Begin the big in

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The financing trends backing the liberalization of the Italian generation market have turned full circle. Following the EU regulation on energy market deregulation, the Bersani Decree (79/99) imposed a maximum 50% market share on state incumbent Enel. Enel met its obligations through the sale of 15,000MW capacity carved into three generation companies (gencos): Eurogen, Elettrogen and Interpower.

In the years following enactment of the Bersani decree financiers were kept busy chasing mandates and arranging deals for the smaller players behind a steady stream of CCGTs. The deals waiting in the wings were many but the fact that this promise did not materialise into a glut of built plants was largely due to Italy's cumbersome permitting and authorization procedures. The years between 2001 to 2006 were characterized by many single CCGT financings punctuated occasionally by the large corporate style refinancings of the genco's portfolios.

While much of the talk during the IPP boom (if one can call three or four financings a year a boom) was the migration from the old and hospitable CIP6 tariff regime and of the particular merits of a tolling versus merchant deals. The issues today are Italy's diminishing energy supply and consolidation among European energy generators – following liberalisation, Italian energy is a market where size equals market strength.

The pinch?

This could have large repercussions for teams of project financiers – unless their bank has good corporate relationships with the likes of Enel and Edison they could find deal flow drying-up and their involvement limited to participation during syndication.

"The margins and terms show just how competitive the market's become and some banks will almost certainly start to feel the pinch", says one banker. The big players in the Italian market – Enel, Endesa, Edison and Eletrabel – do all their deals on a corporate basis. While deal flow by volume may actually increase, by number it will almost certainly go down. It will also be much more corporate than non-recourse – so it may give some banks an excuse to rationalise their project teams.

The current market is dominated by refinancings – a symptom of the vast liquidity in the bank debt market. Eurogen, the 7,000MW portfolio genco carved out of incumbent ENEL, has refinanced its debt twice in the past three years. The latest $2.3 billion deal signed in February – lead arranged by Barclays, Banca Intesa, BNP Paribas, Calyon, Commerzbank, Mediobanca, MCC, SG, Unicredit and WestLB – and takes out the original refinancing package put together in September 2003. The latest deal is not a refinancing in the proper sense of the word because no new money went through credit, rather the existing banks agreed to amendments in the existing documentation.

The first Eu2.3 billion deal refinanced Eu3.8 billion in acquisition debt. The portfolio's support consists of tolling agreements that initially covered 6,000MW of capacity, which will rise to 8,000MW over an eight-year period as new plants come on line. As an indication of how much the bank market has warmed, the first deal had margins that stepped up incrementally from 150bp over Euribor to 195bp, while the second refinancing starts at 75bp.

Next year bankers are predicting more of the same. The third genco, Tirreno, is a likely candidate for a refinancing. The

Tirreno Power (formerly Interpower) financing was the first for a merchant portfolio in Italy. The Eu1.9 billion in debt signed in January 2003 with the seven-year debt priced at 125bp over Euribor years one to two, 130bp years three to four, 140bp years five to six, and 170bp thereafter.

And the ISAB and Sarlux deals are expected to come to market again. ISAB is a 512MW IGCC (Integrated Gasification Combined Cycle) power plant in Priolo, Sicily, 51% owned by ERG Petroli, and 49% by the Mitsui/International Power joint venture IPM Eagle. The 548MW Sarlux IGCC is sponsored by Saras (and formerly Enron) and is located at Sarroc. Both deals benefit from the legacy of the CIP6 regime, and will be about Eu1 billion each when they come to market.

Similarly, in the renewals sector, Irish power company Trinergy has mandated Royal Bank of Scotland as sole lead arranger on its Project S scheme – the refinancing of existing debt and raising of additional credit for its wind portfolio in Italy and Germany.

Trinergy, with financial and legal advice from RBC Capital Markets and Allen & Overy respectively is looking to raise around Eu1.13 billion for its 648MW of wind projects. The deal will consolidate a number of Trinergy facilities – notably those from its takeover of wind farm developer IVPC earlier this year – into one package: IVPC had three project financings in place when it was bought – those for the IVPC4, IVPC6 and IVPC2000 projects.

Greenfield development?

An overarching issue is whether there will be many more greenfield power financings in Italy in the future. One Italian financier says, "The earthquake about the shortage of Italian capacity seems to have subsided. Given the European-wide drive to consolidation, generation is more than ever a big-player game. And the big players in the Italian market – ENEL, Endesa, Edison and Eletrabel – do all their deals on a corporate basis."

That said, Endesa is looking to seriously add to its output in Sardinia where it has 1060MW of capacity most of which comes from the 1,040MW Fiume Santo plant. Endesa has put forward proposals for a number of new Sardinian plants. In a meeting with the Sardinian regional president in July the two sides outlined a number of energy schemes on which they will co-operate including an initiative to build a 400MW coal-fired power plant next to a new wind farm.

But overall development has slowed and there are unlikely to be too many more tolling-agreement based CCGT deals in the next two years because of the difficulty of obtaining clean sites for easy permitting and also because the dominant players have already positioned themselves. Also, the scope for a developer to build an IPP and sell it on is diminished when the incumbent ENEL and the gencos follow through on their plan for repowering, thereby increasing Italy's reserve capacity.

The last CCGT financing to close was Rizziconi in February. Sponsored by EGL, the 800MW project is backed by a long term tolling agreement and had no trouble finding takers for its Eu455 million of project debt: The 20 year debt pays 110bp during construction, scheduled to take around 2.5 years, then falls to 100bp until five years of operation. The rate rises to 120bp until 10 years of operation, and tops out at 140bp. The deal has an average debt service cover ratio of 1.3x and 2.5 year tail on its tolling agreement.

The deal pricing reflected the tolling agreement, but the terms on the deal reflected how far sponsors of Italian power projects have pushed the envelope. What is particularly interesting about the deal is its amortization profile – most of the repayment is back-ended to the last few years of the lifetime of the debt when a cash-feed mechanism kicks in. Such cash feed mechanisms or dividend locks are usually found at the beginning of a repayment schedule when equity is more likely to be squeezed. In the Rizziconi deal banks were not only being asked to lend for longer, but also being asked to defer the bulk of repayment over a longer period.

Waste-to-energy

The waste to energy sector – expected to pick up substantially – is also proving slow to deliver. The Eu1.4 billion Siciliaenergia 150MW waste to energy project sponsored by Falck subsidiary Actelios launched to syndication in June and is expected to close before year-end.

The project involves construction of three incinerators and operating them under a 20-year concession. Together the plants will produce 150MW of electricity, which will be purchased by GRTN at twice the normal power tariff for the first eight years of the PPA (in Italy, incineration is classified as a renewable energy and hence subsidised under the old CIP6 tariff scheme).

Underwritten in December 2005 by Banca Intesa, Royal Bank of Scotland, UniCredit Infrastructura and Cassa di Depositi e Prestiti, the deal features Eu1.18 billion in debt split between a Eu935 million senior tranmche, a Eu40 million VAT facility and a Eu37 million standby facility.

The financing uses three separate SPVs – Palermo Energia Ambiente, Tifeo Energia Ambiente and Platani Energia Ambiente – ensuring that the debt for each project is ring-fenced. However, if one of the plants were to run into financial or operational difficulty, there are cross-default clauses and one of the other SPVs would take over the poor performing plant's operations.

Tenor on the debt is 15 years debt leaving a five-year tail on a 20-year power CIP6 purchase agreement (PPA) with Italian parastatal grid operator GRTN. The debt is priced at 140bp during the three-year construction after which it drops to 127.5bp before rising over the term to 140bpo again.