DEAL ANALYSIS: Tanjung Bin

03/04/2012

The RM6.7 billion ($2.19 billion) financing for Malakoff's Tanjung Bin Energy coal-fired power project shows that it may be possible for international banks to compete in Malaysia's traditionally insular project finance market. The financing, for a 1,000MW supercritical coal plant, brought together a domestically-issued sukuk, Malaysian ringgit senior bank debt, a ringgit senior tranche and an uncovered international tranche.

The foundation of the Malaysian project finance sector is the domestic sukuk market, and that market's cornerstone is the government-run Employees Provident Fund. While pension funds in other jurisdictions have struggled to accept construction risk and more speculative ventures, the EPF and its kin have been happy to fund on greenfield deals. The market is liquid, though not always cheap, and in the project sector funds toll roads, pipelines and power projects.

A small number of conglomerates dominate the Malaysian independent power sector, including Genting, Ranhill, YTL, Powertek, Malakoff, and, confusingly, the country's national power company, Tenaga Nasional Berhad (TNB), still 35% state-owned. Plant development has until recently been a developer-driven, bilateral process, which has made for solid debt coverages, but mounting public criticism of the model.

Malaysia has, as a result, moved towards a formalised bidding process, run by the country's Energy Commission. Tanjung Bin Energy is the first large financing to emerge from the process. The winning bidder still receives a pass-through on their fuel costs from offtaker Tenaga, but must bid the cheapest energy and capacity tariffs possible. This competition has driven sponsors to be more creative.

The commission released the request for proposals on the project in September 2010, with bids due in April 2011, and selected Malakoff as preferred bidder in June. The process was familiar to international power sponsors, allowing developers to submit comments on draft power purchase and coal supply agreements. Bidders have to supply their own site, however, which provided an advantage to incumbent bidders, which would benefit from existing infrastructure.

The counterparty on the 25-year power purchase agreement is Tenaga Nasional Berhad, while a Tenaga subsidiary, TNB Fuel Services, is counterparty on the 25- year coal supply agreement. Both agreements signed in December 2011, and were the basis for the project's long-term financing. The engineering, procurement and construction contractor on the project is Alstom, with construction due to be complete in 2016.

The sponsor and its financial adviser, HSBC, examined the use of the sukuk market, as well as enhancement from government- owned bond insurer Danajamin, but decided that uncovered debt, with a slight advantage towards the international market, was the most competitive. Danajamin, probably the only bond insurer to launch successfully since the last financial crisis, is believed to work most effectively at extending the maturities and depressing pricing on lower-rated credits.

Given Tanjung Bin's Alstom EPC contract, the size and experience of Malakoff, which owns 25% of Malaysia's generating capacity, or 5,020MW, and the Tenaga contracts, it was highly rated even without any cover. The Ratings Agency of Malaysia owned primarily by the largest banks in the country, awarded the project an AA3 rating.

The financing consists of a RM3.29 billion sukuk with a maturity of 16 years from commercial operations, RM700 million

12- year domestic loan, a 15-year $400 million offshore loan, RM1.3 billion junior equity bridge. The lead managers on the sukuk, which was issued in tranches with maturities of between 5 years and 20 years and at profit rates of 4.45% to 6.05%, were HSBC, Maybank (both as lead arrangers), CIMB, Affin, Bank Muamalat, OCBC, RHB. The arrangers of the ringgit bank debt were Maybank and RHB, while the junior debt arrangers were Affin, CIMB, Maybank, RHB.

The cast of arrangers on the international debt gives a hint as to which banks are currently most aggressive in pursuing regional project finance business. Mizuho, HSBC, BTMU, SMBC, OCBC came into the deal on the back of a cross-currency swap of the same length as the debt, and the sponsors took advantage of an attractive basis swap market. The PPA is denominated entirely in ringgit, so bank appetite and liquidity in the cross-currency market will set the limits for non-Malaysian lenders' participation in the market.

The financing documents for the deal signed in February 2012, and the sukuk for the project closed in March. RAM noted that the deal had an average finance service coverage ratio (FSCR) of 1.16x and 1.74x (without and with cash balances (post-distribution), respectively. The financing includes locks on distributions at a 1.2x FSCR, and a default if it drops below 1.05x. The deal also includes a commitment from Malakoff to guarantee a standby letter of credit sufficient to allow the project to produce a 1.5x FSCR in the event that the project cannot refinance three bullet maturities on the sukuk.

The deal, despite ushering in a slightly unfamiliar cast of lenders, still lacks any export credit agencies. The next project to come to market, the 1,000-1,400MW Prai combined-cycle gas-fired plant, is more likely to feature an ECA tranche. Several of the nine shortlisted bidding groups on that deal feature Japanese or Korean content, and will probably be looking to use low- cost and long-tenor debt from these countries' ECAs.

Tanjung Bin Energy
SIGNED February 2012, sukuk issued March 2012
SIZE RM6.7 billion
DESCRIPTION 1,000MW coal-fired supercritical power plant located in Johor, Malaysia
SPONSOR: Malakoff Corporation
DEBT: RM3.29 billion sukuk, RM700 million domestic loan, $400 million offshore loan, RM1.3 billion junior equity bridge
SUKUK MANAGERS HSBC, Maybank (both also lead arrangers), CIMB, Affin, Bank Muamalat, OCBC, RHB
RINGGIT DEBT ARRANGERS: Maybank, RHB
RINGGIT JUNIOR DEBT ARRANGERS: Affin, CIMB, Maybank, RHB
OFFSHORE DEBT ARRANGERS: Mizuho, HSBC, BTMU, SMBC, OCBC
SPONSOR LEGAL COUNSEL: Shearn Delamore
LENDERS' LEGAL COUNSEL: Clifford Chance and Albar and Partners
LENDER TECHNICAL AND ENVIRONMENTAL: Mott MacDonald
LENDER INSURANCE ADVISER: Aon