Transaction Update: Exeltium S.A.S.

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Credit Rating(s)	
Senior Secured	
EUR1.583 bil fltg rate bank ln due 06/30/2019	
Local Currency	BBB-/Stable
Senior Secured	BBB-/Stable

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Transaction Description

France-based Exeltium S.A.S. is a virtual power project (VPP) transaction, which provides cheap, wholesale power to large, energy-intensive industrial companies with operations in France. The transaction has a single large upstream contract with French state-owned electricity company Electricite de France S.A. (EDF; A+/Stable/A-1). The transaction's objective is to provide long-term certainty for industrial offtakers in terms of the price and volumes of electricity available.

In 2010, Exeltium secured a €1.58 billion senior secured bank loan due 2019 from a pool of banks. It used this loan to fund an upfront fee of €1.75 billion payable to EDF for the power contract. Exeltium will repay the debt on an ongoing basis with receivables from the various major industrial offtakers under downstream contracts.

Transaction Details

Table 1

Exeltium S.A.S.	
Participants	
Arrangers	Natixis, BNP Paribas, Societe Generale, Credit Agricole CIB
Trustee	N/A
Sponsors	Sponsors are a variety of industrial companies with energy-intensive operations in France
Offtakers	See table 2
Engineering, procurement, and construction contractor	N/A
Technology	Virtual power project
Fuel type	N/A
Upstream contractor	Electricite de France S.A.
Operator	Exeltium S.A.S.
Key features	
Sector	Power generation
Bankruptcy remote	The financing meets Standard & Poor's Ratings Services' criteria concerning bankruptcy remoteness and special-purpose vehicle structures
Debt service reserve account	Maintain a debt-service reserve to fund the next six months' interest and principal payments
Default tests	Maintain both a historical two-year cash flow ratio and a two-year projected cash flow ratio of 1.10x

Table 1

Exeltium S.A.S. (cont.)	
Distribution tests--discounts to offtakers	Prevent distributions unless both the historical two-year cash flow ratio and two-year projected cash flow ratio are at least 1.25x. In addition, if two rating agencies rate the put option provider below 'BBB-' or equivalent, no discounts are made to offtakers
Debt/equity ratio	80% of senior debt to 20% equity and subordinated debt
Security collateral	Limited value of security and enforcement in view of the virtual nature of the project
Cash sweep	30% from years 3-5; 100% from years 6-9.5

N/A--Not applicable.

Rationale

The long-term 'BBB-' rating on the €1.58 billion senior secured bank loan due 2019, raised by Exeltium, reflects a composite of credit factors outlined below:

The 'BBB-' rating reflects the following credit risks:

- Exposure to counterparty risk. Currently, exposure to speculative-grade offtakers has increased to 32%, an increase from approximately 15% six months ago. Despite this increase in the revenue counterparty risk, it does not yet constrain the projects current rating according to our counterparty methodology (See Related Research below). Furthermore, counterparties are required to post an increased level of collateral if their credit quality deteriorates.
- The offtakers' ability to break their power contracts with Exeltium at preset windows in years 10, 15, and 20. Such breaks would, in all likelihood, be driven by the strike price (fixed price) for power being higher than the market price, meaning that the project had become uneconomic.
- The credit quality of the put option provider has deteriorated, triggering a lock up of discounts. If not resolved, this may prompt offtakers to opt out, increasing Exeltium's exposure to the put option provider's credit quality, which is currently speculative grade. Should a lock up continue, we believe it could make refinancing Exeltium's current debts more difficult.
- An aggressive capital structure, as the significant 60% bullet debt maturity in June 2019 demonstrates. (We calculate the 60% bullet maturity using our base-case forecast and including the cash sweep stream). This maturity creates significant refinancing risk. However, the transaction will have partially amortized the debt at the point of maturity.
- An aggressive financial profile, typical of project financing, with approximately 80% of senior debt to 20% of equity and subordinated debt. The base-case annual senior debt service coverage ratios (ADSCRs) are a minimum of 1.42x and an average of 1.63x, computed according to Standard and Poor's definition, which excludes interest income.
- The relatively weak security package available to lenders. This package does not include the physical power assets themselves.

These risks are offset by the following strengths:

- Low or minimal operating risk, including power supply risk. Exeltium benefits from a 24-year 'take-or-pay' power agreement for 148 terawatt hours (TWh), split into seven blocks. EDF is the major electricity provider in France and thus benefits from a diversified production portfolio.
- The competitive price Exeltium offers, in particular with discounts (although these are now in lock up), of the power transaction compared with the current and projected market electricity prices.
- Various structural features that are likely to incentivize Exeltium to manage the project to mitigate risks. For

example, the project's covenants include a cash sweep (from year three onward) and margin-increase mechanisms which, in our opinion, provide Exeltium with an incentive to refinance the bank loan prior to its ultimate maturity date.
- The availability of a put option, signed with a major industrial group, for 51% of volumes that the offtakers may give up from 2020, thereby partially mitigating offtaker risk, although the credit quality of the put option provider has recently led to a lock-up situation.
- An automatic upstream price decrease from 2020. This protects Exeltium in the event that market prices fall below a certain threshold for the remaining 49% of volumes.

Liquidity

The project benefits from a liquidity facility covering six months of full debt service payments.

In addition, offtakers must post a minimum of four months of cash collateral guaranteeing all obligations to Exeltium. Offtakers must provide additional security according to their creditworthiness (for further details, see section below titled "Offtaker risk").

Outlook

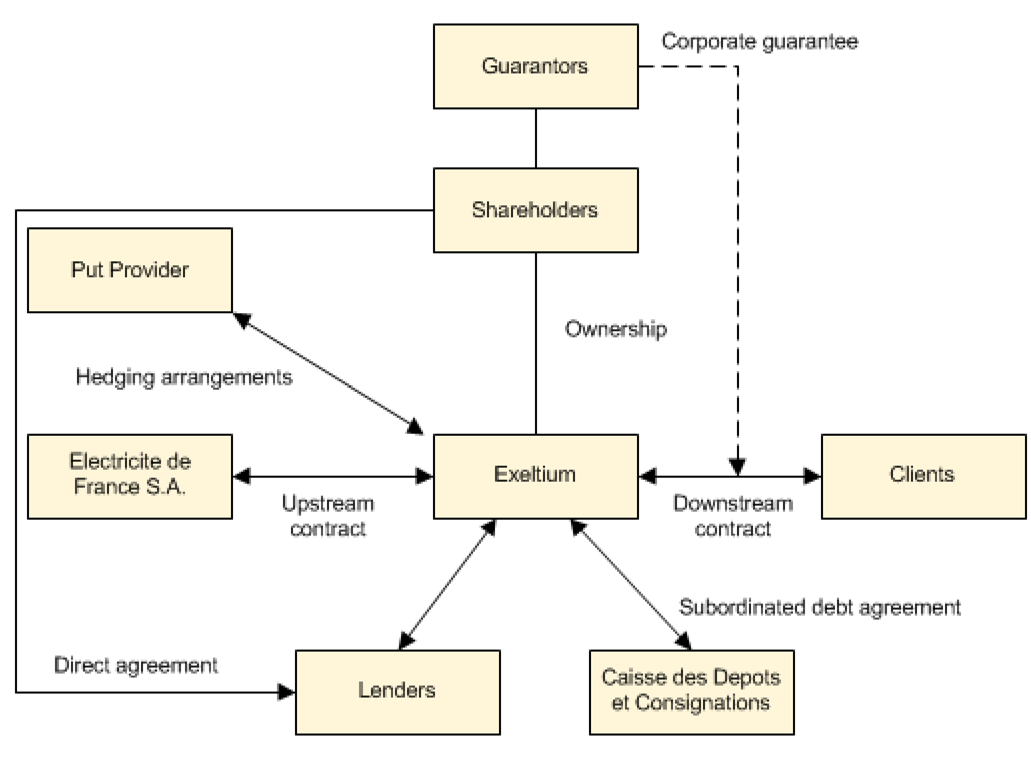
The stable outlook reflects our view that Exeltium will continue to offer a competitive price, thereby reducing the likelihood of offtakers opting out of their contracts in 2019. We would likely lower the rating if the credit quality of the portfolio of offtakers--calculated on a weighted-average basis--further deteriorates to a level that constrains the issue ratings, on application of our project finance counterparty methodology. We believe this could occur if the credit quality of material offtakers deteriorates, or, if the market price of electricity drops to less than Exeltium's price on a sustained basis, because this would increase the likelihood of offtakers opting out in 2019. This would subsequently increase Exeltium's exposure to the speculative-grade put option provider. We would also consider a negative rating action likely if the current lock up is not resolved, as we are of the opinion that the lack of discounts may make Exeltium unattractive to offtakers and increase their likelihood of opting out in 2019.

Finally, we are also likely to take a negative rating action should Exeltium draw on its liquidity line repeatedly, or if the put option provider reduces its operations in Western Europe, resulting in a lower need for power.

We consider that there is limited scope for a positive rating action at this stage.

Transaction Structure

Exeltium S.A.S Transaction Structure



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Project Update

Operations and maintenance

Exeltium's four main operating tasks are set out below. To date, there have been no operational issues and all operations have gone to plan.

- Taking orders for electricity from offtakers, including those through the operating system of EDF's French electricity transmission system operator RTE Réseau de Transport d'Electricité (formally known as RTE EDF Transport S.A.; AA-/Watch Neg/A-1+). This essentially involves balancing the supply from EDF with client demand on a daily basis. Exeltium verifies that total sales (downstream contracts) equal total purchases (the upstream contract).
- Managing surpluses. Clients specify changes in their demand through Exeltium's operating system. Any surpluses are sold to market counterparties or considered as positive imbalances and settled directly with the network. Any loss on the price agreed with client in the downstream contract is borne by the client.
- Managing all administration, including billing clients.
- Managing the contracts. This involves monitoring clients' use of electricity and calling on specific guarantees when required.

Counterparty exposure

As per our new criteria "Project Finance Construction And Operations Counterparty Methodology" published on Dec. 20, 2011, we assign a Counterparty Dependency Assessment (CDA) to counterparties which are material and cannot be easily replaced without significant time or cash flow implications. In this transaction we have individuated two groups of counterparties: upstream and downstream. Upstream consists of EDF, which does not currently constrain the rating.

On the other hand, the composition of the downstream portfolio via the long-term offtake contract could affect the credit quality of Exeltium's revenue line. In this case, the CDA is calculated on the basis of the revenue-weighted basket of higher-rated counterparties that cover at least 85% of revenues. Based on this analysis, Exeltium's rating is not currently constrained.

Our rating on Exeltium is not currently weakened by the current weighted average rating of the portfolio of offtakers. Should the credit quality of the portfolio deteriorate further then our rating on Exeltium could be constrained. Such a scenario could occur should there be either a downgrade of individual offtakers and/or an increased exposure to the credit quality of the current put option provider following opt out.

French power market and future prospects

The offtakers (see below) pay Exeltium for electricity at a price that they anticipate will remain below the market price over the term of the transaction. The price paid is a composition of fixed and variable components, the latter of which are linked to a number of factors.

We believe Exeltium will be able to maintain its competitive advantage over the medium term, and the reasons for this are as follows:

- Market participants expect prices to spike in 2015-2016 as a result of the shutting down of coal plants and a lack of investment in gas-fired generation in France.
- The nuclear phase-out campaign, pursued by newly established French president Francois Hollande, together with the country's greater dependency on relatively unreliable and inflexible renewable energy, is expected to cause volatility in energy prices.
- France's heavy reliance on electricity for the domestic heating of about one third of existing houses and three-quarters of new houses means that we anticipate continued robust demand for electricity within France.

In our view, the combination of the above may create shortages in the electricity market, which would enable the project to remain economic and continue to offer its clients a competitive advantage in the medium term, either in term of lower prices or long-term price visibility.

Project offtakers/counterparties

Any company that fulfils the criteria for being electro-intensive in France is defined under the Framework Law (Article 43 of the Rectifying Finance Law 2005). Any company meeting this criterion can become a shareholder and client of Exeltium (a company cannot have an electricity contract without having a shareholding as well).

In total, we understand that there are 26 companies involved in Exeltium--six founding companies and 20 additional companies. In total, Exeltium's clients will consume about 31 TWh of electricity per year at each of its sites.

Currently, approximately 68% of Exeltium's clients are rated investment grade. The main sectors that these clients cover are the metal, chemical products, and industrial gas sectors, which account for 94.2% of contracted volumes. This is largely due to a legal requirement that the offtakers be electro-intensive companies. However, as stated above, Exeltium is able to on-sell electricity to the market if these counterparties default on their debt.

On a short-term basis, counterparty risk is offset by the requirement for all counterparties to provide a guarantee or collateral of at least four months of its offtake value. This amount increases as the counterparty rating falls, as detailed in the table below. The offtakers can pay this in cash or substitute a bank guarantee rated at least 'A-'.

Table 2

Offtakers Collateral

Rating	Additional Deposits
BBB- or above	None
Between B- and BB+	2 months
CCC+ and below or not rated	4 months

The 10 first offtakers represent approximately 88% of the sold volume. The respective ratings we assign to these offtakers are listed below.

Table 3

Offtakers

Top Ten Clients	Rating
Rio Tinto Alcan Inc.	A-/Stable/A-2
ArcelorMittal	BB+/Negative/A-3
Arkema S.A.	BBB/Stable/A-3
L'Air Liquide S.A.	A/Stable/A-1
Solvay S.A.	BBB+/Negative/A-2
Total S.A.	AA/Stable/A-1+
Norske Skogindustrier ASA	B-/Negative/B
Ineos Group Holdings S.A.	B-/Stable/--
Rhodia	BBB+/Negative/A-2
Roquette Freres	--/--/A-2

Put option provider

The credit quality of the put counterparty has deteriorated and has triggered the lock up in discounts.

Consequently, Exeltium is no longer able to guarantee the payment of the discount to its offtakers until the lock-up event is solved. However, the offtakers cannot opt out of their contracts until 2019, and we believe that the likelihood of them doing so after this date remains low, given that the current and projected short-to-medium term French electricity market price compares well with the contracted price. Concurrently, we believe that the likelihood of opting out will also depend on the successful resolution of the lock up, which would enable Exeltium to return to offer discounts, hence the project will offer a more competitive price than the market.

Failure to arrange a solution to the downgrade of the put option provider within 18 months will trigger a cash sweep using the cash locked within a dedicated account. This would be applied to the installments on the senior loan in inverse order of maturity and in doing so, would reduce the overall amount of senior debt outstanding. This would subsequently mean no discount for the offtakers. Exeltium does not pay dividends, but it can discount the downstream price. There is consequently a clear incentive for the offtakers/shareholders to arrange a solution suitable for the lenders, which may take the form of one of the following available options:

- Exeltium can suggest any solutions that cover the contractual obligation under the put option (such as a guarantee or margin call). If these solutions are not acceptable to the lenders, Exeltium can address the exposure to market prices with another hedging solution.
- Exeltium can terminate the put option in the case of a material deterioration in the put option provider's financial quality. In this case, a termination amount payable by the put option provider is computed. This amount could be used to find a new hedging solution acceptable to the lenders.
- Any other solutions that the lenders find satisfactory covering potential exposure to market prices.

If an acceptable solution cannot be found, the downgrade of the put option provider to speculative grade could have a negative influence on the project, although only if this is coupled with a sustained drop in the price of electricity in the French market--which we do not currently envisage. This would increase the likelihood of offtakers opting out, hence forcing Exeltium to exercise the put, which would increase the projects exposure to the put option providers credit quality (currently speculative grade) and potentially cap Exeltium's rating as a result.

Financial Risk Profile

Financial forecasts

Exeltium has revised its financial forecasts to include actual results to June 30, 2011, and has updated its macroeconomic assumptions. The new forecasts demonstrate a Standard & Poor's-defined ADSCR (excluding interest income and using our inflation assumptions) of a minimum of 1.47x in 2018 and an average of 1.61x. This represents a slight weakening of the average but an improvement of the minimum in the project's forecast financial performance compared with June 2011, when the forecasts were for a minimum of 1.42x and an average of 1.63x.

The deterioration in the average ADSCR from the June 2011 model largely reflects the correction of a modeling adjustment, a small change in the modeled debt profile, and the exclusion of interest income.

Under our sensitivity analysis, we run a selection of scenarios over the life of the bank loan, a sample of which we list along with the outcomes in Table 1. Under our combination stress tests, the minimum ADSCR falls to 1.31x in 2016, with an average ADSCR of 1.53x. In our opinion, these sensitivity tests demonstrate the project's relative strength, especially compared with its peers in the same rating category.

Table 4

Sensitivity Analysis

	2011 figures after model adjustments			
Scenario	**Minimum ADSCR**	**Average ADSCR**	**Year of minimum ADSCR**	**Loan life coverage ratio**
1. Standard & Poor's Base Case	1.47	1.61	2018	1.93
2. Low Price Energy (Poyry Case)	1.47	1.61	2018	1.93

Table 4

Sensitivity Analysis (cont.)				
3. Default of 20% offtakers from 2013 to first opt-out*	1.44	1.6	2017	1.86
4. Zero inflation	1.47	1.62	2018	1.94
5. Operating costs +20%	1.47	1.61	2018	1.93
6. 30% opt out since Year 10	1.47	1.61	2018	1.84
7. Combined 2 and 3	1.39	1.57	2018	1.84
8. Combined 2 and 4	1.47	1.62	2018	1.94
9. Combined 3 and 4	1.44	1.59	2017	1.86
10. Combined 2,4, and 6	1.47	1.62	2018	1.94
11. Combined 2,3,4, and 6	1.34	1.54	2018	1.81
12. 100% defaulted and 2	0.95	1.25	2016	1.17

ADSCR--Annual debt service coverage ratio. *The default of 20% of clients leads to a higher stand-alone ADSCR given Exeltium's ability to sell the power to the external market at a higher price than the one envisaged in the offtake contracts.

The financial model base case is built around our assumption that inflation will be 2.5% in 2013 and 2% thereafter.

Refinancing risk

The overall term of the transaction is 9.5 years, although the deal structure is sculpted to amortize over 22 years. One of the transaction's key weaknesses is refinancing risk, which occurs only one year after the offtakers' first opt-out window.

The transaction includes a number of incentives for management to seek refinancing at an earlier stage due to the following factors:

- 30% of cash is swept into automatic prepayment of debt if the debt is not refinanced before the start of year three.
- 100% of available cash flow is swept into the automatic prepayment of debt if the transaction is not refinanced by the start of year six.
- There is an increased margin to provide the transaction with a greater incentive to refinance.

Due to these incentives, the 'BBB-' rating on the bank loan reflects our belief that Exeltium will develop a credible refinancing plan when the 100% lock up nears in 2015. In our view, this would likely leave adequate time to complete the refinancing.

Related Criteria And Research

All articles listed below are available on RatingsDirect on the Global Credit Portal, unless otherwise stated.

- French Power Transaction Exeltium Senior Secured Debt Ratings Affirmed At 'BBB-' On Satisfactory Project Performance, Dec. 20, 2011
- Updated Project Finance Summary Debt Rating Criteria, Sept. 18, 2007

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