## What is infrastructure debt?

| Energy | • A global asset class  
|        | • Huge scale, measured in the trillions  
|        | • Diversified sector  
|        | • Typically defensive / low correlation to the business cycle  

| Energy debt | • Predominantly private debt – higher yield than corporate bond or leverage loans  
|            | • Backed by energy assets or projects – equity investors provide a cushion against loss  

Energy Infrastructure, a diversified asset class
How infrastructure debt works

- **Project company**
  - Builds or buys an infrastructure project
  - May own the assets outright, or through a concession

- **Equity investors**
  - Own the project company
  - On average, provide about 35% of the capital of the project company

- **Lenders**
  - Provide debt to a project, secured on the assets
  - On average, provide about 65% on the capital of the project company

- **Operator**
  - Operates the project under a management contract

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Defensive characteristics of infrastructure

- Infrastructure is typically resilient in a recession
- Moody’s research (chart below) shows that infrastructure credit is about one third as volatile as corporate bonds
- Infrastructure performs well in recessions (shaded areas below)
- Some infrastructure sectors (e.g. utilities, renewable energy) are more defensive than others (e.g. container ports)
Infrastructure debt is resilient

**Equity cushion** provides protection
- Averages 35%
- Needs to be fully wiped out before lenders suffer a loss

**Security** over assets
- Gives lenders control and a senior-ranking position following a default

**Strong covenants**
- Financial covenants provide protection against underperformance
- Operational covenants ensure the project is properly run

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**Low default rates** for infra debt

**High recovery** following default
Infrastructure debt has a high yield

Historically dominated by banks, but following the financial crisis and tougher regulatory capital rules, **bank lending has declined**.

Demand for capital is higher than ever, leading to a **supply-demand imbalance**.

Infrastructure debt is a specialist asset, leading to **high barriers to entry**: many lenders are not equipped to participate.

Private debt backed by infrastructure can yield **3%+ more** than equivalent bonds or leverage loans.

Returns on infrastructure debt are **double** those of high yield bonds, with **lower volatility**.

- Share price of SEQI (46% total return)
- NAV of SEQI (33%)
- High yield bonds, Sterling hedged (16%)
Matching credit profile with capital providers

The risk-return profile continuum

- **High Yield Lenders**
  - LIBOR+ 500 - 700
- **Investment Grade Lenders**
  - LIBOR+ 100 - 250

Who is this for?

- Mezzanine / High Yield funds such as Sequoia
- Structured Finance Desks (DB, JPM, GS)
- Family offices etc.

- Banks (HSBC, Barclays, SocGen)
- EIB / EBRD
- Insurance & Pension (Aviva, AXA, Allianz)
- IG Debt Funds
Developing the capital structure

Simple capital structure

- OpCo debt (1st lien Senior Secured)
- Equity

Capital structure with junior debt

- OpCo debt (1st lien Senior Secured)
- Junior debt (2nd lien / Mezz / Holdco)
- Equity

- Classic project capital structure
- All debt at the opco level, with direct pledge over all assets of the project
- Significant difference between debt yield vs equity IRR
- Requires significant owners’ equity contribution
- More conservative risk-return profile

- Opco debt as before, now with the addition of a further layer of debt with 2nd lien on assets and/or shares of the opco
- Offers investors the opportunity to capture a yield between opco debt and equity yields
- Less owners’ equity needed
- Higher equity IRR achievable

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- Higher equity IRR achievable
## Case study 1 – Forsa Energy (UK gas peaker construction financing)

- Provided HoldCo debt to finance the construction of three 20MW gas peaking plants in UK
- Flexible generation technology is an emerging asset class expected to become increasingly important as renewables increase the intermittency of the grid.

### The need
- Raise subordinated debt to participate alongside senior financing to a portfolio of gas peaking plants
- Borrower need to develop a platform to roll-out its future plant construction

### Sequoia’s proposition
- Provide a HoldCo loan with the provision to increase facility size as the sponsor rolls out its portfolio
- Allow the borrower to recycle equity capital to future projects

### The value add
- Provide a flexible platform to support sponsor growth activity
- Enhancement of equity returns to the sponsor
- Free up borrower capital to utilise on future CapEx
Case study 2 – NEOEN (French renewables holdco financing)

- Headquartered in Paris, France and active in the solar power (60% of portfolio) and wind power (40%) sectors
- Significant presence in France, Portugal and Australia
- Entered Euronext in 2018, raising €450 million
- First French unicorn in the renewables field

The need

- Raise €40 million equity on existing portfolio to fund new asset development
- Need to achieve quick turnaround of change of control waivers from various lenders at opco level

Sequoia’s proposition

- Provide a loan at the holding company level
- Free up €40 million of equity to fund new projects
- No change of control triggered at the opco level of any project

The value add

- Faster execution than equity raise
- No mandatory prepayment triggered at the opco debt level
- No equity ownership dilution
- Enhancement of equity returns
Conclusions

• The addition of mezzanine debt on energy projects can fill the gap between senior debt and equity by reducing the size of equity commitment and enhancing equity IRR.

• Private Debt funds, such as Sequoia’s infrastructure debt funds are well placed to provide junior debt capital to meet our energy capital needs:
  – Enhance value to all capital providers to a project
  – Provide superior flexibility in financing terms, which reflect the nature of our capital
  – Offer an attractive risk-return asset profile to investors

• Growth of Private High Yield Debt funds goes hand in hand with:
  – Investors seeking to deploy their capital with more predictable performance than equity but having higher returns than senior debt
  – Equity sponsors adding a further layer of debt in order to enhance equity IRR