THE UNDERGROUND CAPITAL MARKET – HARD TO ACCESS BUT WORTH THE TROUBLE

PRIVATE PLACEMENT DEBT DEAL OF THE YEAR

Transaction: *Norspan LNG VII AS $220 Million Senior Secured US Private Placement Bond Issue*
Winners: *Barclays, Pareto Securities*

Everyone knows that debt capital is in short supply and expensive. The banks have pulled in their horns, as they deal with loan losses and regulators. The Norwegian bond market is back in fits and starts and remains discriminating with short tenors. And, lastly, the MLP market is priced at implied yields which make it difficult to do accretive drop-downs with equity finance. Perhaps the only active source of capital these days is the leasing market out of Asia.

Nevertheless, there is money out there but it is highly selective and it keeps a low profile. It has been around forever but for the most part has avoided shipping, with few exceptions. We refer to the private placement market, which is largely risk averse as its funding come primarily from insurance companies and pension funds. Entrée usually requires a credit agency investment grade debt rating. With a paucity of shipping companies with an investment grade rating, nominations in this category are at best infrequent. This year we received two strong nominations in this category.

Citibank nominated the £650 million (including a £70 million add-on) private placement it led on behalf of the DP World London Gateway Port Limited, a newly developed deep-sea container port purpose-built to handle Ultra Large Container Vessels. The senior secured facility matures in December 2045 and consists of fixed rate, floating rate (fully hedged) and inflation-linked tranches. The structure resulted in significant savings for the issuer as it consists of 30-year fixed rate debt locked at historically low base rates with a long principal repayment grace period. Obtaining this long-term fixed rate financing at such an early stage in the development is highly unusual. The financing was structured to allow DP World to continue to execute on its growth strategy by allowing for additional debt incurrence to build three further berths and allow for further recap once the debt has started to amortize.

In addition to overcoming the fact that it was a shipping transaction, this year's winner had to overcome the additional challenge of structuring a project financing owned by an SPV whose sponsors were seeking non-recourse financing. The question was how to garner the exalted investment grade credit rating which was required.

Fortunately, the industrial shipping company Knutsen of Norway owned the perfect asset, a 2010-built DFDE LNG carrier, which was chartered to Gas Natural SDG, a Spanish natural gas utility, with a remaining fixed period of about fifteen years. The combination offered the possibility of a non-recourse project financing with security in the vessel and contractual cash flows from a BBB/Baa2/BBB+ rated utility. After receiving investment grade ratings from both Kroll Bond Rating Agency and Fitch Ratings, Knutsen structured a deal with an SPV issuer, Norspan LNG VII AS, as issuer and then went out to its investment bankers who proffered a

$220 million note due in 2032 to pension funds and insurance companies located in the US.

When compared to recent MLP dropdown prices for LNG carriers, $220 million for non-recourse financing is fairly attractive. The offering was well received and heavily over-subscribed. The margin for the Notes was cleared at 235 bps, in line with expectations, and the Notes will pay a fixed coupon during its tenor of 4.66%, which is the spread above the 10-year US Treasury bond, which was the benchmark in terms of duration since the notes are structured as an annuity in contrast to most bank loans. With the election of Donald Trump and the likely implementation of his policies, there were dramatic shifts in the equity, currency, commodity and debt markets, with the latter adversely affecting government bond prices with yields jumping about 50 bps in the wake of his election raising the price to the issuer. Proceeds of the offering will be used to refinance bank debt and to pay dividends to the shareholders. The transaction is somewhat unusual in that the financial covenant allows for distributions based upon a debt service coverage ratio test despite the fact it is a project financing. Details of the transaction are shown below in the Guts of the Deal.

GUTS OF THE DEAL

Issuer	Norspan LNG VII AS (SPV)
Sponsor	Knutsen OAS Shipping AS
Amount	$220,000,000
Notes Offered	Senior Secured US Private Placement Bond
Coupon	4.66%
Issue Price	100.00%
Yield	4.66%
Spread to Benchmark Treasury	2.35%
Tenor	15.2 years
Amortization	Annuity with an average life of ~10.0 years
Guarantees	None
Ranking	Senior debt in project financing
Security	First mortgage, assignment of time charter and other customary securities in a transaction of the kind.
Undertakings	Traditional and customary
Financial Covenants	See Dividends
Dividends	Subject to distribution test (Debt Service Coverage Ratio)
Use of Proceeds	Refinance bank debt and dividends to shareholders
Credit Rating - Fitch & Kroll	BBB-
Lead Manager	Barclays
Co-Manager	Pareto Securities
Governing Law	U.S.
Incorporation	Norway
Listing	Not listed