Shanghai surprises

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With the ?i?s dotted and the ?t?s crossed on BP and Sinopec's Shanghai Ethylene Cracker financing, Ashley Wilkins is a happy man. SG's head of project finance in Asia (SG was the co-ordinating financial advisor) believes the deal is one of the most important to come out of China in recent years.

The US dollar and renminbi (Rmb), $1.8 billion equivalent limited recourse financing for the $2.7 billion development is the first very large-scale petrochemical complex fundraising to close in China. It is the largest debt financing a Chinese enterprise has entered into since the Asian economic crisis. When it opens the Shanghai Ethylene Cracker Complex (SECCO) will be the country's largest such project with a production volume of 900,000 tonnes per year.

The project also gets first mover advantage achieving financial close well ahead of two competing petrochemical transactions, Shell Nanhai and BASF Nanjing, says Wilkins. This despite the fact that the Shanghai development was, for a long time, third in the running behind the other key projects. Once the joint feasibility study report was approved by the State Council in August 2001, the financing arrangements moved swiftly forward. Financial close was achieved on January 11.

?First mover advantage was very important to the sponsors and the financiers ? one of the key risks after financial close for a project of this size is availability of resources,? says Wilkins. The danger for the other petrochemical ventures yet to be financed is that Chinese construction companies, equipment providers and raw materials will be tied up by SECCO's substantial resource requirement.

The speed with which SG has been able to move the project forward is largely due to the financing strategy chosen by the sponsors. BP and Sinopec guarantee most of the financing. There are three tranches: a $708 million US dollar term tranche; a Rmb8.12 billion local currency term tranche and a Rmb963 million working capital tranche. It is only this last limited recourse tranche which is not guaranteed by the sponsors but is arranged and financed by domestic Chinese banks. Sources close to BP Amoco and Sinopec say both will consider a more extensive limited recourse refinancing of the current deal at a later stage.

Another financier involved in the transaction says this is the first time Chinese banks have provided US dollar funding to a project of this type. At the same time, record terms were achieved for a complex project financing of this nature. ?That's really a reflection of the very strong sponsor support,? says the financier.

Tenor for the US dollar term loan is 12 years, commitment fee is 30bp and margin 70bp and the repayment profile is back ended. For the renminbi loan, tenor is 20 years, repayment is also back-ended and the interest rate is set at 10% below the People's Bank of China rate. Tenor of the renminbi working capital facility is 10 years and the interest rate is again 10% below the People's Bank of China rate.

When Project Finance reported on the deal in its December 2001 issue, banks supporting the competing projects expressed skepticism that those terms could be achieved. ?What we hear,? said one banker, ?is that local banks might stretch to 18 years but they are more likely to do 16 years and definitely won't do 20.?

Allocations for the US dollar term loan facility are as follows: Bank of China, China Construction Bank, Bank of

Communications, ICBC, $114.5 million; HSBC, IBJ, $100 million; Shanghai Pudong Development Bank, $50 million.

Allocations for the RMB term loan are: Bank of Communications, Rmb1.8 billion; Bank of China, China Construction Bank, ICBC, Rmb1.5 billion; Agricultural Bank of China Rmb823 million; Guangdong Development Bank, Bank of Shanghai, Rmb500 million.

The working capital facility allocations are: ICBC, Rmb363 million; Bank of Communications, Shanghai Pudong Development Bank, Rmb300 million.

The US dollar tranche is still in syndication, but market response to the transaction is reported to be strong, partly due to the competitiveness of the project and partly because of the project's first mover advantage.

The BP project is said by its bankers to have by far the lowest production costs of the ethylene crackers set to be financed. According to the sponsors, the Shanghai cracker will have an ethylene capacity 100,000 tonnes greater than the annual output for Shell and CNOOC's Nanhai plant. And yet Shell's project is forecast to cost over $1 billion more than the BP venture. Even taking into account the additional facilities that the Shell project will feature, an official involved in the BP bid says the project will have a better profile of capital cost to production volume.

Nevertheless, the underlying economic rationale for both projects is still compelling and all the projects are expected to tap loans at attractive rates. Demand for ethylene is one of the key questions, even more so given the global economic slowdown, as a substantial chunk of the output of these projects will be exported. ?But at least 40-50% of local demand for ethylene is still uncovered by local production according to industry estimates and has to be imported. Even taking the global downturn into account, overcapacity is not an issue. Wilkins thinks this is a conservative assessment: ?even if all three projects were up and running today there would be a huge shortfall in demand for ethylene.?

SECCO

Status: In syndication

Cost: $2.7 billion

Location: Shanghai, China

Description: financing for 900,000 tonne-capacity ethylene cracker

Sponsors: BP, SPC, CPCC

Arrangers: Bank of China, China Construction Bank, China Industrial and Commercial Bank, the Bank of Communications, China Development Bank, Bank of Shanghai, Guangdong Development Bank, Agricultural Bank of China, Shanghai Pudong Development Bank, HSBC, IBJ

Co-ordinating financial adviser: Societe Generale

Co-advisors: CCB, BOC, (ICBC ? independent advisor)

Contractors: AMEC and ABB Lummus

Lawyers to the borrower: Skadden Arps Slate Meagher & Flom, King & Wood

Lawyers to the borrower:

Allen & Overy, Haiwen