

Knowledge Sharing – Submission II



Genex Power Limited

ABN 18 152 098 854



Australian Government

Australian Renewable

Energy Agency (**ARENA**)

ABN 35 931 927 899

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1) Summary Project Financing Data

Section	Description	Value	Units	Inclusions / exclusions / notes
Finance Details	Debt / equity ratio	0.800	ratio	
	Value of other grants (eg R&D Tax Credit, State government grants, etc)	\$0	\$ (Ex. GST) pa	
	Discount rate (if not Weighted Average Cost of Capital)	10.00	% pa	Include basis for assumptions adopted
	Equity Net Present Value	\$10,764,770	\$ (Ex. GST) pa	NPV10
	Cost of finance	4.75	% pa	Include notes on any linkages to Bank Bill Swap Rates and Margin
	Debt Tenor	6	years	
	Debt Amortisation	19	years	
	Debt provided by CEFC?	Y		Subject to agreement between Societe Generale and CEFC
	Contracted price per unit of electricity supplied	\$88.00	\$ (Ex. GST) / MWh	assuming Solar 120
	Contracted Electricity Volume (year 1)	144880.000	MWh	Include notes on maximum quantity if appropriate
	Assumed degradation	0.35	% pa	Include notes if assumed year 1 degradation is different to later years
	Electricity price indexation	0.00	% pa	assuming Solar 120
	Assumed inflation	2.50	% pa	
	Forecast O&M costs	\$1,530,000.000	\$ (Ex. GST) pa	
	Insurance	\$147,500	\$ (Ex. GST) pa	
	Project lifetime	30	years	
	PPA/Lease contract period	20	years	assuming Solar 120
	Project internal rate of return (IRR), pre-tax, calculated over 25 year project life	9.295	% pa	
	Equity IRR, post-tax, calculated over 25 year project life	13.05	% pa	Include basis for assumptions adopted
	Procurement / Construction	Number of tenders received for primary contract(s)	7	Number
Average price of tenders for primary contract(s)		\$115,000,000	\$ (Ex. GST) pa	

Price of selected tenderer(s) for primary contract	\$102,472,000	\$ (Ex. GST) pa	following further cost reduction in the preferred contractor negotiations
Difference between pre tender estimate and awarded price	\$20,000,000	\$ (Ex. GST) pa	
Total variations to contract during construction period	TBC	\$ (Ex. GST) pa	
Contractor requested variations during construction period	TBC	\$ (Ex. GST) pa	
Contingency amounts used (include justifications)	\$4,050,000	\$ (Ex. GST) pa	

2) Lessons Learnt in Securing Project Financing

a. Contracted revenue is a requirement for large-scale project financing

With the emergence and advancement of renewables in the Australian economy, new aspects of project financing, wholesale activity and grid operations are developing. In addition to these market transitions, the average size of each project is increasing, resulting in project costs well exceeding the 8-figure range.

Given the scale of these projects, significant debt portions are required to reach financial close. In order to borrow these large debt pieces, both commercial and 'specialised concessional-funding' banks require a high degree of contracted revenue to underpin the financing structure.

Initially, project developers of smaller utility-scale renewable projects were capable of borrowing debt from commercial banks without any pre-existing contracted revenue. Banks were more willing to take risk, given the size of the projects and the sudden movement towards renewables in the economy. However, now that these projects are increasing in size, in addition to the uncertainty of the future of renewables within the wholesale electricity market, banks are highly averse to providing debt for uncontracted projects that intend to operate on a merchant basis (i.e. buying and selling straight into the market).

Genex Power was able to secure a 20-year revenue support deed from the Queensland Government. This provided the banks with great comfort, given the existence of pre-determined revenue, length of tenor and the reputability of the contracting partner.

The feedback received from the banks, and the associated lesson learnt, was that large-scale renewable projects must have a high degree of contracted revenue in order to be considered bankable. Thus, there appears to be little-to-no room for large-scale merchant-based renewable projects going forth, at least at this moment in time.

b. Foreign exchange and interest rate movements

Through the assigned EPC contractor for the Project, Genex Power procured the primary pieces of equipment required for the Project from top-tier international suppliers. These included:

- Photovoltaic modules from First Solar (United States)
- Inverters and transformers from SMA (Germany)
- Tracking system from NEXTracker (United States)

These three companies were selected as suppliers based on their proven technological experience, high product quality and low cost (in comparison to any Australian-based suppliers). Although usually highly beneficial, international procurement presents further risks which must be considered in project financing.

Given these transactions involve the exchange of foreign currency, the foreign exchange rate came to play a significant role in determining the final numbers within the project financial model, simply due to the sheer volume and therefore cost of the equipment.

Being a public company on the ASX, Genex Power obtained a proportion of the required project capital through its shareholders. Capital raising was initially completed with discounted shares offered to its existing shareholders. Unfortunately, an unforeseen, adverse price movement occurred in the foreign exchange rates, resulting in a shortfall of the required capital. This meant Genex had to return to its shareholders to raise the additional capital. This was viewed as a negative by some shareholders, particularly those who partook in the initial capital raising given it results in further dilution as well as the greater discount per share given during the second capital raise.

There are various ways that this risk can be mitigated, such as the use of hedging instruments (futures, forwards and options). There are, of course, advantages and disadvantages of each hedging mechanism and with the amount to be hedged. Various hedging mechanisms were used for the Project, mitigating the risk somewhat. However, there was an unforeseen price

movement in the foreign exchange rate that was unfortunately not entirely pre-accounted for.

The lesson learnt is that careful consideration of the foreign exchange rate must be incorporated within the financial close process, engagement in adequate hedging mechanisms is a must as is the possibility of raising supplementary capital to alleviate any risk of price movement.

c. Acknowledging that banks have different requirements

The Project was funded in part by Société Générale, an international commercial investment bank, and by the Clean Energy Finance Corporation, a specialised Australian bank established to promote the growth of renewables in Australia.

Given the existence of two debt-providers for the Project, it became apparent that each bank had differing processes and components involved in securing project financing. Know-your-client due-diligence procedures, debt-to-equity ratio requirements, debt-service-cover-ratio requirements and debt-service-reserve-account requirements, are just some of the ways in which banks can differ in terms of project financing requirements.

In order to satisfy the requirements of each debt-provider, recipients (i.e. project developers) should be flexible and accommodating in terms of interaction with these banks to ensure that each and every criterion is satisfied as part of the securing financing procedure.

d. Understanding renewable project financing and the timelines involved

Although Genex Power has acquired a strong board and management team, with decades of experience and expertise across investment banking, engineering and construction, and project development, the Project was the first renewable energy project developed from the team as a collective.

As such, successfully reaching financial close presented a great opportunity for those involved, leading to new skills and knowledge in terms of what is involved in renewable energy project development and the timelines involved in securing project financing.

Financial close was initially proposed for Q4 2016, with this date being communicated to the market given Genex is a listed organisation. However, project financial close was not reached until Q1 2017, 2-3 months after the proposed date. Although not ideal, this minor delay did not translate toward any negativity in terms of share price value or other negative corporate effects.

The specifics involved in securing renewable energy project financing is something which is difficult to foresee, particularly for project developers who had not previously completed project financing in the renewables industry. Whilst setting clear, confident milestones is important, particularly for a public company whose value is centred around meeting and exceeding milestones, it is important for project developers to not set overly ambitious timelines and to fully understand the complexity and duration involved. This was particularly apparent for the Project, as it involved the interaction between a number of financiers, each with their own internal requirements and processes (as outlined in 2.c.).

3) Criteria, Benchmarks, Standards & Key Project Metrics Demanded by Commercial Debt Providers

a. Debt-Service-Cover-Ratio (DSCR)

The Kidston Project was sized off a 1.25 DSCR on P50 cashflows. Projects are typically banked on DSCR ranging from 1.40 to 1.25 depending on the bank and the risk profile of the projects. Aggressive banks are now consistently banking projects with strong offtake at 1.25 DSCR

b. Debt-to-Equity Ratio

The Kidston Project achieved a total leverage of 80%. That is total debt/total project cost is 80%. This was an artificial debt “CAP” placed on the project by the bank as the cashflow could’ve possibly supported an even higher leverage. The debt cap is applied to ensure some “skin in the game” from the equity investors.

c. Debt Service Reserve Account

A 6-month DSRA was imposed on Genex for the Kidston Project. Most competitive bank are comfortable with 3 months DSRA for projects with strong offtake. Whilst the Kidston Project has a strong PPA in the form of the Solar150, the banks considered Genex a relatively weaker equity sponsor and therefore increased the DSRA to 6 months.

4) Recommendations to Increase the Competitiveness & Reduce the Cost of Project Financing

Genex Power, at the time of pre-financial close, had a market value of ~\$55M. Given this is a small company in terms of ASX-listed organisations, it was considered to be of greater financial risk for debt-providers in comparison to a larger-organisation with multiple projects under development or even in operation. As such, it was crucial for Genex to reduce risk in other areas in order to obtain favourable financial terms from the debt-providers.

One such way risk was mitigated was in the selection of top-tier equipment suppliers (First Solar, SMA and NEXTracker). These large, international organisations were (and still are) the top of their respective fields at the time of project financing, and therefore selection of these suppliers gave great comfort to the debt-providers that there would be little-to-no technological risk for the Project.

This rationale was emulated for the engineering consultant selected, with AECOM acting as the owner’s engineer. AECOM provide worldwide engineering expertise and the selection of AECOM by Genex was considered favourably by the debt-providers. Likewise, the engineering and construction

company selected, UGL, holds extensive first-hand experience for project construction and maintenance. Once again, this was considered to be highly beneficial for securing project financing, particularly for a company looking to complete its first project.

Although these five companies are at the top of each of their respective fields, it was still a requirement from the debt-providers that strong performance guarantees were put in place to alleviate any longer-term risk. This was completed in some cases in the form of bank guarantees issued by the parent company, to provide further comfort to the debt-providers.