Renewable Energy

First Sustainable, LLC

"While there is certainly no exchange for trading such projects, once operational, such projects can be fairly easily bought and sold. As such projects behave as nothing more than a long term set of cash flows with bond like returns. While such transactions can take some time to execute, willing buyers are reasonably readily available."

Scott R. Sidell - CEO, First Sustainable, LLC

First Sustainable is looking to fund a USD3 bn pipeline of solar projects in Europe through master purchase agreements (MPA) and subsequent securitisation … elaborate.

The USD3bn comprise about 600MW of solar projects, most of which are located in Europe - in countries such as Spain, Germany, Italy, France and increasingly in Central Europe - in countries such as the Czech Republic, Slovakia and Bulgaria. These projects are typically 5-20MW's each, with some in Europe, being as large as 50MW's. At present we have fewer projects based in the US and Canada (they typically range from 1-10 MW's). But, we do plan on working on some much larger projects there (Southwestern US) soon.

Your criteria for sourcing such projects?

The Master Purchase Agreement approach contemplates adherence to a rigorous set of underwriting requirements which include:

- Construction completion guarantee by an investment grade construction contractor
- Guaranteed fixed cost 20-25 year operating and maintenance agreement with an investment grade contractor
- Investment grade liquidated damage obligation for breach of construction completion guarantee
- 20-25 year performance guarantee on solar panels by investment grade manufacturers
- 20 year or greater extended warranty on all critical equipment
- 20 year or greater investment grade obligation to buy the power generated

Why have you chosen to focus on solar vs. wind, geo-thermal etc. renewable energy projects?

Of those mentioned, we believe solar photovoltaic (PV) is the most mature, reliable renewable technology with a proven track record. It is also characterised by the most predictable and stable operating costs. Consequently, investment grade contractors are willing to offer guaranteed fixed cost operating agreements, so investors can be confident the operating costs will be known up-front. The cash flows associated with solar projects, we think, are the most predictable amongst the renewable technologies, since it is possible to eliminate any surprises with regard to unexpected operating costs. This should make solar projects appealing to prospective investors who seek long-term, stable, investment grade payment streams because of the favourable risk adjusted returns that they offer relative to unsecured debt for the same or similar credits.

Sustaining deal flow?

For the foreseeable future, public policy worldwide will continue to support broad and powerful subsidies for renewable energy (i.e. there will be an on-going supply of such projects). This is the single most important factor that will sustain an on-going pipeline of such projects. In fact, we are convinced the pace of developing such projects should and will actually increase.

Do you see banks as competition?

Not at all. On the contrary, to the extent that a long-term fund investor is unavailable to absorb the entire project capital structure, banks are instrumental in providing the capital base needed to structure the financing approach we pursue. Our role is to help create a structure that makes it convenient and efficient for global investors, including banks to provide capital for such projects.

Potential risks involved in such an allocation and how you seek to mitigate them?

There are three key risks to financing a shovel-ready project:

- Construction risk
- Operating risk
- Output risk

Construction and operating risk can be addressed by selecting an investment grade construction and operating contractor who is willing to enter into an iron clad agreement that specifically mitigates such exposure. Output risk in the solar context is principally a function of sunshine. Most rational investors understand that such risk is trivial, given the *de minimus* statistical variance of sunshine over long periods of time. For those investors required to structure absolutely fixed payouts with no variance, we can arrange a sunshine variation mitigator from an investment grade obligor, in exchange for a fee that will reduce the investor's IRR by a modest amount.

How do you deal with geo-political; regulatory risks?

We stick to stable countries that have trusted legal systems

Authored by: Sona Blessing

Distinction from private equity players?

We are not a private equity player - we act as an intermediary that arranges rather than invests in projects. The projects we represent, or arrange financing for, do not preclude private equity participation. Given that we often seek to finance 75-85% of these projects with senior debt - these projects often provide an opportunity for leveraged, private equity type investors. Private equity investors would be precluded to the extent that we are able to finance projects with long term investors, such as pension funds, endowments and foundations, based on the assumption that they would absorb the entire capital structure in such projects.

Average duration the investor would be obligated to provide USD100-500 mn for projects that meet established criteria?

Arguably, the investor that enters into a Master Purchase Facility would have a commitment to stand-by with such capital for 1-5 years, depending on the agreement, and will be obligated to finance the project for that period. Once the capital has been deployed, investors should expect to hold their investment for 20 years, assuming no exit is sought.

Provisions for interim liquidity?

While there is certainly no exchange for trading such projects, once operational, such projects can be fairly easily bought and sold. As such projects behave as nothing more than a long term set of cash flows with bond like returns. While such transactions can take some time to execute, willing buyers are reasonably readily available.

Actual returns on an annualised basis and the fee structure?

Such projects can currently provide IRR's of 9 -10%, unleveraged.

Ability to customise structures to meet the specific needs of an investor?

The nature of Master Purchase Agreements is to customise a set of underwriting parameters that satisfy an individual investor - i.e. tailoring project eligibility criteria to suit individual investors.

Other remarks, comments, observations …

The Master Purchase Facility offers investors an efficient solution to acquiring stable, long term, investment grade cash flows by reducing transaction costs; it provides a secure vehicle to project developers, so that they can rely on the financing - provided they satisfy and comply with certain project structure parameters. Such reliability provides comfort to developers, which should motivate them to cooperate with us, thereby reinforcing our project pipeline and developer relationships. The targeted result: achieving efficiency, swiftness and a standardised approach in delivering solar power plants that satisfy investor's appetite for high yielding, stable, investment grade payment streams.

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