IJGlobal
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Shiloh II: What price US renewables?

19/12/2008

EDF Energies Nouvelles subsidiary enXco closed the financing for its $380 million Shiloh II wind project on 17 November. The financing, led by Nord/LB, was one of the first tests of lender appetite for US wind projects in the post-Lehman Brothers environment.

It faced a difficult path to close, despite the presence of one of the world's largest utilities as a sponsor. Its debt was also subject to several pricing flexes, as well as shifts in the composition of its arranger and tax equity groups. But the entire US renewables market has been characterised by extreme shifts in funding costs and the abrupt departure of several debt and equity players.

Shiloh II is a 150MW wind farm located in Solano County, California, in a region known as the Montezuma Hills Wind Resource Area. The developer of Shiloh II, enXco, developed a first project at the site, Shiloh I, also of 150MW, and subsequently sold it to PPM, now part of Iberdrola, in 2005.

EDF first bought a stake in enXco in 2002, and since then it has moved from developing and building plants on a turnkey basis – selling them to wealthier utilities at completion – to owning and operating, thanks to a tax equity market that allows foreign owners without a tax base to monetise US wind projects' tax credits.

Its debut deal as an owner-operator was the Fenton financing, a $385 million debt and tax equity facility led by Union Bank of California, with Dexia Credit Local as agent bank. Fenton solved the difficulties of coordinating leveraged debt and tax equity by having one bank – UBOC – arrange both, although lender pressure forced UBOC to cede the agent title to Dexia to avoid potential conflicts. GE and Wells Fargo joined UBOC on the tax equity.

Pricing on the 18-year Fenton debt was roughly 125bp over Libor, and enXco wanted to improve on that benchmark. Fenton closed in January 2007, and in March 2008, the developer looked to mandate an arranger on Shiloh II. The period encompassed the fall of Bear Stearns but preceded deeper problems in the commercial bank market.

Nord/LB picked up the mandate, together with an unnamed second bank, based on a keen pricing commitment thought to be in the region of 112.5bp over Libor. The first sign of trouble was the departure of the second bank. By August, as the crunch deepened, and several large renewables banks were restructured or partially nationalised, enXco and the lead arranger realised that the pricing would not stand even though the deal did not suffer from any structural flaws.

Shiloh II benefits from a 20-year power purchase agreement with Pacific Gas & Electric, whose finances have recovered this decade to such an extent that it is now solidly investment grade. Behind the PPA stands the state of California's renewables portfolio standard, which mandates that its utilities must buy 20% of their power from renewable producers by 2010.

Nevertheless, the debt's pricing increased first to 137.5bp, and then, as conditions worsened, endured a more drastic flex to nearer 225bp. The increase is only the most extreme example of the pressure on margins that the crunch has imposed upon sponsors, and while EDF might have thought itself immune, the clannish US wind finance market has been able to impose its terms on its US subsidiary.

Nord/LB brought in two French lenders – CIC and Dexia – to support the deal, showing that sponsor pull can be effective at the right price. Dexia, in particular, is extremely familiar with both EDF and enXco.

The financing also managed to overcome the departure of a tax equity investor from the original line up and closed with a group of three: JP Morgan, NY Life and MetLife. Notable by its absence from this group is GE, which was present on Fenton, and whose corporate parent has endured its own financial difficulties. Also notable, however, is GE's presence on recent Invenergy financings as a tax equity investor.

The deal also contended with the US market's slightly lower familiarity with the RePower 2MW turbines that the project uses. The MM series, to which Shiloh II's turbines belong, have a four-year operating history, and Nord/LB, for one, is very comfortable with them. But the ultra-conservative US market is looking for a deeper commitment from the turbine maker to the US, which it has been slowly providing, in terms of manpower and facilities. And as one banker familiar with the deal noted, "the spares and components used on the equipment can be sourced fairly widely." The turbines have experienced 95-97% availability, and REPower has built up a good reputation for after-sales care.

The debt financing ultimately brought in $225 million, leaving EDF to make up the balance. The three banks to close on the deal will follow up on interest from participants in 2009. If margins subside again that year, Shiloh II will look like an attractive asset. For now fortune has bruised, as much as favoured, the bold.

All in all, Nord/LB would have hoped for a smoother debut as a top-tier renewables arranger. However, Unicredit also struggled to syndicate a simpler debt package for Invenergy, a process that has now been deferred until 2009, and FPL's latest project financing has been cast as a club financing. But both enXco and Nord/LB coped flexibly with a confluence of shocks.

Shiloh II
Status: Closed November 2008
Size: $380 million
Location: California
Description: 150MW wind farm
Sponsor: enXco
Debt: $225 million
Lead arranger: Nord/LB
Arrangers: Dexia, CIC
Independent engineer: Garrad Hassan
Lender legal counsel: Latham & Watkins
Sponsor legal counsel: Winston & Strawn