

Offshore wind navigating into new territory

Briefing's key takeouts

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With panel contributions from

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Offshore wind continues to be a key source of dealflow for the project finance market, with France set to enter the fray in 2018. But the emergence of merchant projects will likely test the limits of the currently strong equity and debt liquidity. Leading industry players chewed over the market's latest trends at an inspiratia briefing hosted by Moody's Investors Service this week

Offshore wind is undergoing a seismic shift, driven by falling hardware costs, the introduction of competitive tenders, an increasing track record of construction and cheaper financing.

Two years ago, talk in the industry was about how to get project costs below €100 per MWh. Now, it is about how to build and finance schemes at costs half that price or – increasingly – with elements of merchant risk.

At an inspiratia briefing in Paris on Tuesday [6 March], hosted by Moody's Investors Service, a panel of offshore wind experts discussed the investment structures and financial engineering required to deal with this industry-wide trend.

French market

Offshore wind's new market dynamics create an intriguing environment for the next wave of construction deals to come through – in the UK, Belgium, the Netherlands and especially in France, which is lagging behind its European neighbours but may finally finance its first project in 2018.

The country awarded six projects across two tender rounds in 2012 and 2014 but activity since then has been slow. Development teams have spent the last few years since bid award developing a regulatory framework, attaining key permits and overcoming legal challenges.

"We've all been looking forward to getting these projects financed and finally built," said Fabien Levaillant, who is leading the team at [BNP Paribas](#) advising [EDF Energies Nouvelles](#), [Enbridge](#) and [wpd Offshore](#) on the development of three wind farms from round one.

But before the first projects do eventually come to market, they need state aid approval from the European commission, which will scrutinise their feed-in tariff levels – reportedly somewhere between €170 and €200 per MWh – to avoid overcompensation.

As a remedy, the French government may introduce a profit-sharing mechanism to allow it to capture some of the anticipated upside from the projects.

For round three, the state is reflecting on the first two rounds and adapting the rules so it runs smoother. For one, the tariff will be a CfD rather than a FiT, while construction of the offshore grid will be the responsibility of [RTE](#).



Debt liquidity

When they eventually come to market, the French projects will join a healthy pipeline of offshore wind deals in Europe – with new financings and refinancings on the horizon in all major markets, providing dealflow for banks, institutional lenders and other debt providers.

"The offshore wind sector has allowed for a range of investor risk appetites to be satisfied, from through the construction phase with strategic industrial sponsors providing construction guarantees, to operational refinancings with varying levels of risk transfer relating to performance or cost budget," said Christopher Bredholt of Moody's Investors Service.

"The quantity of deals coming to market in the next few years will challenge banks and we expect continued growth in other sources of debt capital," he added.

These other sources of debt capital include export credit agencies (ECAs). Denmark's EKF has played an active role in offshore wind already, while institutions from Belgium, Germany, Norway and Japan have also been seen on deals.

According to Evan Stergoulis from [Watson Farley & Williams](#), the ECAs could be among those set to plug the gap left by the [European Investment Bank](#) (EIB), whose funding capabilities in the UK may reduce after Brexit.

"People like EKF have no lack of desire to put large sums of money to work and seem willing to provide liquidity should funders such as the EIB become unwilling or unable to participate in some UK projects or elsewhere, filling that gap by potentially writing large tickets," Stergoulis said.

Elsewhere, there may be an increase in the use of project bonds, particularly for operational refinancings. [Global Infrastructure Partners](#) (GIP) has used such instruments on both its offshore wind deals to date, Gode Wind 1 and Borkum Riffgrund 2.

"It offers a much longer tenor and eliminates the refinancing risk – that's a very attractive feature – and I think it was worth the effort for us to go down that path," said Antoine Kerrenneur from GIP.

"It was more complicated, it took more time than doing a classic bank financing. But cost-wise, once you take into account the fact that the bond doesn't have any up-front fees, it is very competitive – aligned with or close to bank financing. All-in, we thought it was a very attractive solution."

Merchant environment

While the inspiratia panel seemingly had no concerns about debt liquidity, if current market precedents around cover ratios and gearings are pushed, then the debt limits could be tested.

This is even more true as projects come through with some form of merchant price exposure, such as those from Germany's offshore wind auction last year. Banks are used to considering a portion of merchant risk – through the UK's ROC regime, for instance – but full merchant deals will shrink the liquidity available.

On the equity side, the investor pool will also be reduced without another product taking the risk and hedging it appropriately. The current players clamouring for deals won't be there at the same levels, the panel said.

Meanwhile, utilities have evolved, said Jerome Guillet from [Green Giraffe](#), to the extent that none of them now possess all three key offshore wind skills – construction experience, merchant risk appetite and project finance capabilities.

Guillet said, "These are three very different competencies and none of the utilities have all of them, and since it's hard to bring utilities together in consortia, teams of IPPs and other players that have these strengths can beat utilities as a single player."

Further research

[French offshore wind: good things come to those who wait](#)

[A big step forward: regulatory amendments in French offshore wind sector](#)

[France committed to reaching 70GW of clean energy by 2030](#)

Moody's research

[Power Generation Projects - Global Credit impacts of carbon transition cover a wide spectrum \(Dec 2017\)](#)

[WindMW Credit Opinion](#)

[WindMW Issuer Comment](#)

[EMEA utilities outlook from Nov 2017](#)

