DEAL ANALYSIS: El Arrayán

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Chile is probably the best-placed country in Latin America to develop a vibrant wind sector. It has plentiful though not always high-grade wind resources, healthy utilities, and a capable banking sector. Conventional power projects in good years can expect to borrow at low spreads and for long tenors. Conventional generators can also expect healthy prices particularly at peak demand on the countrys merchant market.

But project financings for Chilean wind projects have been few, and foreign sponsors are more likely to fund new construction on balance sheet. The reason for this comparative paucity of deals is the combination of a merchant wholesale market and a renewables incentive regime based on a renewables portfolio standard rather than a feed-in tariff.

Chile is dependent on imported gas and coal for the bulk of its marginal power requirements, and large peak spikes in prices are common. Under Chiles renewable portfolio standard, its utilities should buy 5% of their requirements from renewable sources, but the penalties for not doing so not to mention off-peak power purchases are low enough that many utilities simply include the penalties as a cost of doing business. But as Chile moves towards an eventual 20% target it will be harder for utilities to bear the costs of compliance in this way.

The $245 million financing for the El Arrayán wind farm uses a hedging agreement with a large mining offtaker to mitigate merchant price risk. It also features the largest commercial bank presence to date in Chilean renewables. The lead arrangers of the $210 million 15- year construction-to-term debt and $15 million in letter of credit facilities, of which half came from the Danish ECA EKF under its ELO programme, were Bank of Tokyo- Mitsubishi UFJ, Crédit Agricole and Sumitomo Mitsui Banking Corporation, while Chilean lender Corpbanca provided a $20 million VAT facility.

El Arrayán is a 115MW project located in Ovalle commune, Limari province. It will consist of 50 Siemens 2.3MW turbines, which will be manufactured in Denmark, and its engineering, procurement and construction contractor is Skanska. It dispatches into the central SIC power grid and is set to come online in early 2014.

According to the sponsors registration for clean development mechanism credits, which dates to March 2012, the project has a total cost of $265 million, and a capacity factor of 34.6%. The document concludes that the project, without carbon credits, would produce a base case internal rate of return, without carbon credits, of 7.34%, though CDM registrations are designed in part to prove that projects would not be economically viable without carbon credits.

The projects sponsors are Pattern Energy, the wind developer founded by former Babcock & Brown wind specialists and the original project developer, with 15%, AEI, the emerging markets-focused independent power producer, with 55%, and Antofagasta Minerals, the Chilean miner, with 30%. Pattern signed a joint development agreement with AEI in November 2009 that covered projects in Brazil, Argentina and Chile. In January 2010, AEI bought a 55% stake in the project, giving it the right to nominate the projects chief executive officer, while Pattern nominates the projects lead developer.

Antofagasta acquired the stake after exercising an option that accompanied its agreement to hedge 280,000MWh per year of the projects output under a 20-year agreement. Antofagasta owns Minera Los Pelambres, the project company for the copper mine of the same name, and the projects offtaker.

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The amounts payable under the hedging agreement would vary monthly, according to the monthly production levels, with an annual true-up mechanism in case aggregate annual production falls below the amount covered by the hedge. Excess production would be sold on the merchant market. The hedge is sized in such a way that it covers the projects P99 production (or the production level that the project is expected to exceed 99% of the time), while at P95, some revenues would be merchant.

Several bankers who looked at the deal described the structure as aggressive, even with the Pelambres hedge. The project cost, even the CDM filings figure is accurate, is lower than other projects using the same make of turbines, which makes the debt/equity ratio on the deal even more impressive. Nevertheless, sources close to the arrangers describe the EKF contribution as lowering overall financing costs rather than making up for weak lender appetite. The deal is understood to have to have priced 275bp and 325bp over Libor.

Even within the rough outlines available for the financing, the Antofagasta hedge looks to have resulted in extremely competitive debt terms. Working with an industrial offtaker might be a necessary response to the vagaries of the Chilean merchant market. But it also looks like the best way to maximise tenor and leverage and keep a lid on debt costs.

Parque Eólico El Arrayán SpA
STATUS: Signed May 2012
SIZE: $265 million
DESCRIPTION: 115MW partially-hedged wind project located in northern Chile
SPONSORS: AEI (55%), Antofagasta Minerals (30%), Pattern Energy (15%)
DEBT: $245 million
LEAD ARRANGERS: Bank of Tokyo-Mitsubishi UFJ, Crédit Agricole and Sumitomo Mitsui Banking Corporation
VAT FACILITY PROVIDER: Corpbanca
ECA: EKF
TURBINE SUPPLIER: Siemens
EPC CONTRACTOR: Skanska
SPONSOR LEGAL COUNSEL: Andrews Kurth (international), Carey y Cia (local)
LENDER LEGAL COUNSEL: Milbank Tweed (international), Philippi, Irarrázabal (local)
INDEPENDENT ENGINEER: Burns and Roe
LENDERS INSURANCE ADVISER: Moore-McNeil
MARKET CONSULTANT: Mercados Energéticos Consultores

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