

ERRM: Tighter and tighter

01/12/2005

Iberdrola's Eu217 million financing of a 199MW windfarm portfolio in Murcia has set a new benchmark for ever tightening margins on Spanish wind deals.

The project company, Energias Renovables de la Region de Murcia (ERRM), is 50%-owned by Iberdrola, Spain's second largest energy utility, with a 50% equity stake accruing to mainly local groups from the Murcia region in south-east Spain. These groups are: Caja Murcia, Inversiones y Proyectos 3, Grupo Fuertes, Energia Hidroelectrica de Navarra and Instituto de Fomento de Murcia.

The farms are part of a concession from Murcia's regional government. The portfolio will eventually consist of 10 windfarms, three of which are already operational with a further seven to be built between now and 2008. Current operational capacity is 42MW – the plan being to increase this to 139MW by the end of 2006 and 199MW by the end of 2008.

The debt portion of the financing consists of a Eu141 million 16-year term loan and a Eu15 million credit facility. There is a completion guarantee in place from Iberdrola, keeping margins down to 25bp until all the projects are completed in 2008.

Pricing then varies according to cover ratios. Initial reports that the average expected price is 80bp were predicated on incorrect estimates of the ADSCR. Base-case cover ratios are expected to average 1.3x, at which debt will pay a margin of 60bp – low even by Spanish standards. Margins rise to 70bp between cover ratios of 1.2x and 1.3x, and to 80bp below 1.2x.

Margins have been getting ever tighter on Spanish wind deals due to a combination of a stable wind regime, which offers sponsors a reliable income, and high liquidity in the project finance market in general.

One possible reason for differing estimates on the likely margins is the criteria used for base-case modelling: the ERRM transaction uses variable rate tariffs, whereas the norm on Spanish wind deals is to use fixed rate tariffs, which lead to more conservative estimates. Variable rate modelling has proven a more accurate indicator of revenue streams, but fixed rate modelling gives bigger cushions – a factor that has contributed to decreasing Spanish margins.

Although most Spanish wind deals to date have used fixed rate modelling, Endesa's Eu450 million Valencia portfolio financing, which was seen as a benchmark low for pricing when it closed earlier this year, also uses variable rate modelling. Comparisons between Valencia and ERRM are instructive. On a similar base-case ADSCR, the Valencia deal is expected to pay a margin of 75bp during operation. ERRM pays lower margins, but over a shorter tenor and on a lower debt-equity ratio.

Mandated lead arrangers on the deal were BBVA, Banesto and Calyon, each providing Eu33 million. Given the tightness of the margins, the MLAs decided to pre-syndicate to reduce underwriting risk. Banco de Sabadell, Fortis (each Eu15 million), Barclays, Caixa Catalunya (each Eu10 million) and Banco Santander (Eu7 million) came in as lead managers with a participation fee of 40bp.

Other than the low margins, the most notable feature of the financing is its flexibility. Iberdrola has total leeway to change the configuration of windfarms included in the portfolio. No other windfarm portfolio financing has given the sponsor such a great deal of discretion, and it is unlikely that this will set a new model as few other sponsors are as strong as Iberdrola or have their breadth of wind capacity in development.

Iberdrola is itself the electricity provider for the Murcia region, so will act as offtaker for ERM's output. The windfarms will be built by EPC contractor Energias Eolicas Europeas, a 50/50 venture between Iberdrola and EHN, while the turbines to be used are manufactured by Gamesa and Ecotecnica.

Iberdrola has windfarms in development and operation in 12 different regions of Spain, but generally pursues corporate financing rather than project finance for its windfarms. The exceptions to this are for regions – like Murcia – where the local authorities specify that local groups must have an equity stake in the project company.

One such project planned for 2006 is a portfolio financing of 10 to 15 windfarms in the Castile-Leon region. This portfolio is likely to have a capacity of 700MW to 800MW to be brought into operation between 2006 and 2009. Iberdrola's equity stake will be around 60% to 70%, with Caja Duero included among the local equity providers. The deal, for which an MLA is yet to be appointed, will probably have a gearing of 70% to 75%.

Given how much Spanish wind margins have fallen since the BioVent financing, which priced in the 110bp to 150bp range, Iberdrola says it will also refinance that portfolio in 2006.

The government may modify the country's tariff regime in March, putting a cap on variable tariffs. The tariff has averaged around Eu90/MWh in 2005, compared to an anticipated Eu75/MWh. Faced with a system that is paying out more than it was designed to, the government is considering a limit on the variable-rate tariff so that it may not rise above 15% of the fixed rate tariff.

Energias Renovables de la Region de Murcia

Status: Closed October 2005

Size: Eu217 million

Location: Murcia, Spain

Description: Portfolio financing of 10 windfarms, three operational and seven in construction

Debt: Eu156 million

Mandated arrangers:

Banesto, BBVA, Calyon

Lead managers: Banco de Sabadell, Fortis, Barclays, Caixa Catalunya and Banco Santander

EPC: Energias Eolicas Europeas

Legal counsel to lenders: Garrigues

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