MAIDEN BOND IS A COMPLEX ISSUE

THE ACWA POWER MANAGEMENT & INVESTMENTS ONE TRANSACTION IS A COMPLEX STRUCTURED BOND ISSUANCE, WITH A NUMBER OF FIRSTS ATTACHED TO ITS NAME. ROHIT SINHA, DIRECTOR OF ACQUISITIONS AND PROJECT FINANCE, SHARIQ RAHMAN, DIRECTOR OF CORPORATE FINANCE, AND ARVIND MISHRA, EXECUTIVE DIRECTOR OF TAX, ACWA POWER DISCUSS THE STRUCTURING AND IMPLEMENTATION

On May 3 2017, while the Fed was releasing its statement, ACWA Power was pricing its maiden bond issuance, a US$814m structured bond, issued by ACWA Power Management & Investments One Ltd (APMI One) backed by cashflows from a portfolio of eight power generation and water desalination projects in the Kingdom of Saudi Arabia (KSA), and the associated operations and maintenance companies.

For many experienced bankers involved in the transaction, this was the first time that they were pricing a transaction during a Fed announcement, but for this transaction, this was one of the many unusual things that happened.

This was a transaction of many firsts: the first ever private “investment grade” bond from the Kingdom, the largest dollar bond issue by a private sector company in KSA, the first time Moody’s and S&P had rated emerging market IPP/IWPP holding company debt “investment grade”, the first ever senior structured multi-asset transaction from the MENA region, the largest single tranche of holding company debt issued in the emerging markets, and the first corporate non-recourse transaction from the MENA region since 2013.

Jefferies acted as the sole structuring adviser for the issuance. Citi and Jefferies acted as joint global coordinators along with CCB Singapore, Mizuho, NCB Capital and Standard Chartered Bank as joint bookrunners, and MUFG and SMBC Nikko as co-managers.

Background

ACWA Power is a leading private developer of, investor in and operator of a portfolio of power generation and desalination plants – both within the Kingdom and regionally in the Middle East, North Africa, Turkey, Southern Africa and South-East Asia. Its portfolio of plants in operation or development represent 23GW of power and 2.5m cubic metres per day (m3/day) of desalinated water

It is the owner of eight projects in KSA that have an aggregate contracted capacity of 10.1GW of power and 2.3 m3/day of desalinated water – 23% of power generation in KSA and 34% of water generation in KSA. ACWA Power operates many of its projects through First National Operations & Maintenance Company Ltd (NOMAC), an indirect wholly owned subsidiary of ACWA Power and one of the market-leading private sector IPP/IWPP operators, globally.

Sponsors’ objective

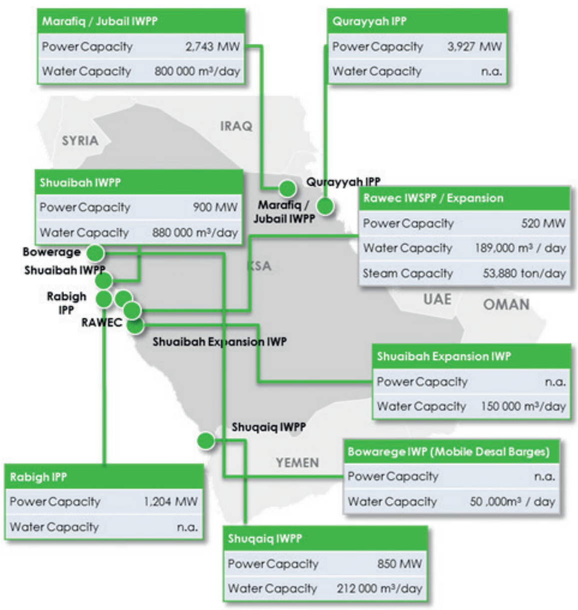
ACWA Power has been an avid fund-raiser for its rapidly growing portfolio, having raised more than US$25bn of financing over its history. This has typically been in the form of project financing at the project companies, with very limited corporate debt required and raised from banks. The company had been looking to diversify its sources of funding, including looking at debt capital markets.

There is an imminent mega opportunity in the form of the possible privatisation of government owned power and desalination plants in the Kingdom, where the scale of funding needed will be huge.

So this transaction, as a way of diversification, would also ensure that its traditional sources of financing – bank markets – would preserve their liquidity for ACWA Power, as it continues on its next phase of growth. This transaction would also give ACWA Power, visibility within the investor community, proving useful for future issuances.

In addition, some of these eight assets were funded on their respective equity contributions, by short-term corporate facilities with typical tenors of four to six years. ACWA Power wanted to take away any residual refinancing risk from these facilities and replace them with longer-term facilities that matched the long-term nature of the assets. Any

FIGURE 1 - PLANT LOCATIONS



incremental financing would be used for the future growth of the ACWA Power portfolio.

Structuring

With the objectives outlined above, ACWA Power worked with Jefferies to look at various financing alternatives for a capital market transaction. ACWA Power wanted to only do an investment grade transaction, given the pricing and liquidity differential between such instruments versus a sub-investment grade instrument. In addition, ACWA Power wanted the transaction to be non-recourse to the parent; so as to preserve the ACWA Power corporate balance sheet capacity.

Given the inherent bankable structure of the long-term contracts, the project companies themselves are levered typically at a 75%–80% level. Hence, a holding company, which gets its cashflows from a portfolio of such companies and is thus structurally subordinated to the project financing, is usually not investment grade.

To get over this hurdle, features inherent to the project financing world were picked up and applied to this capital market transaction. The issuance was decided to be structured similar to a project bond, backed by cashflows from the eight assets (which were all levered), and the associated operations of NOMAC KSA (which was unlevered).

Also, given the contractual structure, it was decided to not have the KSA holding company issue the bonds, but rather a United Arab Emirates-based special purpose vehicle incorporated in Dubai International Financial Centre (DIFC), which would service the bonds through assignment of cashflows.

Certain other securities in the form of a reserve account and pledges were also provided to enhance the security structure – features that are more common in project financings and project bonds.

The bond issue was finally structured as a long-term (maturing in 2039) instrument, amortising during the tenor to match the cashflows from the portfolio, with a weighted average life of c. 13.6 years.

Rating approach

Attainment of investment-grade ratings from two agencies – Moody's and S&P – for a first-of-its-kind portfolio issuance required a deep understanding of the rating process, recognising that neither agency had rated such a structure before. The rating process itself lasted close to four months, with both agencies spending considerable time in understanding ACWA Power and doing a deep dive into each of the projects themselves.

Considerable education and analytical support was required both from the advisers and ACWA Power in addressing all questions and concerns. In addition, the structure was tweaked to ensure that the rating agencies were comfortable that there were no structural weaknesses, and that investors would have adequate protections from any cash leakages, and adequate security in case of enforcement.

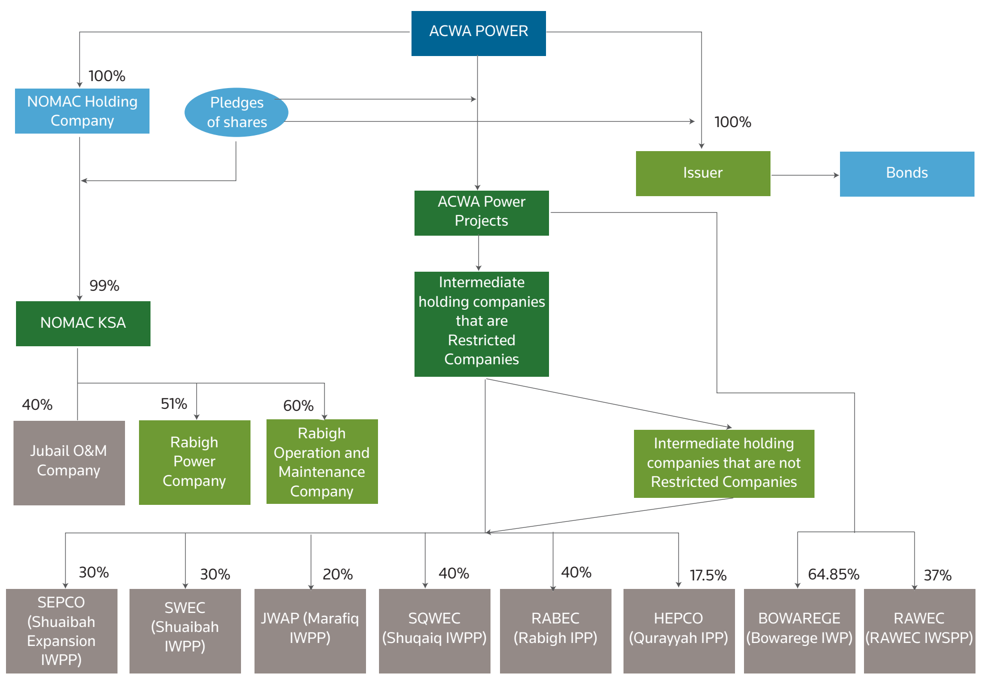
After this long and arduous rating process, Moody's and S&P rated the issuance Baa3/BBB– (outlook stable) respectively.

Execution challenges

Unlike simple capital market transactions, the execution process was extremely challenging. Right from the advisers who had to produce bespoke documents for every aspect, which was a hybrid of project finance and regular capital market transactions, the portfolio itself was large and project financed with multiple stakeholders – partners and offtakes among others.

There was also an aspiration to have a sukuk tranche alongside conventional debt, and the documents have built-in flexibility to address that – this added another level of complexity.

FIGURE 2 - BOND STRUCTURE



More than one hundred consents were sought for implementing the structure and related security. While almost all of them were received, one of them was held up and time uncertain, and it was decided to remove one asset from the structure reducing the secured assets from nine to eight.

The marketing process

Given the specialised nature of the credit, the long tenor, and the amortising profile, it was expected that infrastructure funds and/or pension funds would look at the credit. While initially the thought was to do this as a private placement, it was decided to do it as a 144A/Reg S transaction in order to tap as many pockets of liquidity as possible.

ACWA Power had well recognised from day zero that the inherent subordination of the cashflows, but well mitigated by the diversified portfolio and a robust contractual structure, and the complex transaction structure would require a lot of investor education and outreach. We also knew that investors would require a lot of education around the contractual structure, which is designed to make these projects bankable and attract investment.

In addition, the Kingdom was a new jurisdiction for many investors and for the first private sector investment-grade offering from the Kingdom, a number of investors were looking at the opportunity for the first time. The fact that the KSA sovereign came up with its debut issuance in 2016 and followed and it up with a sukuk issuance in early 2017 helped a lot in this aspect of investor education.

Hence an extensive pre-marketing campaign was done to get investor feedback at every stage of the process. Jefferies met over 50 of the most active market participants across the private debt, infrastructure and EM markets across the world. These investors became the anchor investors once the deal was announced.

The execution process also led to delays in 2016, only allowing ACWA Power to reach out to investors in late November 2016. Roadshows, led by the senior management of ACWA Power, were held across the GCC, Asia, Europe and North America.

With the financials becoming stale in mid-December 2016, the markets being volatile, and end of the year fast approaching, it was decided to re-launch the transaction in 2017 with a refresh of the financials.

During this time when the financials were refreshed and the documentation was updated for time, the bookrunners continued engaging with investors on the credit story, structure of the transaction as well as developments in KSA. This proved to deliver on a very positive traction, when the transaction was eventually announced.

Eventual distribution

The transaction was announced on April 24 2017 followed up with a series of 1-to-1 conference calls with investors during the week.

Formal price guidance of 6.25% was announced on May 2 2017 with a commencement of bookbuilding. The next morning, on May 3 2017, given the strong demand, the pricing was tightened with price guidance to 6.00%–6.125%.

Eventually, a total of more than 120 investors participated in the transaction with a final order-book of US$1.8bn allowing a tightening of the price to 5.95%. The transaction was upsized to US$814m from an initial announcement of US$600m – the maximum size allowed by the financial parameters to achieve investment-grade rating.

With a 2.2x oversubscription this represented good demand for such a structured long-tenor offering. But most importantly, ACWA Power now has a set of high quality investors, which are expected to be tapped into for future issuances.

As a KSA based company, ACWA Power also wanted to issue sukuk alongside the bond, if there was sufficient investor demand. Given the pricing and the resultant size implications, and with the split of demands coming in, it was felt that a US$200m–$250m sukuk issue could be made, but this would not be liquid with a limited set of large investors. Hence, it was decided to abandon the sukuk issue for this time, but the flexibility has been retained.

Conclusion

The transaction has been a big step forward for ACWA Power in further diversifying its sources of funding, and increasingly being visible to international investors that would like to benefit from long-term assets. The transaction managed to achieve investment-grade credit ratings through a hybrid of project finance and typical capital market transactions, which serves as a template for similar portfolio financings in the broader infrastructure sector. ■

FIGURE 3 - THE INVESTORS