GE Commercial Finance

Project Finance as a Tool for Growth

Whether expanding manufacturing facilities, implementing new processing capabilities, or leveraging existing assets in new markets, innovative financing is often at the core of long-term projects to transform a company's operations. Akin to the underlying corporate transformation, the challenge with innovative financial structures such as project finance is that the investment is made upfront while the anticipated benefits of the initiative are realized years later. Experts from GE Commercial Finance and the University of Pennsylvania's Wharton School of Business note the importance of identifying a lender that can thoroughly understand the underlying changes being implemented by the borrower, and get comfortable with the future cash flows arising from the project.

According to Greg Wicander, senior vice president with GE's Corporate Lending team, "in approaching complex undertakings like project finance, prospective borrowers should identify financing providers that have the necessary knowledge base and resources to understand the underlying project's potential and execute the deal."

He notes that GE relies on three "pillars" of success for complex financing: a broad, deep base of industry knowledge; being able to field teams of finance professionals that have the experience and ability to underwrite a wide range of projects; and a seasoned capital markets team.

"We've seen a rising number of companies that need innovative financing to satisfy their capital needs," adds Wicander. "In a significant number of instances they have viable goals but find that traditional lenders are unable to understand their initiatives."

A Responsive Lender Can Move Beyond Traditional Financing

"Project financing is a specialized form of financing that may offer some cost advantages when very large amounts of capital are involved," says Finance professor Richard J. Herring. He's also director of Wharton's Joseph H. Lauder Institute of Management and International Studies and adds, "It can be tricky to structure, and is usually limited to projects where a good cash flow is anticipated."

"Often, a financing institution that's involved in project financing will build up expertise in certain industries," says Herring. "The lender will take on engineers and others who can analyze each project and determine its viability."

Project finance can be defined as: financing of an industrial (or infrastructure) project with myriad capital needs, usually based on non-recourse or limited recourse structures, where project debt and equity (and potentially leases) used to finance the project are paid back from the cash flow generated by the project, with the project's assets, rights and interests held as collateral. In other words, it's an incredibly flexible and comprehensive financing solution that demands a long-term lending approach not typical in today's marketplace.

imagination at work

GE Commercial Finance

However, the pace of project financing has been rising at a significant rate, according to Reuters' Loan Pricing Corporation, which provides loan market news, data and analytics. In 2004, there was some $1.2 billion of project financing activity in the United States. A year later that number more than tripled to $3.7 billion. While most of these financings related to the energy sector, *industrial* project finance remains the domain of a select few institutions.

Project Finance Delivers North America's Newest Steel Mill - SeverCorr

When steel industry veteran John Correnti teamed with Russia's SeverStal Group to form a partnership called SeverCorr LLC to build a state-of-the-art steel mill in Mississippi, the new company turned to GE to arrange for $440 million in senior secured project financing for the new facility.

GE's experts were attracted to the project for several reasons. Foremost, they were impressed by SeverCorr's management team, led by former Nucor CEO, John Correnti, whose track record of building and operating similar projects was well established. Also important to GE was the financial support provided by SeverStal, which viewed the project as a strategic investment. Moreover, SeverCorr was going to be utilizing the latest mini-mill steel making technology, giving them a cost advantage over traditional, integrated steel producers. For example, while so-called integrated mills use iron ore, coke and limestone to make steel, a mini mill uses recycled scrap metal as the raw material, eliminating a number of costly and time-consuming steps.

Mini mills also produce fewer byproducts and require less space, enhancing their cost efficiencies. SeverCorr's facility will be built on a 1,380-acre site in Columbus Mississippi. It's strategically located near the automobile plants that have been built in the region over the last couple of decades. When it goes on line in the third quarter of 2007, SeverCorr will produce 1.5 million tons of high-quality, flat-rolled steel annually, supplying the southeastern United States—a region that is already a net importer of steel due to demand from automobile and other manufacturers.

Besides capital, GE brought something equally valuable to the table: core competencies in the steel industry, and a proven track record that included previous project financing for Steel Dynamics, another successful steel mill operator.

When it came to SeverCorr, there were some challenges involved in structuring a financing package, even though the steel company had attractive growth prospects. As Steven Thomas, senior vice president with GE's Corporate Lending team explains, "A project financing typically is "wrapped" by an engineering procurement and construction (EPC) contractor who actually handles the construction in a turnkey fashion—committing to a completion date along with a firm price. In this case, given management's extensive experience in building similar projects, SeverCorr is acting as its own EPC contractor, thus saving substantial construction costs."

Going the Distance to do a Deal

"To gain a deeper understanding of the market for mini mills in general, and for SeverCorr in particular,

GE Commercial Finance

GE's Corporate Lending finance team worked closely with engineering consultants," says GE's Thomas. "The financing company's specialists also looked closely at SeverCorr's capital structure, its management, the contacts the company had within the industry, and the broader market for its goods.

SeverCorr was also unique in that it didn't have offtake contracts, or guaranteed buyers, for most of its steel output. But GE saw value in the growing potential of the market and in SeverCorr's positioning. "The team at GE Commercial Finance played an important role in making this a reality," says Correnti. "GE's industry knowledge and complex structuring capabilities differentiated their approach and provided SeverCorr a strong financial foundation."

Borrowers Benefit When a Lender Understands New Business Models

"GE is able to successfully structure project financing and other kinds of debt because we understand the way that enterprises and industries operate, which gives our specialists unique insight into the interplay of debt funding and operations," explains GE's Wicander. "This capability was particularly valuable in the case of SeverCorr, where new technology is being layered on a traditional industry."

For its part, GE brings a history of innovation to each of its engagements—an approach that isn't limited to the steel industry. The lender's financial experts are also active in a wide range of industries where technology is facilitating fundamental change, including retail; transportation; automotive; paper and forest; food, beverage and agriculture; general manufacturing; and construction."

Whenever GE enters into a financial relationship, teams of experts work to gain an understanding of the client's company, and the way it fits into the larger environment.

"Our specialists closely examine key areas such as its management, capital structure, the company's position within its industry, and the broader market in which it operates," says Wicander. "We refer to it as a 'whole-company' approach, and its value is evident in the way we're able to satisfy the capital requirements of many kinds of companies in many different industries. Moreover, our capital market capabilities let us tap into a variety of investors, thus allowing us to create capacity for growth. Ultimately, GE's structuring capabilities, in-depth industry experience and access to capital markets enables GE to offer project finance as one of the tools to help customers grow."

imagination at work