Oil, gas and bond pipelines: the case of Aramco/EIG/BLK

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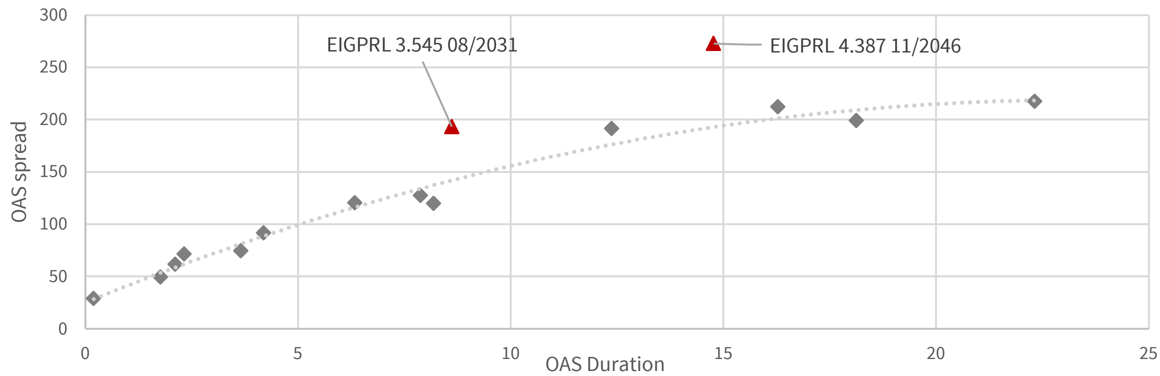
EIG Energy Partners and BlackRock Real Assets' USD+25bn lease-lease-back financing transactions for Saudi Aramco's pipeline networks are starting to test out bond markets for capital to repay bank bridges. The first (EIGPRL) of expectedly quite a few benchmark transaction was met with subdued demand, potentially reflecting a weak public market appetite to provide leverage for private investors in fossil transactions, and/or some queasiness around subordination in practice of transaction bonds versus Aramco's own bonds.

Figure 1. EIGPRL bonds vs the ARAMCO USD curve. Note that the x-axis is on OAS duration rather time to maturity, to better represent the amortizing structure in the EIGPRL bonds. Pricing as of 2 Feb 2022. Source: Bloomberg.



The lease-lease-back transactions is a way to provide ARAMCO with upfront cash to pay dividends to the Kingdom and for direct investors such as EIG and BlackRock Real Assets to get access to long-term fossil infrastructure exposure. The bonds issued in connection with are important in order to provide leverage into the transaction. Thus, the January issuance from EIG for purposes of refinancing the Aramco oil deal is thus an interesting data point to understand how the broader supply of bonds in these transactions could look. **We find that the market prices the new bonds wider/as subordinated to Aramco bonds, even if they are superficially structured as senior secured in the SPV** (details overleaf).

The timing of the announcement of a USD10bn revolving credit facility for Aramco is also interesting ("US$10bn loan refi for Aramco attracts criticism", IFRE, 28 Jan 2021), especially as we are not aware if the bridge financing of the BlackRock gas pipeline lease has gone through yet.[1] Naturally, investors with exposures to banks providing the RCF/bridge should be aware of these quite substantial new loans.

It will be interesting to see the "ESG" treatment of this type of bonds, noting that at least one investor has already put EIGPRL bonds in their ESG fund, as well as the continuing positioning of fossil gas as "green." One technical dimension of this is whether EIGPRL is deemed to be Aramco risk or not, in which case the bond might be excluded from certain investors mandates; example here.

[1] See "Aramco announces $15.5bn landmark gas pipeline deal with global consortium led by BlackRock Real Assets and Hassana Investment Company", Aramco web-page, 6 Dec 2021.

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EIG bond issuance: technical views

The transaction: No less than eleven banks threw their weight behind financing the lease-lease-back transaction of Saudi Aramcos oil pipeline assets. The bond issue by EIG Energy Partners and issuing entity EIG Pearl Holding (EIGPRL) was executed in two tranches: 3.545% 08/2036s (XS2400630005/ US28249NAA90) and 4.837% 11/2046s (XS2400630187/ US28249NAB73). The total issue size was USD2.5bn, reportedly[2] a significant lower amount than intended (USD3.5-4-4bn sought). Given the total EIG deal size of USD12.4bn, this leaves some distance still between the refinancing that the market appears to be willing to provide and the size of the bridge facilities that banks are providing.[3] Use-of-proceeds (UOP) for the bond deal specifically included bridge refinancing beyond the tradition general corporate purpose language. The EIGPRL SPV is registered under Luxembourg law.

Structural features: The bonds are issued in a amortizing and secured format, with the security provided through the SPV that owns the leasing rights to Saudi Arabia's/ARAMCO's oil pipeline network. The SPV is 51% owned by ARAMCO and the the remaining 49% by the EIG led consortium. We are under the impression that any claw-back under the lease agreement, such as seizure of physical assets, will need to be handled under Saudi Arabia jurisdiction as that is where the assets are located. It is hard to conceive a situation where the ARAMCO defaults on other senior lenders but keeps on paying into the EIGPRL structure; it is rather likely the sequencing would be the reverse. Thus, we are of the view that, and the market appears to agree, that the EIGPRL bonds should not be rated at the same level as ARAMCO bonds are. However, the current ratings (A[exp], A1; Fitch/Moody's)[4] are the same for EIGPRL and ARAMCO. The bonds have a dividend stopper: coupons will accumulate but not be paid out in case of a stopping of equity dividends from ARAMCO to the Kingdom.

Valuations: The bonds currently trade at roughly 1.4x spread ratios to the ARAMCO curve (see Figure 1) which likely reflects their effective subordination to ARAMCO risk, as well as the considerable supply pipeline risk. The EIGPRL bonds have, as the start of February, entered the Bloomberg family of bond indices, such as the Global Agg and broad Corporate index.

Pipeline: As indicated, EIG failed to fill intended issuance size, and we would expect the issuer to opportunistically and repeatedly try to fill the gap. Naturally, this puts a dampener on potential upside in the outstanding bonds. Also, further to the EIG transaction, the similar lease-lease-back of the Aramco fossil gas (rather than oil) pipeline network was finalized during COP26 and we would expect that one to start seeking out the bond market in the not too distant future, providing further highly correlated supply. The gas pipeline deal was won by a BlackRock Real Assets consortium – we commented on this earlier in "Arbitraging before the ink has dried", AFII, 11 Nov 2021.

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[2] "EIG Pearl falls short of target in busy bond market", Global Capital, 14 Jan 2022;

[3] For further info on the bridge financing, please see "Operation Private Markets: A Bridge CO2 Far", AFII, 16 Dec 2021. The main bridge USD10.8bn facility was announced in June 2021, under FIGI BBG011MGJ238. Lenders in that facility are (among others, and in alphabetical order): BNP Paribas, Citi, Credit Agricole, HSBC, Intesa, JPM, Mizuho, MUFG, Natixis, SocGen, StanChart and SMBC. The facility is indicated to have a maturity of 1 June, 2022.

[4] The rating reports on the transactions, providing more technical details, Fitch, Moody's.

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