable spread, resets quarterly: Consists of IBRD's average cost margin on related funding relative to the applicable reference rate plus IBRD's contractual spread of 0.50% and a maturity premium for loans with average maturities greater than 8 years, subject to varied application during the incentive and step-up periods (see above). Additional adjustment spread is also added to the interest rate during the step-up period. The variable spread is recalculated on a quarterly basis and applies to the interest period commencing on the interest payment date falling on, or immediately following the recalculation date, but falling prior to the next recalculation date.
Fees	Front-end fee of 0.25% of loan amount is due within 60 days of effectiveness date of the project, but before the first withdrawal from the loan, and may be financed out of loan proceeds. Commitment fee of 0.25% is charged on undisbursed balances and starts to accrue 60 days after signing date except for the loans that benefit from the 4-year grace period.
Maturity Limits and Repayment Schedules	Policy Limits: The average repayment maturity for the SuL must be 20 years. In addition, other IFL Policy Limits also apply: maximum final maturity is 35 years including a five-year grace period (during which only interest is paid). For loans with CRDC, after the 2-year deferral, the loan is repaid according to the original average weighted maturity without extending the final due date. Clients have the flexibility to tailor the repayment schedule during loan preparation. Once the loan is approved by IBRD, the repayment schedule cannot be changed, except to accommodate for an approved conversion to local currency. Clients have a choice of two types of repayment schedules: • Commitment-linked Repayment Schedule: The loan repayment schedule begins at loan commitment. Principal repayments are calculated as a share of the total loan amount disbursed and outstanding • Disbursement-linked Repayment Schedule: The loan repayment schedule is linked to actual disbursements. Each semester's group of disbursements is similar to a tranche with its own repayment terms (i.e., grace period, final maturity, and repayment pattern). Each semester's group of disbursements would have the same repayment terms.
Loan Currencies	• Currency of Commitment: Loans are offered in IBRD's lending currencies: EUR, GBP, JPY, and USD. Other currencies may be available if the IBRD can fund itself efficiently in the market. Clients may contract loans in more than one currency. • Currency of Disbursement: Disbursements may take place in any currency, as requested by the client. Currencies are acquired by IBRD and passed on to the client at market terms. The loan obligation, however, remains in the currency of commitment. • Currency of Repayment: The loan principal, interest, and any other fees must be repaid in the currency of commitment. • Currency conversions are available (see below) as permitted by the World Bank loan conversion framework.
Interest Rate and Currency Conversion	All existing conversion options (interest rate and currency) that apply to IFLs, will be available for SuL, through a partial maturity conversion up to the end of the incentive period, which could be rolled over depending on whether the client prepays, and at their request. All conversions are subject to market availability.
Conversion Fees	For applicable transaction fee(s) for interest rate conversions refer to http://treasury.worldbank.org.
Payment Dates	Debt service payment dates will be on the 1st or 15th day of the month and semi-annually thereafter, as agreed with the client during loan negotiation.
Prepayment	Clients may prepay all or part of the outstanding loan balance at any time including as a result of refinancing at the end of the incentive period for the SuL.. There is no prepayment fee, however for loans with conversion in place, costs resulting from unwinding the market hedge may apply.

The above is not necessarily a complete listing of the terms and conditions of these loans. Clients should refer to their loan agreements and General Conditions with respect to their individual loans.

Contact: **Miguel Navarro-Martin,** Manager, Financial Products & Client Solutions, The World Bank Treasury
✉ mnavarromartin@worldbank.org ✆ +1 (202) 458 4722 1225 Connecticut Avenue NW, Washington, D.C., 20433, U.S.A.