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DEAL ANALYSIS: Reventazón

11/03/2014

Costa Ricas electricity grid is heavily reliant on hydroelectric capacity, which accounts for more than 90% of its generating fleet. State-owned utility Instituto Costarricense de Electricidad (ICE) plans to maintain this mix for the next 10 years, and is developing the 305.5MW Reventazón hydro project in Límon province. When it is complete, Reventazón will be the largest power plant in Central America.

Reventazóns debt structure combined a partially guaranteed private placement, debt from the Inter-American Development Bank (IADB), and a local bank tranche. Most IADB A/B loan structures consist of a direct A loan from the multilateral and a B loan from one or more commercial banks. Reventazón, however, featured a private placement instead of commercial bank debt to partially complement an IADB A loan.

The IADB has operated in Costa Rica since 1961. ICE has honoured all of its obligations under the $6 billion it has borrowed from or through the IADB.

For Reventazón, ICE created a Scotiabank-administered trust, Reventazón Finance Trust (RFT), to issue the notes. That trust buys a participation in the entire IADB B loan to Fideicomiso PH Reventazón, a second Scotiabank-administered trust that owns the project. ICE created similar trusts to help fund earlier facilities, including the Cariblanco, Peñas Blancas and Angostura hydro plants.

ICE will build, operate and maintain Reventazón, and will lease the plant from the borrower trust. The financing passes all construction and operational risks through to ICE, including cost overruns, meaning that the deals credit profile is essentially lightly structured ICE risk. Some of the financing for Reventazón is a direct ICE obligation. In 2012, the IADB granted a $250 million direct loan to ICE, which used about $80 million of the proceeds to part-fund its equity contribution to Reventazón.

Financing the plant through a separate trust had some benefits to ICE. Most significantly, ICE can pass on the cost of the lease payments it makes to the trust to its customers through electricity tariffs. Had ICE borrowed directly, it would only have been able to pass through the yearly amortisation of the asset, thus creating a mismatch between the expected 50-year life of the asset and the probable shorter maturity of any direct borrowing.

For Reventazón, ICE was looking to raise more than $900 million in long-dated debt. The longer the average maturity, the lower the average lease payments, and the lower the amount it would have to pass through to consumers.

Reventazon Finance Trust
STATUS
Closed 29 January 2014
SIZE
$1.4 billion
DESCRIPTION
305.5MW hydro power plant, on the Reventazón river in Límon province, Costa Rica
SPONSOR
Instituto Costarricense de Electricidad (ICE)
DEBT
$904 million
LENDERS
IDB, IFC, Banco de Costa Rica, Banco Nacional de Costa Rica, Banco Popular y de Desarrollo Comunal, Banco Crédito Agricola de Cartago
FINANCIAL ADVISER
BNP Paribas
TRUSTEE
Scotiabank
SPONSORS LEGAL ADVISER
Milbank Tweed Hadley & McCloy
LENDERS LEGAL ADVISER
Clifford Chance; and BLP Abogados
INDEPENDENT ENGINEER
Fichtner
INSURANCE CONSULTANT
Marsh

Long-dated bank debt became scarcer everywhere after the 2008 financial collapse, and again during the Eurozone crisis. It is even scarcer for projects located in countries like Costa Rica whose sovereign ratings are below investment grade.

ICE had already financed the acquisition of the project turbines with a sovereign-guaranteed loan, and the plant would not require any other content that would attract export credit agency financing.

A bond, while difficult to structure and market, would allow the borrower access to longer tenors from institutional investors than banks would offer. ICE mandated BNP Paribas as financial adviser on the issue.

The IADB and other multilateral institutions offer tenors that are benchmarked against the private capital raised, says Philippe Birebent, director in BNP Paribas project finance group in New York. If we had gone to the commercial bank market and got 13 or 15 years, the IADB would have extended tenors in that vicinity. However, by tapping the institutional market and raising 20-year capital, the IADB and the IFC were also able to deploy 20-year capital.

The private placement tenor also encouraged local banks to offer debt with a term of 20 years, inclusive of a grace period of 3.5 years.

The IADB guarantee helps limit negative carry, under which borrowers have to pay interest on unused bond proceeds. According to the IADB, the mechanism is designed to allow institutional investors to fund ahead of the other senior lenders. In the event of an acceleration of the IADB B loan, the multilateral is required to partially buy back the B loan from investors. This amount is equal to the A loan that the IADB would have disbursed had it done so on a pro-rata basis.

IADBs preferred creditor status helped the issue achieve an investment-grade rating, from both Fitch and Moodys, for the notes. Fitchs BBB- rating was higher than its rating on both ICE and Costa Rica.

When the Reventazón placement funded on 29 January 2014, its size was lower than the $415 million at which the deal launched in 2013. Instead, the bond portion consisted of $135 million package of 4(a)(2) Reg-S notes with a coupon of 8.1%.

The IADB says that ICE was looking for a private placement of between $100 million and $415 million, but that the issues final size was going to be dependent on market capacity. ICE brought the issue to market in late 2013, and the IADB was prepared for an issue at the smaller end of ICEs expectations, according to Gian Franco Carassale, a senior investment officer at the bank, and its head of syndications, Jozef Henriquez, who add that sponsor and bank were able to quickly make up the difference.

Market observers suggest that a $400 million issue was ambitious, given Costa Ricas rating. But the issue still brought in five North American investors new to ICE and Costa Rica.

On Reventazón, ICE decided to fill the debt gap with a larger colon-denominated local bank tranche, increasing it from the equivalent of about $200 million to $469 million. Banco de Costa Rica provided C80 million, Banco Nacional de Costa Rica and Banco Popular y de Desarrollo Comunal lent C75 million and Banco Crédito Agricola de Cartage lent C9.5 million. The overall debt requirement was $30 million lower because of fluctuations in the dollar/colon exchange rate.

The financing also includes a $200 million A loan from the Inter-American Development Bank (IADB) and $100 million from the International Finance Corporation (IFC). ICE is providing $475 million in equity to the $1.4 billion project, giving the financing a debt-to-equity ratio of 66:34.

The Reventazón B loan private placement could appear on future deals, even if banks to recover their appetite for B loans. Commercial banks are unlikely to lend on B tranches at tenors even close to what an institution could offer.

Jean-Valerie Patin, BNPs head of Latin American project finance, says the Reventazón issue could be replicated in other countries that are just below investment grade. Importantly, the transactions price compares favourably to the corporate one on a relative basis, he says. The coupon was lower than the $500 million issue of 144A 30-year corporate bonds that ICE issued in May 2013.

Ratings agencies are understood since Reventazón closed to have received enquiries from other Central American entities looking to replicate this formula. But future adoption will depend on the IADBs willingness to co-finance those projects.

The Reventazón project also includes the construction of transmission lines, substations and access roads. Construction of the project is about 55% complete, after beginning in 2010. ICE expects Reventazón to enter operations in 2016.