PP11: No guarantee, no problem

02/02/2011

Awarded to a bidding consortium of GDF SUEZ, Al Jomaih Group and Sojitz, the $2.1 billion financing of the PP11 gas-fired independent power project in Saudi Arabia took just three months from award to reach financial close. It is the fastest project financing US Ex-Im has ever been involved with, and illustrates the increasing commercialism of export credit agencies.

PP11 is significant as it is the first time international banks have taken on uncovered risk on a project since the countrys Ministry of Finance stopped providing a direct guarantee to offtaker Saudi Electricity Company (SEC). The use and misuse of tacit or indirect guarantees was brought sharply to banks attention with the renegotiation of debt for some of Dubais government-related entities. So while the Rabigh IPP deal was the first to be done without a government backstop for the offtake contract, the PP11 deal was the first where international banks got comfortable without ECA cover. Like Rabigh, PP11s 20-year power purchase agreement obliges the Ministry of Finance to replace SEC with an entity rated BBB or above if SECs rating falls below that level.

PP11 therefore marked the return to more normal lending conditions, and by the time the Barka 3 and Sohar 2 IPPs were being financed in Oman, most international banks accepted that government backstops for offtakers with an IPP track record are not necessary.

PP11 is also emblematic of the way power deals are likely to be financed over the next few years with a small group of banks, one or two ECAs and a couple of Saudi banks.

Pre-crisis most deals were syndicated, says Karel Breda, head of acquisitions, investments and financial advisory for Middle East and North Africa at the projects lead sponsor, GDF SUEZ. When we approached banks for PP11 a couple of banks wanted to do a syndication, but we didnt want to because the risks were too high. Club deals will be a continuing trend in the region.

Sponsored by SEC (50%) and a consortium of GDF SUEZ (20%), Al Jomaih Group (15%) and Sojitz (15%) total project costs are $2.1 billion, with a $1.553 billion debt package and a $500 million equity bridge loan that will repaid after construction.

The financing splits into a $378 million direct loan from US Ex-Im, a $530 million commercial tranche provided by Credit Agricole, EDC, KfW, Societe Generale, Standard Chartered, Intesa and CIC, and $645 million split across two Riyal-denominated Islamic facilities, a $382 million Istisna Ijara facility provided by Saudi Fransi and Samba and a $263 million Wakala Ijara facility provided by Alinma Bank and NCB. The $512.2 million equity bridge loan is provided by Sumitomo Trust, KfW and NCB.

The commercial and Islamic facilities have a door-to-door tenor of 20 years with a 20% balloon payment at maturity. Both facilities carry a margin starting at 250bp over six-month Libor rising 15bp every three years to an eventual 340bp. Upfront fees are between 250bp and 300bp. The US Ex-Im tranche has a 17-year tenor (construction plus 14 years) with an average loan life after construction of 7.25 years to conform to OECD guidelines on ECA support, and a fixed margin. Ex-Ims involvement comes on the back of GEs sale of seven 7FA.4 turbines to the project.

The 20% balloons on the commercial and Islamic facilities will be repaid fully under base case projections, with an 85% cash sweep starting after 10 years of operation, although if no cash is swept the 17-year post-completion tenors leave a 3-year tail on the PPA, which will fully repay the debt.

The projects leverage, at 75/25, is lower than recent benchmarks to accommodate the higher debt margins while maintaining debt service. The average debt service coverage ratio is 1.2x, a distribution lock-up kicks in at 1.10x and the default trigger is 1.05x. The loan life coverage ratio (LLCR) is 1.3x. And there is a 6-month liability reserve account. These compare favourably, from a sponsors perspective, with Rabighs metrics of 1.25x ADSCR and 1.2x minimum DSCR and distribution lock up at 1.15x.

For PP11 the GDF SUEZ-led group posted the second-lowest bid, but the lower Marubeni/Kansia/Masader bid of SR0.0777 per kWh was non-compliant it included a 100% dispatch figure, rather than the 70% in the bid documents, a 0% return for the government shareholder in the scheme and an unrealistic cost of debt. The GDF SUEZ group bid SR0.1079 per kWh and has kept to the tariff.

Combining agency, international and local lenders with different maturity dates involved delicate inter-creditor arrangements. Once US Ex-Im is repaid, on a pro rata basis local banks would have greater voting rights than international banks. The financing documents therefore include a rebalancing that affords the international banks more comfort.

One lesson learned by SEC and its advisers from the PP11 tender is the need for active management of Saudi bank liquidity. On PP11 two Saudi banks backed four bids, which to many bidders was an unacceptable situation that threatened bid confidentiality. For the upcoming Qurayyah IPP, each bid can have a maximum of two Saudi banks and each Saudi bank can back a maximum of two bids, the so-called 2 by 2 rule.

Ive always supported this idea, says Breda. There needs to be the right balance between sponsors and banks. In the current market exclusivity is an extreme position for sponsors to take with banks but the other extreme position is for banks to back three or four consortiums.

PP11 IPP
Status: Signing 16 June 2010, financial close 22 June
Size: $2.1 billion
Location: Riyad, Saudi Arabia
Description: financing of 1,730MW gas-fired IPP in Saudi
Sponsors: SEC (50%), GDF Suez (20%), Al Jomaih Group (15%) and Sojitz (15%)
Equity: $512.2 million as an equity bridge loan from Sumitomo Trust, KfW and NCB
Debt: $1.553 billion
Commercial debt lead arrangers: Credit Agricole (global documentation & coordination), Standard Chartered (technical, insurance and modelling) EDC, KfW, Societe Generale, Intesa and CIC
Islamic lead arrangers: Alinma Bank (Wakala documentation), NCB (Wakala documentation), Saudi Fransi (Istisna documentation), and Samba
Agency: US Ex-Im
SEC financial adviser: Citi
SEC legal advisers: Muhannad al-Rasheed and Baker Botts
SEC technical adviser: Fichtner
Sponsors legal adviser: Milbank Tweed
Lenders legal adviser: White & Case
Lender technical adviser: Shaw Group
Insurance: JLT
EPC and equipment: HHI (EPC) and GE (turbines)