INTERNATIONAL FACULTY OF FINANCE

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Highlights from our recent webinar

Refinance in Renewable Energy Project Finance Transactions

Hosted by Duncan Hughes

Unpacking the Complex Financing Journey of Renewable Energy Projects

As countries race to transition to sustainable energy sources, financing the development of large-scale renewable power projects like wind and solar farms has become critically important yet incredibly complex. In a recent webinar, veteran project finance banker Duncan Hughes walked through the multi-stage evolution and intricate considerations involved in properly capitalizing these capital-intensive initiatives.

Unlike conventional power plants which primarily just require an EPC contractor, feedstock supplier, offtaker, and financing sources, renewable projects involve a host of additional moving pieces. Wind and solar farms need specialized equipment from original equipment manufacturers (OEMs) like Vestas engaged under dedicated turbine supply agreements.

They require sizable tracts of land or maritime areas secured through leases. Transmission agreements must be put in place to evacuate the generated power into the grid, which often involves complex interconnection infrastructure for remote plant locations like the 3.6 GW Dogger Bank offshore wind farm being built 130 km off the Yorkshire coast.

Renewable projects also face the intermittency challenge of only producing power when the wind is blowing or sun is shining. This frequently necessitates backup facilities or battery storage, further increasing complexity. The intermittent nature has also given rise to innovative offtake models beyond traditional power purchase agreements (PPAs), such as priority grid access rules in markets like Germany and corporate PPAs where major tech companies directly purchase renewable energy to offset their Scope 2 emissions.

From a financing perspective, Hughes explained how the capital stack evolves considerably over a renewable project's multi-decade lifespan. In the earliest development stages, sponsors provide high-risk seed equity as many proposed projects never obtain the required licenses and permits to move forward. Once key contracts like the OEM supply and offtake agreements are secured, banks get involved through loan facilities, potentially including "equity bridge" loans to fund the final development stretch before being taken out by a larger equity raise from additional investors.

But commercial banks have little appetite to hold debt for 25-30 years matching a project's operating life. This has led to widespread use of "mini-perm" structures, where banks provide loans covering just the construction period plus a few operating years. These come in "hard" and "soft" varieties - the webinar poll showed strong preference for the flexibility of "soft mini-perms" which use incentives like cash sweeps and dividend stoppers rather than hard repayment dates to encourage timely refinancing.

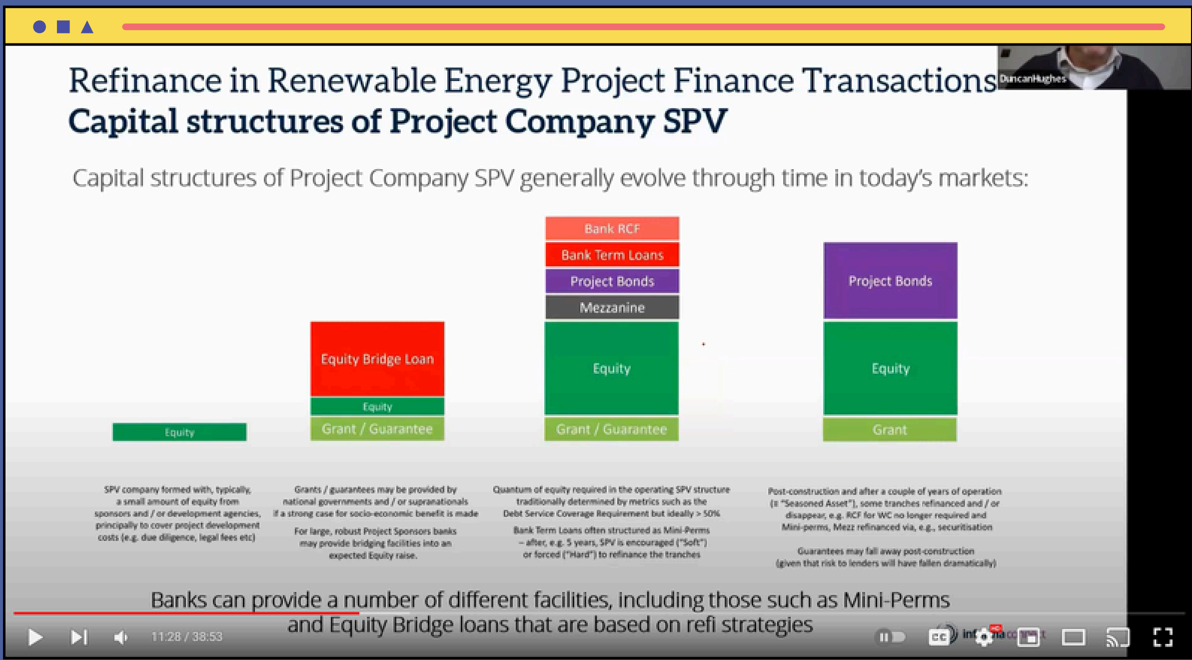
The ultimate refinancing goal for most renewable projects is to access the immense appetite for long-dated green bonds from institutional investors like pension funds and life insurers. These liability-driven investors have massive long-term liabilities to cover and funds are being forced to allocate 10-30% of assets to sustainable investments to meet environmental targets. However, the supply of appropriate green bonds to match their long-dated needs is quite limited.

This has created a burning demand for operating renewable project bonds, compressing yields for those able to achieve an investment-grade rating. Hughes noted particular tightness at the very long end of 30 years or more, where pension liabilities are concentrated.

Issuing these coveted long-tenor bonds provides a cost-effective refinancing for projects while allowing banks to recycle their capital into new construction loans.

Navigating this complex multi-stage financing journey requires close partnerships between project developers and investment banks experienced in syndicated lending and green bond issuance for renewable projects. Getting the right capitalization plan and optimal financing structured at each phase is crucial for ensuring the long-term bankability of sustainable energy projects.

Watch the full webinar on YouTube



Click here to view the webinar

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