Latin American Upstream Oil & Gas Deal of the year 2013: Odebrecht Offshore Drilling

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The $1.69 billion bond refinancing of three drillships for Odebrecht Oil & Gas was probably the largest non-recourse bond financing to date in Latin America. The deal came to market in the unsettled period after the US Federal Reserve said it would scale back its bond purchasing programme. It closed after a month-long postponement, at a 6.75% coupon.

But the Odebrecht Offshore Drilling Finance (OODF) issue, despite this backdrop, demonstrates that Odebrechts bank-to-bond model for financing offshore oil and gas infrastructure is strong enough to withstand market volatility. It even included some more sponsor-friendly terms, and was structured to allow the issuer to acquire additional assets.

There might be mounting nervousness about the financing burden that Brazils national oil company, Petrobras, faces in developing its pre-salt deposits. The collapse of Eike Batistas EBX group may leave project finance lenders with their first losses in Brazilian oil and gas in recent memory.

But Odebrecht, with interests spanning Brazilian and Mexican petrochemicals, Central American design-build, and a concessions business in Brazil, Peru and Colombia, still commands investor attention. It is now the largest single supplier of ultra deepwater drilling services to Petrobras, with seven vessels under charter.

Odebrecht had refinanced two of those vessels Norbe VIII and IX in the bond market in 2010. The $1.5 billion in bonds, for which Banco do Brasil, HSBC, Banco Santander, Deutsche Bank were underwriters, priced for a yield of 6.375%. The proceeds refinanced a $1.34 billion bank and export credit agency construction package that Odebrecht closed for the two vessels in 2009.

The main assets in the OODF portfolio are the ODN I and II vessels, which were also initially financed in the bank market. Their 12-year $890 million financing syndicated and closed in December 2010, with 19 commercial banks, GIEK/Eksportfinans and Kexim participating. Santander and HSBC participated. ABN Amro closed the $440 million 8.6-year financing for the portfolios third vessel, Norbe VI, in 2007.

The Odebrecht waited until the rigs were operational before launching the refinancing. ODN I entered operations in September 2012, and ODN II the month before that. Both ships were built at the Daewoo yard in South Korea and can operate at depths of 3,000m. Norbe VI was built in Abu Dhabi, and has been in operation for Petrobras since 2011.

Odebrecht Offshore Drilling Finance Limited

Status

Priced 26 July 2013, closed 2 August 2013

Size

$1.69 billion

Description

Bond refinancing of ODN I and ODN II ultra deepwater drillships and Norbe VI semi-submersible drilling rig

Sponsor

Odebrecht Oil & Gas

Debt

$1.69 million in nine-year bonds with a 6.75% coupon

Bookrunners

HSBC, ItaúBBA, Morgan Stanley (all global coordinators), Banco do Brasil, BNP Paribas, Santander

Underwriter legal counsel

White & Case; Stocche Forbes (Brazil), Wolff Theiss (Austria); Miranda & Amado Abogados (Peru); Patton, Moreno & Asvat (Panamá), Higgs & Johnson (Bahamas)

Sponsor legal counsel

Davis Polk & Wardwell; Dorda Brugger Joris (Austria); Maples & Calder (Cayman Islands)

Agent legal counsel

Thompson Hine

Lender technical adviser

Okeanos

Odebrecht bought the two ODN vessels from Delba, which had struggled to close the financing, and retains a 40% stake in the two. But Odebrecht has the benefit of 100% of distributions from the ODN, because it lent Delba its equity commitment, and Delbas distributions are swept to repay that loan.

The sponsor had originally intended to include a fourth vessel Tay IV in the portfolio, but decided against, given Tays shorter-dated charter, and the fact that a fourth asset would take the bond beyond $2 billion. Odebrecht instead structured the deal to allow for follow-on issues for additional assets, provided they are drill-ships, have five years remaining on their charter, and the ratings agencies affirm their rating on the issuer.

Odebrecht launched the $1.88 billion bond financing in May 2013, with the aim of using $400 million of the proceeds to pay itself a dividend, and the rest to refinance the construction debt. The global coordinators were Itau BBA, HSBC and Morgan Stanley, while the bookrunners were Santander, BNP Paribas and Banco do Brasil.

But the deal came to market just after 22 May, when the US Federal Reserve started hinting at an end to its bond purchases. The move unsettled fixed income markets, with many investors selling assets to meet redemptions and unwilling to look at new issues. Odebrecht decided to withdraw the issue before formally pricing it, and kept in touch with anchor accounts to see when sentiment would recover.

The deal came back to market in July, and priced on 26 July at a 6.75% coupon, when the ten-year treasury yield stood at 2.58%. The slightly higher coupon meant that, to keep the debt service coverage ratio at the same level, it had to reduce the size of the issue to $1.69 billion. Even at a slightly reduced size, the deal is on some measures the largest cross-border project bond in Latin America.

The new bonds have a larger balloon payment than the Norbe VIII/IX issue, at $736.5 million (around 40% of outstanding principal) compared to a $450 million balloon (around 30%) on the first. But the OODF bonds mitigate this residual value risk in the same way, by using a retention account, on top of a three-month operating expenditure and six-month debt service accounts. The second set of bonds retention account should take the balloon down to 20% of principal, compared to 15% on the Norbe VIII/IX issue.

The OODF documentation also includes a block on distributions if the last four quarters DSCR is less than 1.1x. and if the last six quarters are less than 1.15x. The combination of the bonds structural features and Odebrechts record operating drill-ships helped the bonds sell down, despite a difficult period for Latin American issuers.

OODF now looks like a solid financing platform for Odebrechts other offshore assets. Odebrecht recently closed a $580 million follow-on OODF issue to refinance the debt on the Tay IV semi-submersible rig.

Santander, HSBC and BNP Paribas were coordinators on the follow-on issue, which was a reopening of the 2013 bonds, while Morgan Stanley, Itau and Bradesco were bookrunners. The new debt priced at a 10bp premium over where the bonds traded when Odebrecht launched the deal, for a yield of 6.625%.

The deal featured some additional enhancements, because Tays charter runs to 2020, before the maturity of the bonds. The sponsor enhanced the package with a $30 million sinking fund, and an extension to the debt service reserve from six months to 12 with a letter of credit. These enhancements allowed Fitch to affirm its BBB rating and Moodys its Baa3 rating.

The marketing for the 2013 bonds focused on the travails of OGX. Some OGX and OSX bondholders watched the Odebrecht financings closely to see if the sponsor had any interest in picking up OSX fleet of floating production, storage and offloading vessels, though the bond documentation does not allow the inclusion of FPSOs.

For the reopening, investors were starting to pay closer attention to Petrobras. Petrobras, unlike OGX, has plentiful reserves, and a demonstrated need to mobilise drill-ships to exploit them. But its capital expenditure requirements are immense. Moodys recently downgrade of Petrobras from A3 to Baa1.

Odebrecht now has only one drill-ship that is not bond financed. Odebrecht owns the majority of the Delba III drill-ship, which Delba financed in 2008 with a $488 million WestLB and Inter-American Development Bank-led financing. The vessel experienced cost overruns, and lenders stepped in to provide more debt, and Odebrecht to provide more equity.

Delba and the German KG fund investors that provided the equity at close are now minority owners. But the increased debt means that Delba III has greater leverage than would be easy for the OODF financing to accommodate.

Re-chartering Delba, not to mention the OODF assets, into the late 2020s might allow for a new financing, but that exercise can wait for another day.