San Jacinto: King of Leon

24/02/2011

Ram Powers $160 million debt financing for phase II of its San Jacinto-Tizate geothermal project highlighted healthy lender interest in an asset class as niche as Nicaraguan geothermal, even if this interest comes from development finance institutions. It also offers up some answers, if partial ones, to how lenders can get comfortable with resource risk on geothermal projects. The financing has yet to fund, as the sponsor copes with some disappointing drilling results at the site, but stands as a powerful proof of concept for the geothermal market, and a landmark financing for Nicaragua.

Ram Power is a US-based and Canadian-listed developer and operator of geothermal projects. Formed in 2008 around a core of former Ormat management and the merger of three listed Canadian developers, it focuses on projects in the US and Central America. San Jacinto, which was owned by Polaris Energy, is the most advanced of the projects that were included in the merger. Its shareholders ended up with a little over 54% of Ram after the 2009 mergers.

San Jacinto is located near the town of Leon in Nicaragua, and at the time of the merger was a 10MW demonstration that was funded with a quasi-corporate loan. At the time of the acquisition, Polaris was looking to expand the resource, at a cost of roughly $100 million. The project benefits from power purchase agreements with two local utilities, Disnorte and Dissur, whose ultimate corporate parent is now Gas Natural.

The financing of the 36MW phase 1 was assembled in the aftermath of the crisis, when even DFI debt appetite was limited. The $77 million in debt consisted of $20 million each in senior debt from Cabei, EDC and FMO, a $10 million senior B loan from Cordiant Capital, and a $7 million subordinated loan from FMO. Cabei/FMO mandate was signed before Polaris merged with Ram, but to bring in EDC and Cordiant, Ram had to increase the pricing on the debt and included onerous cash sweeps. The deal signed in December 2009, and funded in March 2010 after Ram made its required equity investment.

Even before the financing for phase I had signed, Ram started work on a phase II financing, which would back a further 36MW expansion, based on Rams estimates. The IFC took the lead in structuring the financing, and brought in lenders through its syndications group, even though any other DFI would sign its own facility documentation rather than use the IFCs wording. The sponsor hoped for greater leverage, better terms, and more flexibility on resource risk.

Project finance lenders, in whatever market, have traditionally refused to lend against unproven geothermal resources. In practice this has meant sponsors having to complete an expensive drilling programme before they even start documentation.

For the phase II financing, however, Ram was able to persuade lenders to accept a borrowing base type arrangement for funding on the San Jacinto project. The concept has a long history in the oil and gas sector, where lenders repayment prospects are also dependent on geology. Calpine is also believed to have included a similar concept in some of its financings for the Geysers assets in California, though limitations on banks in-house ability to assess geothermal resources has limited wider acceptance of the structure.

Under the borrowing base, $70 million of the senior debt becomes available when the lenders adviser, GeothermEx certifies a 64.8MW resource, a total of $98 million will be available at 70MW, and then another $7 million will be available for each additional 2.4MW proven. Under this schedule, the full $140 million would only be available when the resource is proved to 84.4MW.

The phase II debt consists of $140 million in 13-year senior loans from the IFC, as administrative agent ($30.3 million), IDB ($30.3 million), DEG, FMO, Proparco (each with $18.9 million), OeEB ($15.1 million), Cabei (with $7.6 million) and BIO (funding part of FMOs share), as well as a $20 million 14-year subordinated C loan from the IFC. The senior debt is priced at 650bp over Libor, while the C loan is priced at 400bp over an IFC-calculated base rate.

The deal attracted $235 million of debt commitments with this pricing and these terms, though EDC and Cordiant insisted on being bought out after the sponsor convinced the other phase I lenders to accept a restatement of their debt to bring the tenor, pricing and cash sweep provisions more into line with the phase II deal. FMO and Cabei bought out the EDC debt, and CIFI bought out Cordiant. Given the response, Ram might have been better to wait to take both phases to market, though in 2009, it was not clear that lending markets would ever recover enough to digest both phases at once.

The financing signed on 6 November, during a busy period for renewables financings in Central America, and highlighted just how much Cabei has come to dominate the regional power finance market. The lions share of the credit for closing the deal, say sponsors, advisers and other lenders, should go to the IFC, which was able to take charge of the financing process even though it was not a part of phase I.

Since signing, Ram has struggled to prove the resource to levels that would allow the debt to fund, and there have been cost overruns at both phases, with most of the increases on the first phase. With the expenditure of more equity on drilling, some of which has been funded with a corporate loan, it should be able to fund later in 2011. It seems likely that even if, as it predicts, it can recover $45 million of its equity expenditures it will settle for gearing that, at a little under 60%, will be only a little more than the first phase.

For lenders, the deal has already proved the worth of the borrowing base and also the importance of resource verification. Sponsors, however, will still need to find cost-effective ways of funding drilling to prove resources. The new corporate financing carries a 12% interest rate, and shareholders can be impatient. Just before Project Finance went to press, chief executive Hezy Ram, who founded and lent his name to the sponsor, stepped down over differences in opinion with his board.

Polaris Energy Nicaragua and San Jacinto
Power International Corporation
Status: Signed 6 November 2010, awaiting funding
Size: $160 million
Location: Leon, Nicaragua
Description: Expansion of 36MW geothermal project to 72MW
Sponsor: Ram Power
Phase II senior debt: $140 million
Administrative agent: International Finance Corporation
Lenders: IFC, IDB, DEG, FMO, Proparco, OeEB, Cabei and BIO
Phase II subordinated debt: $20 million IFC C loan
Sponsor legal adviser: Akin Gump
Lender legal adviser: Shearman & Sterling
Sponsor financial advisers: Greentech Capital Advisors, PAF Securities
Resource consultant: GeothermEx
Market consultant: Mercados Energeticos Consultores
Insurance adviser: Moore McNeil
Independent engineer: Shaw Group
Environmental consultant: Gerencia Ambiental Internacional
Model auditor: Ernst & Young
Offshore collateral agent: Citigroup
Panama depositary agent: Scotia

Onshore collateral agent: Banco de la Producción