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Research Update:

Spanish Solar Project Sonnedix Finance 'BBB+' Debt Ratings Affirmed; Outlook Stable

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Rating Action Overview

- Sonnedix Finance S.A., the issuer (previously known as Vela Energy Finance S.A.), has continued to demonstrate strong operations since issuing its senior secured bonds, sustaining high availability and generation levels above our P90 assumption.
- Our rating on the project remains constrained by the credit quality of the bank account provider, CaixaBank S.A. (BBB+/Stable/A-2).
- We therefore affirmed our 'BBB+' issue rating on Sonnedix Finance's senior secured debt.
- The outlook on the debt remains stable, reflecting that on the bank account provider and our expectation of stable operations, coupled with the minimum annual debt service coverage ratios (ADSCR) close to 1.30x after 2026.

Project Description And Key Credit Factors

In 2016, Luxembourg-based limited-purpose entity Sonnedix Finance S.A., the issuer (previously called Vela Energy Finance S.A.) issued three series of notes totaling €404.4 million. Sonnedix Finance S.A. lent the proceeds of the bonds to Sonnedix Equityco S.L. under an on-loan agreement. Sonnedix Equityco S.L. then lent the proceeds to 35 special-purpose vehicles (ProjectCos) that own and operate 42 solar photovoltaic (PV) parks. The bonds rank pari passu, mature in June 2036, and have a coupon of 3.195% paid on June 30 and December 31 each year.

The portfolio has an aggregate gross generating capacity of approximately 87.7 megawatts (MW) on a nominal basis, with peak capacity of 98.4MW. The portfolio of PV parks owned by the ProjectCos is closed, meaning that PV assets cannot be added or removed during the term of the financing. The majority of the parks began commercial operations in 2008, and they all benefit from regulated remuneration for an additional 17 years.

Strengths

- The deployed technology has a solid track record. Of the installed generation capacity, 72.9% consists of crystalline silicon modules, the most widely used technology in PV plants worldwide.

21.7% uses cadmium telluride (CdTe) thin-film technology, which we consider to be commercially proven, and mostly provided by the world's leading manufacturer, First Solar. The remaining 1.4% uses amorphous silicon thin film technology. Therefore, we expect the technology to continue supporting generation in line with the track record.

- Geographic and technological diversification protect against unexpected disruptions. The plants are in different parts of Spain, and the technology was provided by several different manufacturers. In addition, the project benefits from a cash-pooling mechanism.
- The vast majority of revenue is regulated. Renewable projects under Spanish regulation benefit from a more stable remuneration regime than peers in other regions. This is because most revenue come from the regulated component of the regime, which is unrelated to demand or production, subject to a minimum threshold of electricity production. This feature underpins the project's stability of cash flow and limits market risk.
- The O&M agreement covers the full replacement of inverters for around 80% of the installed capacity in the plants. The replacement of the remaining 20% is incorporated into our forecasts, and mitigated additionally by the maintenance reserve account.

Risks

- Following the remuneration revision for renewables projects in late 2019, in our base case, we assume a 7.09% rate of return for Sonnedix Finance over the next four years. Currently, we lack visibility on open litigations for the PV parks in the portfolio and the Comisión Nacional de los Mercados y la Competencia (CNMC) has not confirmed the applicable rate of return for each plant. As such, we assume they will be entitled to a remuneration of 7.09% until December 2025. We assume the debt will be exposed to regulatory reset risk after this date as the remuneration remains uncertain.
- Although not unusual, some modules show visual defects such as yellowing, snail trails, discoloration, and hot spots. However, under the regulatory framework, the majority of revenue depend on reaching a defined generation threshold, which we do not regard as difficult to achieve. This, along with the adopted corrective module replacement program, mitigate the risk of underperformance.
- The debt does not benefit from a perfected first-ranking security interest on land and equipment to avoid incurring the associated stamp duty liability. Instead, it relies on a binding contractual obligation (a promissory mortgage) from the issuer to grant security over equipment on the occurrence of defined trigger events, including the debt service coverage ratios (DSCRs) falling below 1.10x. However, the project's receivables--that is, their rights to remuneration under the regulatory regime--are pledged as security, which we view as a mitigant.

Rating Action Rationale

PV plants have continued to demonstrate strong performance since the start of operations. The project achieved high availability levels, more specifically 99.2% in 2020, and generation levels have been on average 149,525 Mwh in the past three years, above our P90 assumption (a production scenario with a 90% probability of being achieved). This supports our assumption that the plants' generation will continue to be robust during their lifespan. We view the portfolio diversification as positive, since, in any given year, if a particular plant underperformed, another plant's overperformance would offset the setbacks on production.

Reducing costs to operate similar PV portfolios in Spain prompted us to revise our assumptions on O&M and inverters expenses. The downward trajectory of costs has been underpinned by the lower cost of the equipment and spare parts, increasing competition, and economies of scale in the PV Spanish market. The revised assumptions translate to slightly higher ADSCRs under our base case and downside case assumptions.

The credit quality of the bank account provider, CaixaBank, currently constrains the project's creditworthiness. As a result of the project´s strong track record and improved metrics under our assumptions, Sonnedix Finance can now reach an S&P Global Ratings-adjusted preliminary operations phase SACP of 'a-' ahead of counterparty limitations. However, the credit quality of the project is weighed down by our view of CaixaBank's credit quality (BBB+/Stable/A-2), since the replacement language included in the documentation in the event of a downgrade of the counterparty is not consistent with our financial counterparty criteria. This led to today's rating affirmation and the maintenance of a stable outlook.

Outlook

The stable outlook reflects that of the bank account provider, CaixaBank S.A., which currently constrains the rating. It also reflects our expectation that the project will maintain strong ADSCRs, with the minimum close to 1.3x from 2026 onwards thanks to high availability levels, the effective management of operations by an experienced operator, and limited risk of cost overruns for major maintenance or equipment repairs.

Downside scenario

We could lower the rating on the bonds if the minimum ADSCRs under our base case trends toward 1.2x. This could occur, for example, upon higher operation and maintenance costs--most notably the replacement of inverters--or following the revision of the reasonable rate of return.

In addition, we would lower the rating on the notes if we downgraded CaixaBank, given the direct exposure the project has to this counterparty. Similarly, we would revise the outlook on the notes to negative if we took the same action on CaixaBank.

Upside scenario

We could raise the rating on the notes by one notch if we upgraded CaixaBank. Similarly, we would revise the outlook on the notes to positive if we took the same action on CaixaBank. This would need to be coupled with strong operational and financial performance.

Base Case

Assumptions

- Reasonable rate of return: 7.09% for all the life of the debt absent legal comfort on open litigations.

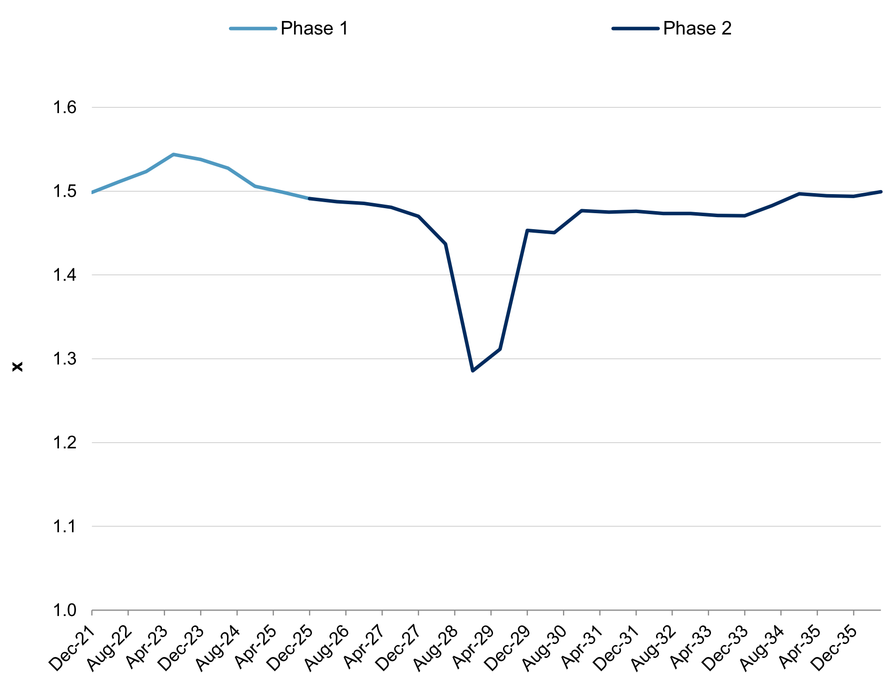
- Give back money to CNMC: All plants are at the moment remunerated at 7.398% by the CNMC. Plants that will be remunerated at 7.09% will need to compensate their over-remuneration once the rate of return is confirmed. We incorporate in our analysis that Sonnedix Finance will have to return to the CNMC the €450,000 received in excess as of December 2020 project company estimate.
- Generation: Electricity production volume exceeding 90% when assessed statistically over a one-year period.
- Degradation: 1% for silicon modules and 1.25% for thin-film modules per year, in light of the corrective module replacement program that is still pending to be completed.
- Availability: 98.5% for silicon modules and thin-film cadmium telluride (CdTe) technology; 95% for thin-film amorphous silicon technology.
- Rooftop capacity (3.4% of installed capacity): Excluded as the buildings where the rooftops are located are maintained by entities outside the scope of the projects.
- O&M expenses: In line with the contract price of €42,000 per MW per year.
- Cost of replacing inverters: Total cost of €4 million distributed from 2024 to 2033 to replace the inverters not covered by the O&M contract and should replacements in a given year be higher than the maximum amount covered per year.
- Module replacement: Replacement of 0.5% of modules per year, considering a replacement cost of €0.40 per peak power for all PV plants.
- Inflation: 1.56% in 2021; 1.3% in 2022; 1.4% in 2023; 1.47% in 2024, 1.85% from 2025 to 2029, and 1.91% thereafter.
- Promissory security associated stamp duty costs included in the metrics.

Key metrics

- We expect a minimum ADSCR of 1.49x (in December 2025) and an average of 1.52x from 2021 to 2025. During this period, we assume no material market risk and therefore our operations phase business assessment (OPBA) is '2'.
- We expect minimum ADSCR of 1.29x (in December 2028) and an average of 1.46x from 2026 to 2036. During this period the project is exposed to market risk on account of a potential change in the reasonable rate of return. We reflect such risk in a higher OPBA of '3' during such period.
- The preliminary operations phase stand-alone credit profile (SACP) is derived from the weakest combination between the OPBA and the minimum ADSCR, which takes place in the second phase, from 2026 to 2036. We assess the preliminary operations phase SACP at 'bbb'.

Chart 1

S&P Global Ratings' Base-Case ADSCR



DSCR--Debt service coverage ratio. Source: S&P Global Ratings.

Downside Case

Assumptions

- Reasonable rate of return: 7.09% until December 2025, 5.58% thereafter.
- Give back money to CNMC: Same as base case.

Generation: Electricity production volume exceeding 99% when assessed statistically over a one-year period.

- Degradation: 1.25% for silicon modules and 1.56% for thin-film modules per year.
- Availability: 92.5% for silicon modules and thin-film cadmium telluride (CdTe) technology; 89% for thin-film amorphous silicon technology.
- Rooftop capacity: Same as base case.
- O&M expenses: Same as base case.
- Cost of replacing inverters: Total cost of €4.5 million distributed from 2024 to 2033.

- Module replacement: Same as base case.
- Inflation: Base case+1% during first 5 years, then as base case.
- Promissory security associated stamp duty costs included in the metrics.
- Operating expenses (except land rental, O&M and energy tax): Base case +5%.

Key metrics

- The strong performance of the project under our downside scenario in both phases is commensurate with a downside assessment of 'aa'. It is expected that ratios are above 1.2x in most of the cases. As a result, we apply a two-notch positive adjustment in the second phase to the preliminary operations phase SACP, leading to an adjusted preliminary operations phase SACP of 'a-' ahead of counterparty limitations.

Rating Score Snapshot

Operations phase SACP (senior debt)

- OPBA: 2 (from 2021-2025) and 3 (from 2026-2036) (1=best to 12=worst)
- Preliminary SACP: bbb
- Downside impact on preliminary SACP: aa (+2 notches)
- Liquidity: Neutral
- Comparative analysis assessment: None
- Adjusted preliminary operations phase SACP: a-
- Financial counterparty ratings adjustment: bbb+ (CaixaBank S.A.; BBB+/Stable/A-2)
- Operations phase SACP: bbb+

Modifiers (senior debt)

- Parent linkage: Delinked
- Structural protection: Neutral
- Senior debt issue rating: BBB+

Operations phase SACP

- We assess the project as having low operating risk, and we assign an OPBA of '2' between 2021 and 2025 and '3' between 2036 and 2036 (on a scale of '1' [lowest risk] to '12' [highest risk]).
- We view the OPBA of '2' as exceptional for Spanish PV assets. It combines both the benefit of fixed remuneration and a favorable mechanism on its remuneration that mitigates production risk.

- Under our base case, we expect a minimum ADSCR of 1.29x and an average of 1.46x between 2026 and 2036. During this period, the project will be exposed to a review of the reasonable rate of return, which is reflected in a higher OPBA of '3'. The combination of the business and financial profiles of the project during this phase is consistent with a preliminary operations phase SACP of 'bbb'.
- Our downside assessment of 'aa' results in a two-notch uplift to the preliminary operations phase SACP, leading to an adjusted preliminary operations phase SACP of 'a-' in the second phase, ahead of counterparty's limitation.

Revenue Counterparty

- In our view, the final electricity consumers represent the ultimate obligors for the regulated payments. As such, the credit quality of the revenue counterparties does not constrain the rating.

O&M Counterparty

- In our opinion, the project's routine O&M requirements are relatively straightforward and there are suitable alternative operators available if required. We conclude that the ProjectCos would be in the position to replace Sonnedix España Services S.L. (previously Vela Energy S.L.) if required, and therefore we do not deem the operator's creditworthiness as a key rating factor.

Financial counterparties

- CaixaBank S.A. (BBB+/Stable/A-2) acts as the project bank account provider. The bank account provider's issuer credit rating constrains the project's rating on the notes since the replacement language included in the documentation in the event of a downgrade of the counterparty is not consistent with our financial counterparty criteria.

Liquidity

- We consider that the project's liquidity to be commensurate with that of rated peers and we assess it as neutral to the rating.
- The project maintains a six-month, forward-looking, debt service reserve account (DSRA) equivalent to 50% of the following two semiannual payments.
- The project also benefits from maintenance reserve accounts (MRAs) to fund replacement of inverters, replacement of thin film modules, and corrective actions taken on the defects identified on some modules. In addition, any underspent in yearly corrective maintenance is trapped in a maintenance reserve account up to a cap.
- Furthermore, if the DSRA and MRAs are not at the required level, there is no distribution to the subordinated noteholders.
- There is adequate headroom under the financial covenants. The annual backward- and forward-looking DSCR distribution lock-up ratio is set at 1.15x, which is below the ratios calculated under our base-case analysis and under our downside-case analysis.

Related Criteria

- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- Criteria | Corporates | Project Finance: Key Credit Factors For Power Project Financings, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Project Finance Transaction Structure Methodology, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Project Finance Operations Methodology, Sept. 16, 2014
- Criteria | Corporates | Project Finance: Project Finance Framework Methodology, Sept. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Project Finance: Project Finance Construction And Operations Counterparty Methodology, Dec. 20, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed	
Sonnedix Finance S.A.	
Senior Secured	BBB+/Stable