African Power Deal of the Year 2008

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Rabai Power: Unruffled

For a project that had to survive political unrest, challenges to its contract and the credit crunch, Rabai's financing package came through the last two years relatively intact. Sponsors of power projects in emerging markets still enjoy a surplus of debt providers looking for suitable projects. Those behind Rabai, however, exploited this overhang in the most effective and efficient way possible.

The lead sponsors of Rabai are Aldwych International, an emerging markets power specialist in which FMO and several development funds are shareholders, with 34.5%, and Mitsui-owned Burmeister & Wain Scandinavian Contractor, a Denmark-based specialist turnkey contractor for diesel power plants (25.5%). FMO came in alongside Aldwych for another 20%, while Danish development supplemented BWSC's equity with an additional 20%.

The last two were not involved with the initial bid for the project, which was submitted in 2005, was called Embakasi, and was located near Nairobi airport. The offtaker and awarding authority, Kenya Power and Lighting Corporation, then moved the project to Rabai, near Mombasa, and retendered the project in 2006. Aldwych and BWCS, which won the first tender, also won the second, although not in a clear enough fashion to avoid a legal challenge.

Following the 30 November 2006 award of the project as the lowest cost technically compliant bidder, the lowest-cost technically non-compliant bidder, Simba, challenged the award at the Public Procurement Complaints, Review and Appeals Board, which heard the complaint on 18 January 2007 and dismissed it four days later. Simba took its challenge to the country's High Court, withdrawing it on 5 October, ten days before its hearing.

Two months later, Kenya held a general election, and the disputed poll for president led to a massive outbreak of political violence. It was only in May 2008 that the sponsors set about bringing together a bank group to fund the plant. They held a funding competition at this time, which essentially pitted the International Finance Corporation and a handful of commercial lenders against a group of development banks and emerging markets infrastructure funds.

The second group came out on top and included DEG, Proparco, European Financing Partners, FMO, and the Emerging Africa Infrastructure Fund (EAIF), the last two of which are Aldwych shareholders, but stress they competed for the mandate vigorously. Development banks are shielded from the uncertainties of the interbank market, because they typically enjoy high ratings and/or cheap funding as a result of their state ownership.

The senior lenders are providing a Eu79 million 15-year senior loan priced at 350bp over Libor, equivalent to 70% of the project's Eu113 million cost. Because lenders were not comfortable providing higher levels of gearing, Proparco and the EIF proposed to provide, and the sponsors accepted, a Eu5.6 million mezzanine loan at 750bp over Libor. Sponsor equity accounts for the remaining 25% of the project's cost. Such margins no would longer seem high even for power projects in the US, but the lenders held their margins from May through to close on 8 October 2008.

The sponsor group took several steps to keep the project moving forward as the project wended its way towards close. BWSC executed its contract for the project's five Wartsila 18V46 generator sets, as well as a 6.5MW steam turbine generator even before financial close, rather than lose its slot. FMO temporarily took its stake up to 37.7% so that all the sponsor equity was in at close, but subsequently sold down its stake again. The project is set for final completion in 2010, after which it will sell power to KPLC under a 20-year build-own-operate-transfer concession.

The country's bout of political instability aside, Kenya is still experiencing strong growth in demand for power, though from a very low base. The 90MW Rabai plant will run on bunker oil, which will be imported into Mombasa, and is a staple of the country's generation sector, although Kenya does benefit from some geothermal and hydro capacity. In time, the sponsors hope to run the project using gas located offshore, though this prospect is still distant.

Lender reassurance comes in part from a projected 1.6x debt service coverage ratio, and partly from a comfort letter from the Kenyan government, a necessary measure to bolster investor support in the wake of the early 2008 violence. Kenya enjoys a good reputation among developers, as a result of its moves to deregulate its power sector and the strong performance of projects such as Tsavo, which closed a financing in 2000.

At the same time, as the overlapping groups of debt, mezzanine and equity providers indicates, the African power market is a cosy one. The FMO, in particular, stands out for its ability to operate in several parts of the project's capital structure, as does the Frontier Markets-managed Emerging Africa Infrastructure Fund. A large number of Rabai's supporters operate in support of policy goals divorced from market conditions, a fortunate state of affairs for Rabai, if little comfort to its peers in other markets.

But other countries in Africa are likely to benefit from the attentions of this insular group of development lenders. Several West African states are looking to increase generation capacity in advance of local oil and gas finds or the arrival of the West Africa Gas Pipeline from Nigeria. Nigeria has probably the strongest slate of power projects in development, although here a strong domestic market will provide healthy competition.

Rabai Power Ltd
Status: Closed 8 October
Size: Eu113 million
Location: Kenya
Description: 90MW greenfield independent power project
Sponsors: Aldwych International (34.5%); Burmeister & Wain Scandinavian Contractor (25.5%); FMO (20%); IFU (20%)
Lenders: DEG; Proparco; FMO; Emerging Africa Infrastructure Fund (EAIF); European Financing Partners
Financial adviser to EAIF: Frontier Markets Fund Managers
Sponsor legal counsel: Trinity International (international), Kaplan & Stratton (local)
Lender legal counsel: Allen & Overy (international), Anjarwalla & Khanna (local)
Independent engineer: PB Power
Environmental consultant: Coastal Environment Group
Insurance advisers: Aon (sponsors), Marsh (lenders)