

# Post-COVID merchant solar: The financier view of Banco Sabadell

**Project finance** | José Rojo speaks to Roger Font of Banco Sabadell for his take on the financing landscape for unsubsidised PV projects following the COVID-19 outbreak

**F**or European solar, the onset of the COVID-19 crisis has come to disrupt one particular segment that had dominated some of the most recent industry spotlight.

In conferences and one-on-one interviews last year, the talk was of the success story of subsidy-free solar; the triumph of PPA- and merchant-based developments precisely in those countries – Spain, Italy – where deployment had been brought to a halt by swings of subsidy policies.

Fast forward to spring 2020, and the picture has muddled. The nosediving of power prices brought about by quarantining measures has crippled the business case of merchant solar ventures. Spanish solar operators have come forward to warn that the funding taps will dry, as banks tighten their terms and conditions before they support a solar venture relying on direct sales to market.

Will the headwinds derail Europe's merchant solar shift or will it prove a temporary pause? *PV Tech Power* put the question to Roger Font, Banco Sabadell's global head of project finance, asset and specialised lending. Recently interviewed, he walked this publication through Sabadell's approach with solar lending so far and plans around merchant deals this year.

**PV Tech Power:** Could you explain to our readers Banco Sabadell's vetting process and rationale when it comes to granting loans to renewable projects?

**Roger Font:** As a bank, our advantage is we've got a very structured financing framework. Based on the project type, the framework applies different criteria to the loan terms, the ratios, the structuring, the leverage level and so forth, so it's all very clear. The other difference is we've got solid knowledge of the market in Spain and abroad, which means we can go for smaller but also bigger projects. There'll be ventures of 30MW but also 400MW, where we'll go alongside other banks.

Thanks to this knowledge, when a sponsor comes forward, we either already know them or we can review them like any other firm: the shareholders, the management team and so forth. Then there is technical due diligence into aspects such as generation parameters, EPC costs and others. When we insert these parameters into our framework it soon becomes very clear what we can and can't provide and, based on that, we can make our offer.

**How many renewable deals did you finance in 2019 and do you expect the flow to slow down following this year's COVID-19 outbreak?**

Last year we financed 2.3GW across 32 renewable transactions, split between 23 greenfield projects and nine brownfield projects. Of the 23 greenfield projects, nine were auction-backed renewables – five with PPA, four without – and 13 went down the merchant route. Of the 2.3GW total we financed last year, 60% was



**COVID-19 has muddled the waters for subsidy-free solar projects such as Iberdrola's 500MW Núñez de Balboa in Spain**

solar capacity and 37% wind power.

All in all, last year we provided more than €800 million through these 32 renewable transactions. Given that some were syndicated, these deals represented a higher €1.8 billion. As for 2020, the number of overall projects we fund will likely not be the same given COVID-19 but the financing model we're striving for will be largely similar. Regarding categories, only 300MW of the 2.3GW last year were pure merchant. The merchant volumes we finance in 2020 are obviously going to be higher than last year's 300MW but as for the exact share – it's tricky to say at this point.

**Even before the pandemic, some in Europe feared a cannibalisation bubble could be forming. Now that power prices have plunged, what are merchant's solar prospects?**

[At Banco Sabadell] our belief is that the sponsors who are carrying out merchant renewable projects have a very high level of sophistication and market knowledge, they have access to all the different information sources so we feel quite reassured on that front. Regarding the talk of a bubble, we don't think in those terms. I see many projects are currently underway, either merchant- or PPA-based, and the present drop in power prices is the specific result of low oil prices and the drop in demand that will eventually bounce back.

**What are Banco Sabadell's expectations in terms of European power prices, both currently and the upcoming recovery?**

In our case and the other banks more generally, we are working under scenario assumptions that there won't be a return to power prices of €50/MWh, in part because of the installed renewable capacity that we see today. Instead, we think we'll be looking at prices of around €40/MWh in the medium to long term. Next year, we're not thinking of €50/MWh but €45/MWh prices.

However, it's important to understand the role of sponsors versus the role of banks. Their play is an equity play whereas what we seek are returns through the supplying of debt. We're not



pretending to have a forecasting vision or to know more than market consultants – the prices I mentioned are the base we're working under and with which we feel comfortable.

**Some of the analysts we talked to say that if power prices do not recover, merchant projects might have to be shelved in the near term. Will activity freeze in places like Spain?**

We're not that worried about the long term. I think there are going to be several merchant deals in Spain this year, and when I say several, I don't mean just two or three. Again – the sponsors we see in the merchant segment are among the most sophisticated we see in the global scene and they have a high equity capacity, which is necessary as merchant players tend to get less debt. If you tick those two boxes, then you realise these sponsors are first rate.

*“Good merchant projects, featuring the right amount of financing and the appropriate structures, will continue to be funded”*

**Some on the developer side have warned banks could be closing the merchant solar funding taps. Are financing terms becoming tighter as power prices fall?**

I can't say we are seeing [this talk of] taps being closed. Good merchant projects, featuring the right amount of financing and the appropriate structures, will continue to be funded. In general terms, the structuring choices of loans haven't changed. Obviously, any alterations to the price curve that forms the base of our assumptions will impact on the volume of debt being supplied. And it's also true that there have been increases to the banks' own funding rates, whose cost is affected by the risk premium of Spain itself.

What is happening, and this is my personal opinion, is that what we do see is many sponsors who were perhaps considering a PPA play – they either turn to merchant or they opt to delay because of the uncertainty around the falling PPA prices. They're likely waiting to see how PPA prices reposition themselves when the market stabilises again.

**Might shorter-term PPAs be the answer for solar developers looking to underpin revenues for just a few years, while the economic shock subsides?**

In terms of financing share, a very short-term PPA does not result in more debt being provided to a project than under a merchant

model. You do see a difference with, say, a 10-year PPA – that's where you would grant the solar project more debt. The numbers are what they are – the longer the better. We have seen some developers seeking PPA cover for two or three years but they are very few. With the projects we're currently studying, we're beginning to note some are going for five-year PPAs, but again it's not that frequent.

**Since the COVID-19 pandemic emerged, has Banco Sabadell been approached by merchant renewable developers seeking funding?**

Several have, yes. We actually signed three renewable funding deals in the post-pandemic weeks, a brownfield transaction and two merchant transactions. There's been some delay on the licensing front but we're continuing to work on it and we hope to sign these deals and others still. I'm hoping to conclude several transactions before the summer, with and without PPA.

**Are there any differences in the profile of the merchant solar projects currently coming forward with financing requests?**

There haven't been any changes with COVID-19. I think all sponsors that had secured authorisation for certain megawatts are pressing on, they have tried to speed up as much as possible with the capacity they had requested. What I'm hearing as well is that [Spain's] administration has not shut down, they're still working on licensing, which is very positive. It's true there has been a bit of a standstill given the volume of delays with licensing, but these projects are now in a position where they're about to be financed. We do see larger projects than last year, but it's similar in general terms.

**Whether the pandemic ends up disrupting merchant solar in a meaningful way, the segment's reliance on power price forecasts will stay in place. How reliable is the data banks access?**

In January, [Banco Sabadell] carried out a review of the various analysts. We spoke to some and examined the power price curves offered by each. The picture was different across each data provider – some prioritised supply and put much stock on the role of new generation, while others also thought it important to factor in the demand, the possible increases from new technologies such as electric vehicles, hydrogen and the electrification of power-intensive infrastructure such as data centres. With these different versions, what a bank can do is to look at the trends, if not at the exact numbers. And if you look at the various consultancies, it is possible to draw some trends across all the different reports. What we do as banks is to end up in a position where we're comfortable around these trends and form our own opinion around the base case and the power price curve. ■