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DEAL ANALYSIS: Sabine Pass Liquefaction

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Cheniere Energy Partners closed the $3.6 billion debt financing for its Sabine Pass export liquefied natural gas facility on 31 July, overcoming a shrinking cast of potential lenders and a poor credit rating. It did so roughly three years after first considering building an export facility next to its existing, underused, import terminal in Cameron Parish, Louisiana.

To prevail, Cheniere had to rope in 11 lead arrangers willing to write tickets of at least $250 million. This required building a syndicate beyond the group of traditional project lenders in the US, including luring in investment banks, which are typically wary of making their balance sheets available to highly-leveraged developers.

Cheniere Energy Partners, a publicly-traded partnership, owns Sabine Pass LNG, the project company for the existing import terminal, and Sabine Pass Liquefaction, the project company for the proposed export terminal. Cheniere Energy, itself publicly-traded, owns 77.8% of Cheniere Energy Partners, and is its general partner. Between them, and before the export terminal financing closed, Cheniere Energy, its holding company for the stake in the partnership, and the import terminal were subject to a little under $2.7 billion in debt.

Bank of Tokyo-Mitsubishi UFJ, Crédit Agricole, Credit Suisse, Deutsche Bank, HSBC, JPMorgan, Morgan Stanley, Royal Bank of Canada, Société Générale (also Chenieres financial adviser), Standard Chartered and Union Bank were joint lead arrangers. BBVA (via Compass), CIC, GE Capital, ING, Korea Development Bank, LBBW, Lloyds, Mizuho, Santander (via Sovereign) and Scotiabank were participating lenders. HSBC, SG and Credit Suisse had led 2005 and 2006 bank financings for Chenieres import facility at Sabine Pass, while Credit Suisse has led several bond and B loan financings for Cheniere and Sabine Pass.

In mid-2011, lenders were sceptical about the prospects for a construction financing for two export trains at Sabine Pass that would cost at least $4.5 billion. Cheniere was looking for $2.4 billion at that time, an ambitious enough total, given the economic climate. As the debt total rose, to $3.6 billion, the number of lenders active in the US market fell. Cheniere also required a large amount of equity, preferably from a well-capitalised private equity firm, in part to bolster the highly-leveraged Cheniere Energys CCC credit rating. And Cheniere would have to educate the market about its history, the technology it was using, its future plans, and the market for LNG outside the US.

The sponsor has assembled a diverse group of offtakers BG Group, GAIL India, Gas Natural Fenosa and Korea Gas Corporation which signed 20-year contracts for a combined annual 16 million tonnes of LNG, eliminating price risk. Cheniere won the authorisation of the US Department of Energy to export LNG to countries with which the US has not signed free trade agreements a license highly coveted by its competitors. The license meant that Sabine Pass would be the first of potentially several export LNG facilities to hit the financing market. Lenders wanted a chance to show off their participation in the first export LNG project in the US in more than 40 years and the second ever.

Cheniere Energy closed two equity issues in 2012 to move the liquefaction project forward. In March it brought in $352 million from a Credit Suisse-underwritten common stock offering, using the proceeds to pay down corporate debt. In July, it brought in $380 million from a second Credit Suisse-underwritten issue, again using the proceeds principally to pay down debt. In June, Cheniere Energy bought $167 million of Cheniere Energy Partners units, the first of $2 billion in equity that Partners would need to raise to fund the liquefaction plant. It funded much of its contribution with a $468 million Cheniere Energy equity investment from Temasek and RRJ Capital.

In February 2012, Cheniere brought in Blackstone (through its Blackstone Energy Partners and Blackstone Capital Partners VI funds) to provide equity for Sabine Pass. Blackstone ultimately contributed $1.5 billion in equity to Partners, and its participation lent credibility to the export facility venture. Bankers closer to the deal say that at least two other equity players were discussing a stake; had Cheniere not attracted Blackstone, another well-regarded backer would have joined, they say.

Cheniere had previously awarded Bechtel, an experienced contractor popular with project lenders, the turnkey engineering, procurement contract for the project, at a fixed price of $3.9 billion. Cheniere added another $600 million in owners costs and contingency, and did not provide a construction guarantee, in part because lenders would not have assigned a great deal of value to one.

But even after lenders digested the enormity of the ticket sizes that theyd be writing (up to $350 million), the deal still looked tempting: Pricing 50-75bp above the majority of project deals in the US and with the prospect of a quick recycling of their commitments. The vast majority of the total bank debt, with the exception of $100 million, will be drawn after the sponsors have contributed $1.89 billion in equity. Some bankers dont expect their commitments to fund until mid-2013, which is attractive to European lenders having to manage the introduction of Basel III capital requirements.

And Cheniere is planning to refinance the bank loan well before maturity in 2020, and potentially within two years. Explains one banker: The seven-year loan is essentially a bridge. Libor plus 350bp is attractive if youre going to be getting repaid in 18 months. The loan is priced at 350bp over Libor during construction and is scheduled to inch up to 375bp during operations. Cheniere will also hedge at least 75% of the projects exposure to Libor.

The bank debt grew from an initial $2.4 billion target in mid-2011, to above $3 billion at the start of 2012. A failed effort to visit the term loan B market may be partially responsible for the final $3.6 billion figure. Earlier in the second quarter of 2012, Cheniere launched two separate B loans of $2 billion in total, one to complement the bank debt and the other to buy a next-door pipeline from Cheniere Energy. One month later, Cheniere squashed the first and postponed the second, respectively. What triggered that decision remains murky.

Meg Gentle, Chenieres chief financial officer, says the sponsor wanted to ensure that the project had sufficient capital to enable construction of the first two trains, so it pursued multiple pools of potential investors. Once it was clear that the banks could increase their cheaper debt to $3.6 billion, Cheniere pulled the seven-year, $1.25 billion first lien term loan. This, Gentle notes, was the ideal outcome because it preferred to raise all of the project-level debt in the bank market.

But some market observers suggest that the B loan market was too shallow to absorb a $1.25 billion term loan that includes construction risk, particularly when its margin is only 425bp over Libor. To close a deal in that market, Cheniere would have had to increase the pricing, perhaps significantly. At the same time, some bankers were apparently incredulous that the difference between the spreads could hit or exceed 150bp.

Another observer strongly disagrees with this view, contending that starkly different risk profiles between the A and B loans would warrant a far higher margin for the proposed B loan. The B loan would have been drawn immediately, ahead of the equity and most of the bank debt, and, he adds, B loans are almost always pricier than bank pieces. Participating banks were willing to accept larger commitment sizes whether or not their arms were twisted.

Cheniere will probably look to refinance the $3.6 billion loan quickly possibly as soon as late 2013. Financing for the third and fourth trains of Sabine Pass also looms, and banks may benefit from ancillary business opportunities. Morgan Stanley, one of the sponsors newer relationships, has already helped underwrite the equity issue for Cheniere Energy that closed in June. Participating banks may also win commodity hedging, advisory and debt capital markets work.

Now, its on to the financing of trains three and four. Gentle expects an engineering and procurement contractor will sign on for phase two by year-end. Financing is scheduled to launch early next year, and may include the bond component.

Sabine Pass Liquefaction LLC

STATUS
Financial close 31 July 2012
SIZE
$5.49 billion
DESCRIPTION
First two trains of an LNG liquefaction project in Cameron Parish, Louisiana
SPONSORS
Cheniere Energy Partners, Blackstone
EQUITY
$1.89 billion
DEBT
$3.6 billion
JOINT LEAD ARRANGERS
Bank of Tokyo-Mitsubishi UFJ, Crédit Agricole, Credit Suisse, Deutsche Bank, HSBC, JPMorgan, Morgan Stanley, Royal Bank of Canada, Societe Generale, Standard Chartered and Union Bank
PARTICIPANTS
BBVA, CIC, GE Capital, ING, Korea
Development Bank, LBBW, Lloyds, Mizuho, Santander and Scotiabank
SPONSOR FINANCIAL ADVISERS
Societe Generale, Credit Suisse
SPONSOR LEGAL COUNSEL
Andrews & Kurth
LENDER LEGAL COUNSEL
Chadbourne & Parke