

CMP448 WG11

Agenda

Topics to be discussed

- | | |
|---|---------------------|
| 1. Welcome and Agenda | Chair |
| 2. Action and Query Logs | Chair |
| 3. Legal Text | Proposer/NESO Legal |
| 4. Workgroup Report – First Review | Chair |
| 5. Future Workgroups/Any Other Business | Chair |
| 6. Close | Chair |
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Action and Query Logs

Legal Text Review

Workgroup Report Review

Cost of Financing the PCF Security

Based on a range of security financing rates (6–20%)¹ and financing periods (0.5–5 years)², the PCF security financing costs range from £75/MW to £8500/MW.

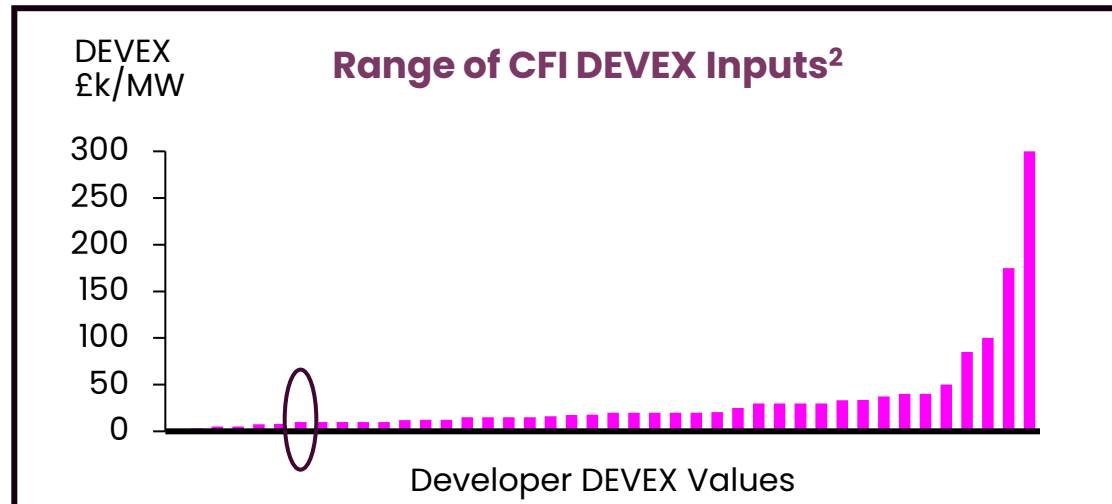
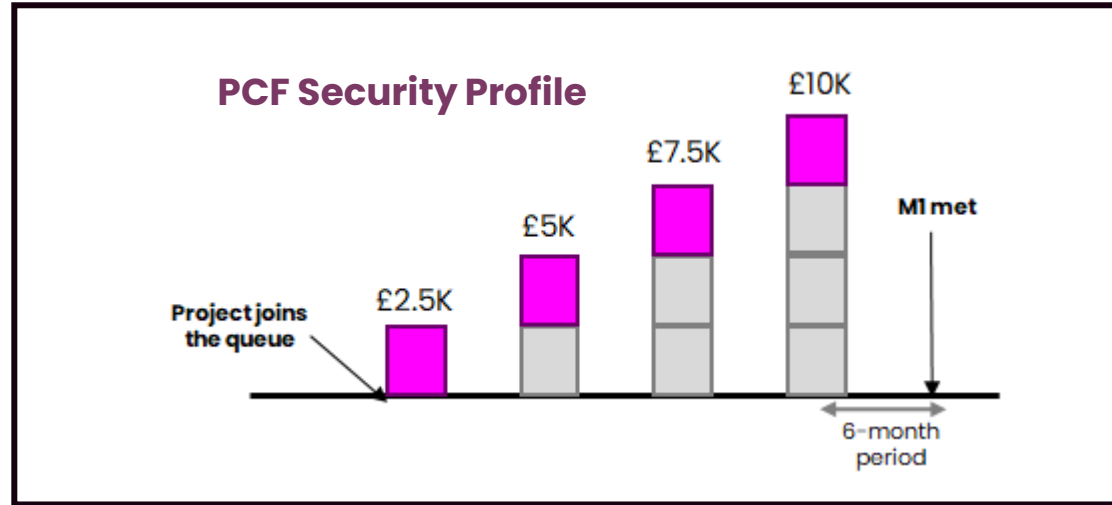
| Key | Financing Cost (£/MW) | | Security Financing Rate (%) | | | | | | | | | | | | | | |
|-----------------------|--------------------------|------|-----------------------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| | | | 6% | 7% | 8% | 9% | 10% | 11% | 12% | 13% | 14% | 15% | 16% | 17% | 18% | 19% | 20% |
| Original Estimate | Financing Period (Years) | 0.5 | 75 | 88 | 100 | 113 | 125 | 138 | 150 | 163 | 175 | 188 | 200 | 213 | 225 | 238 | 250 |
| | | 1.0 | 225 | 263 | 300 | 338 | 375 | 413 | 450 | 488 | 525 | 563 | 600 | 638 | 675 | 713 | 750 |
| Lower Financing Cost | | 1.5 | 450 | 525 | 600 | 675 | 750 | 825 | 900 | 975 | 1050 | 1125 | 1200 | 1275 | 1350 | 1425 | 1500 |
| Higher Financing Cost | | 2.0 | 750 | 875 | 1000 | 1125 | 1250 | 1375 | 1500 | 1625 | 1750 | 1875 | 2000 | 2125 | 2250 | 2375 | 2500 |
| 2.5 | | 1050 | 1225 | 1400 | 1575 | 1750 | 1925 | 2100 | 2275 | 2450 | 2625 | 2800 | 2975 | 3150 | 3325 | 3500 | |
| 3.0 | | 1350 | 1575 | 1800 | 2025 | 2250 | 2475 | 2700 | 2925 | 3150 | 3375 | 3600 | 3825 | 4050 | 4275 | 4500 | |
| 3.5 | | 1650 | 1925 | 2200 | 2475 | 2750 | 3025 | 3300 | 3575 | 3850 | 4125 | 4400 | 4675 | 4950 | 5225 | 5500 | |
| 4.0 | | 1950 | 2275 | 2600 | 2925 | 3250 | 3575 | 3900 | 4225 | 4550 | 4875 | 5200 | 5525 | 5850 | 6175 | 6500 | |
| 4.5 | | 2250 | 2625 | 3000 | 3375 | 3750 | 4125 | 4500 | 4875 | 5250 | 5625 | 6000 | 6375 | 6750 | 7125 | 7500 | |
| | | 5.0 | 2550 | 2975 | 3400 | 3825 | 4250 | 4675 | 5100 | 5525 | 5950 | 6375 | 6800 | 7225 | 7650 | 8075 | 8500 |

The values presented in the above table are intended to provide greater clarity on any potential costs associated with financing the PCF security based on the specific financing arrangements and timelines relevant to a project in scope of the PCF.

Notes:

- Most of the CFI responses that quoted overall cost of capital ranged from 7% to 13%, excluding outliers; we chose an expanded range of security financing rates up to 20% as requested by workgroup members
- The financing period ranges from 0.5 – 5 years, representing an expanded range as requested by workgroup members

Illustrative PCF Financing Scenario



Scenario to illustrate the cost of financing the PCF, including as a proportion of project DEVEX

Scenario assumptions:

- Security Financing Rate¹:** 8% per annum
- Financing Period:** 24 months from joining the Gate 2 queue to passing Milestone M1.
- DEVEX²:** CFI responses reported a significant range for DEVEX. We selected £10k/MW.

With these assumptions, the estimated additional cost of financing the PCF is **£1000/MW or 10% of DEVEX**.

NESO's previous proposal for the PCF, (i.e., £20k/MW before Milestone M7), would have an estimated cost of £6,400/MW (assuming 4 years in queue before M7 and an 8% financing rate).

Notes:

- Most of the CFI responses that quoted overall cost of capital ranged from 7% to 13%, excluding outliers. We believe financing costs for acceptable securities would be based on cost of debt, and thus 8% is a conservative estimate.
- CFI DEVEX estimates for Batteries, Solar, Onshore Wind and Offshore Wind.

Option Valuation Results and PCF Value

Valuation Assumptions

- Suppose a project's **discounted operating cashflows are 98% of the discounted pre-commissioning costs.**
- Additional **DEVEX is paused.**
- Suppose that these operating cashflows and pre-commissioning costs can **change over 6 months** so that the change in the project's NPV **is normally distributed with mean of 0 and standard deviation of 3%.**
- The project will continue if discounted operating cashflows are > 100% discounted pre-commissioning costs after 6 months, and it will be abandoned otherwise.
- Suppose the project's **remaining required pre-commissioning costs (DEVEX and CAPEX) are £500,000/MW.**
- For the avoidance of doubt, **no cost of financing the PCFS** has been included in the methodology to determine the PCF value

Valuation Results

- Applying a financial option pricing methodology, **the value of the "option to delay" is £0.0044 per pound of pre-commissioning costs.**
- On a per MW basis, **the value of the "option to delay" is £2,218.65/MW.**
- A PCF with a value of **£2,500/MW per 6 months** is sufficient to incentivise the developer to abandon this project without a delay.