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Research Update:

Spanish Solar Project Vela Energy Bonds Assigned 'BBB' Rating; Outlook Stable

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Overview

- Luxembourg-based limited-purpose entity Vela Energy Finance S.A. will issue three fixed-rate, senior classes of notes, pari passu, for a total €404.4 million due in 2036. The proceeds of the issuance will be lent under individual loan agreements to Vela Energy Equityco SL, which will then on-lend them to the 35 operating companies (the ProjectCos).
- The ProjectCos will use the proceeds mainly to refinance a portfolio of 42 solar photovoltaic (PV) parks in Spain.
- We are assigning our 'BBB' long-term issue rating to the bonds.
- The outlook on the rating is stable.

Rating Action

On June 22, 2016, S&P Global Ratings assigned its 'BBB' long-term issue credit ratings to the €310.4 million class A1 bond, €66.0 million class A2 bond, and €28.0 million class A3 bond issued by Luxembourg-based limited-purpose entity Vela Energy Finance S.A. (the issuer). The total amount is €404.4 million. The notes rank pari passu, are due in June 2036, and have a coupon of 3.195% paid on June 30 and Dec. 31 each year starting from Jan. 2, 2017.

The outlook on the rating is stable.

Rationale

Vela Energy Finance will on-lend the proceeds of the bonds to Vela Energy Equityco SL under an on-loan agreement.

The proceeds will then be on-lent by Vela Energy Equityco SL to the 35 special-purpose vehicles (SPVs, ProjectCos) that own the solar photovoltaic (PV) parks.

We anticipate that the ProjectCos will use the proceeds of the bonds to:
- Refinance their bank financing;
- Make an initial distribution to the direct and indirect shareholders;
- Pay fees, commissions, costs and expenses incurred in connection with the transaction; and
- Fund the debt service reserve account (DSRA).

Our 'BBB' rating on the proposed bonds is commensurate with our view of the project's operations phase stand-alone credit profile (SACP).

Operations Phase SACP: bbb

The operations phase SACP is supported by our view of the following factors:

- Supportive regulatory framework under which around 80%-85% of total revenues are not exposed to electricity price fluctuation but are remunerated based on a predetermined regulated return, resulting in low exposure to market risk;
- A solid track record of the technology deployed, which has been in use for over 30 years and has relatively simple routine maintenance requirements, managed by experienced operator Vela Energy SL;
- Low market risk, with a regulatory mechanism implemented to guarantee a reasonable rate of return and removing practically all the risk of pool prices variations;
- Strong financial performance, reflecting the portfolio's level of energy output (MWh);
- A lock-up mechanism, which triggers if the equivalent working hours of any solar park fall within 15% the minimum level unless remedying measures are implemented; and
- A minimum debt service coverage ratio (DSCR) of 1.22x under our base case, an average DSCR of 1.50x, and robust performance under our downside scenario.

Revenue counterparty

The electricity system in Spain is divided into two different markets. Under the liberalized market, players settle prices directly with the operator of the Iberian electricity market, OMIE. Generators offer electricity production and energy prices on a daily basis, while suppliers submit the daily estimated consumption from end-consumers.

Under the regulated market, the settlement process starts with the invoicing of the access tolls (TPAs) and metering of the power that the distributors transfer to the suppliers. The invoices are then sent to end-customers, including a margin. End-customers pay these invoices to the suppliers, which retain the margin only and transfer the TPAs to distributors. The National Commission of Markets and Competition (CNMC) is the sole manager of the regulated payments, which settles the remuneration applicable between regulated parties.

Renewable energies producers receive their revenues through these two channels. We therefore apply a counterparty dependency assessment (CDA) to the Kingdom of Spain (BBB+/Stable/A-2) through the governmental revenue counterparties OMIE and CNMC as they take the collection risk on behalf of the government.

Operations counterparty

The operations and management (O&M) contract will be signed by Vela Energy SL and each SPV owning a PV plant. Vela Energy Asset Management (VEAM) will then be the main subcontractor. The contract is "full cover" and will cover the operating and maintenance needs of PV plants. The corrective maintenance cost will fall on the O&M operator, subject to a certain threshold. If the guaranteed availability rate falls below 95%, the penalty will be up to 2.5% of the O&M price for each 1% drop below the trigger. The penalty is capped at 50% of the contract price.

Vela Energy Holdings S.L. operates 37 similar plants with an aggregate peak installed capacity of 121.7MW in Spain. It also manages a portfolio with a peak installed capacity of 125MW owned by third parties.

In our opinion, the project's routine O&M requirements are relatively straightforward and there are suitable alternative operators available if required. We conclude that the ProjectCos would have the management and financial ability to replace VEAM if required, and we therefore do not apply a CDA to VEAM.

Financial counterparty

CaixaBank will act as the project bank account provider. Replacement language included in the transaction documentation is not consistent with our criteria. However, the project's financial counterparties do not currently constrain the ratings but they represent a cap on the bond credit rating.

Transaction Structure

- Parent linkage: Delinked
- Structural protection: Neutral

Liquidity

Our liquidity assessment is neutral, based on the inclusion of a six-month debt service reserve account.

The project also benefits from a maintenance reserve account (MRA) to fund maintenance works on inverters and modules. The MRA will be built up over eight years from an initial amount of €2.1 million.

Furthermore, if the DSRA and MRA are not at the required level, the proceeds cannot distributed to the subordinated noteholders.

Outlook

The stable outlook reflects our expectation that the project will maintain strong DSCRs sustainably above 1.20x thanks to high availability levels, the effective management of operations by an experienced operator, and limited major maintenance risk. Under our base case we assume a reasonable rate of return of 7.398% through the life of the transaction.

Downside scenario

We could lower the rating on the bonds if the minimum DSCRs under our base case were to drop materially below 1.2x. This could happen if for instance the reasonable rate of return in 2020 was to drop to 5% or lower. A downgrade could also follow unexpected and far-reaching adverse regulatory changes causing us to revise our base case and downside case assumptions, although we view such changes as highly unlikely in light of the recent sector reform and the fact that the current regulatory period runs to Dec. 31, 2019. Furthermore, we could lower the rating on the notes if the bank account provider was downgraded below the current rating on the project, given the direct exposure the project has to this counterparty.

Upside scenario

We see limited upside at this stage. However we would consider raising the rating on the notes if the project demonstrates that it can sustain DSCRs above 1.40x, thanks for instance to higher-than-expected revenues.

Ratings Score Snapshot

Operations Phase SACP (Senior Debt)

- Operations Phase Business Assessment (1=best to 12=worst): 4
- Preliminary SACP: bbb-
- Downside Impact on Prelim SACP: +1 notch
- Capital Structure and Avg. DSCR Impact on Prelim SACP: Neutral
- Liquidity: Neutral
- Operations Phase SACP pre-counterparty limitation: bbb
- Counterparty Assessment Limitation: BBB+
- Operations Phase SACP: bbb

Modifiers (Senior Debt)

- Parent Linkage: Delinked
- Structural Protection: Neutral
- Senior Debt Issue Rating: BBB

Related Criteria And Research

Related Criteria

- Key Credit Factors For Power Project Financings, Sept. 16, 2014
- Project Finance Framework Methodology, Sept. 16, 2014
- Project Finance Operations Methodology, Sept. 16, 2014
- Project Finance Transaction Structure Methodology, Sept. 16, 2014
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Project Finance Construction And Operations Counterparty Methodology, Dec. 20, 2011

Related Research

- Credit FAQ: Standard & Poor's Approach To Rating Renewable Energy Project Finance Transactions, April 20, 2015

Ratings List

New Rating

Vela Energy Finance S.A.	
Senior Secured	BBB/Stable

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.