

# Financing options

New sources of lending are coming through for projects in African oil and gas, with some caveats, writes Ed Reed

## FINANCE

### WHAT:

The financing market is opening up to upstream plans.

### WHY:

There are a number of sources of cash available, although there are some concerns about taking on too much diversity.

### WHAT NEXT:

Traders have staked out their position and ECAs are moving towards more involvement.

THERE is an “armoury” of different sources of debt for operators, Bracewell’s managing partner, Jason Fox, told journalists at a recent briefing in the company’s office in London. There is liquidity from the traditional bank market that has always backed independents, he continued, but this has been increasingly supported by newer sources, such as bond markets, and others, for example trading houses.

“There’s a debate as to whether this diversity is a good thing or not. One of the challenges of the recent downturn was that those companies with many different classes of creditors have found it difficult to restructure, so I think diversity is great unless you’re in trouble, and when you’re in trouble you can find it very hard.”

There are a great number of deals around, Fox continued, but it is not like the situation in 2014, when banks and bonds loosened terms. “Many of the deals we’re working on at the moment are for a new class of upstream oil and gas companies that are backed by private equity funds,” he said. These types of companies have a long history in North America and a more recent history in the UK and with some showings in Africa.

### Debt

Reserve-based lending (RBL) is still the “tool of choice” for most independents, although there can be some layering on of other types of debt such as bonds.

Seplat Petroleum raised a US high-yield bond, for instance, and these tend to be large – around US\$350 million and upwards – but there have also been opportunities for smaller amounts of capital to be tapped, with Norwegian bonds becoming popular. While these bonds are listed in Oslo, and governed by Norwegian law, companies do not need a link to Norway to access this type of debt source. “These bonds can be put in place quickly and with a limited amount of documentation, as the disclosure requirement is general rather than detailed and specific,” Fox said.

A newer source of funding for independents has been trading houses, which have become a significant source of deals in the last year. These can either be the independent traders such as Vitol or Glencore, or the trading arms of super-majors such as BP or Royal Dutch Shell.

Smaller companies seeking lower amounts are facing a tougher time, Fox continued. Lenders are leery of the higher risk of such deals and

lenders looking to enter new markets tend to want to participate in the larger deals.

Sub-Saharan Africa has also proved to be difficult, given the defaults stemming from Nigeria. “Some of these defaults are public, some of them have not been made public, because they relate to the financing arrangements of unlisted companies. There is still a wariness on the part of the international banks to lend to the Nigerian market and, looking at the broader African market, there is a pretty small group of banks willing to lend, which is where the trading houses come in.”

While banks may be wary of such work, as a result of new regulations on risk and capital adequacy, export credit agency (ECA) financing has recently moved into the upstream oil and gas debt market. This type of financing has long been an important financing source for the global infrastructure market.

### ECA

ECAs support manufacturing and industry in their own countries by providing financing options to exporters and their customers. “They can provide credit insurance, financial guarantees or, in some cases, direct loans, in order to promote the export of goods and services from the country in which that ECA is based,” Bracewell’s Oliver Irwin said. “ECAs have long been an integral source of funding in the project finance market and have recently entered the upstream oil and gas market.” Indeed, Irwin said that a contractor coming in with funding support from an ECA might well be more attractive to a project sponsor than a cheaper bid from a contractor that does not have that financing attached.

“ECA involvement ... tends to be [focused on] emerging markets, where there are more challenges to getting conventional bank debt anyway,” Fox said.

ECAs have come to play a role in what Irwin described as a “quasi-project finance RBL structure”, with these organisations becoming comfortable with adopting traditional RBL lending techniques such as annual borrowing base redeterminations, alongside aspects of a standard project financing such as long-term tenors and reserve accounts. These new structures present some challenges for ECAs, which have to retool their expertise so they have the required technical knowledge to participate in these financings. ►►

### ECA OPTIONS:

ECAs have provided financing for DEA Group’s financing in Egypt’s West Nile Delta (WND) and discussion is under way for a number of agencies to participate in the Senegal development, involving Cairn Energy and Woodside Petroleum.



▶ One example of this working came in December 2016, when UK Export Finance – the UK’s ECA – participated in a complex hybrid project finance and RBL lending structure to support Vitol’s working interest in the Offshore Cape Three Points (OCTP) offshore oil and gas project in Ghana. This project also involved a slew of multilateral agencies associated with the World Bank, including the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA), the International Development Association (IDA) and the International Bank for Reconstruction and Development (IBRD).

Having an ECA provide an insurance policy or a guarantee to the lenders increases the funding options for a borrower, as the credit risk associated with that loan becomes – at least in part – the credit risk of the relevant ECA, rather than the borrower, who may be located in a commercially or politically challenging jurisdiction. ECAs that can offer direct loans, such as the Japan Bank for International Co-operation (JBIC), Korea’s K-Exim, Canada’s Export Development Canada (EDC) and the UK’s UKEF, “are attractive to borrowers, as these ECAs are typically able to offer longer-term debt at comparatively low interest rates as, unlike commercial banks, they are not subject to the capital adequacy requirements imposed by Basel III”.

**Buying in**

Diversity does not come from the debt side alone, the law firm’s Adam Blythe said, but also on the M&A side. Traders “are not only having a role on the debt side but we’re also seeing them in the equity side”. Service companies are

also playing a role on the buyer side in return for project development contracts.

There is greater supply on the market as well, he continued, with majors taking decisions about where to focus – and where to cut. In Nigeria, for instance, the Western majors have been moving away from the onshore, freeing up space for indigenous companies. Blythe added: “the majors’ retrenchment from certain markets has caused a lot of opportunities to come up for sale, which are attractive for private equity-backed companies to come in and buy.”

New areas are coming up for scrutiny such as Namibia on the frontier exploration side, while Senegal and Mauritania – backed by major oil and gas finds – are also proving attractive. Egypt has also been an area of success in terms of M&A.

Citing BP’s investment with Kosmos Energy in gas projects in Mauritania and Senegal, Blythe said this demonstrated another trend, a “willingness ... to invest in gas reserves ... particularly in Africa, which once upon a time would not have happened. This has been driven, in part, by new technologies that make it easier to commercialise that gas. The emergence of floating LNG [FLNG], and the potential of that to become a commoditised, cheaper project, has been significant.”

The outlook for African resources, therefore, looks largely positive. The transfer of assets should provide smaller companies with opportunities for growth, while financing support – shifting from risk-averse traditional banks to the new breed of ECAs – should help to move fields into production. There are risks, of course. Another oil price plunge would put particular pressure on companies with a range of financial instruments, but the future is looking brighter. ❖