

Novatrans: Terna to the IDB

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Brazil's electricity sector has been going through a quiet rehabilitation. While the odd generation financing such as Termopernambuco, or the recently approved Campos Novos deal, may be a sign of better days to come, the transmission sector is already experiencing heavy investment. The Novatrans financing, the first use of dollar debt for a wires deal, means that international lenders and sponsors should take notice.

Novatrans is a 1,278km, 1,200MW transmission line in three sections linking a substation in Maranhao state to one in Brasilia. It is one of a number of private concessions for transmission capacity that have been awarded since 1999. The concession was bid out in August 2000, awarded on 18 October that year, and began 20 December.

The winner was Argentinean engineering group Socma, but that country's financial troubles led to Enelpower of Italy taking over. Enelpower is still the EPC contractor for the project, but the owner and operator is its 50% subsidiary Terna, the owner of 94.3% of Italy's transmission grid.

The transmission lines have been a lucrative source of revenue for such players as Abengoas, Isolux and Dragados. As much less complicated assets than power plants, they are attractive to pure civil engineering groups, which make most of their money by having plants operational as fast as possible. The earlier into a concession that an owner can operate the lines, the earlier it receives payments.

The payment regime is calculated according to the government's estimate of the cost of a given transmission line, as well as how much it will depreciate over the life of the concession, typically, and in this case, for 30 years. The bidding process is governed by how great a discount to the government's estimate the bidder can offer. This in turn is governed by the bidder's internal rate of return requirements and project management skills.

There is nevertheless, a stringent penalty regime for operators if any sections of their system are unavailable, force majeure provisions notwithstanding. The payments are therefore independent of the electrons moved through the line, and are even independent of the capacity of the government to pay. While the regulator ANEEL assesses the charges, these are levied upon all distribution companies, and they are liable for the transmission charges. Thus, the credit behind the project, while regulated, is not sovereign, and not on Brazil's balance sheet.

This line is separated into three sections:

- 1) Samambaia-Serra da Mesa (250km, online June 2003),
- 2) Serra da Mesa-Gurupi and Gurupi-Miracema (each 255km, and online November 2003),
- 3) Miracema-Colinas (180km, operational in April 2004) and Cilinas-Imperatriz (340km, also April).

This constitutes the only high-voltage north-south connector, although it runs alongside an existing line, so that rights of way are already largely cleared. Only on the last section was there a significant delay, and ANEEL has authorised a corresponding extension.

Most of the concessions to be financed thus far have used the Banco Nacional de Desenvolvimento Econômico e Social,

or BNDES, Brazil's development bank. BNDES has the advantage of offering long-term funding in Reais, in which tariffs are denominated. It has also been an experienced financing partner for Brazil's infrastructure development.

The main downsides are that BNDES' processes can be slow, and that it cannot share documentation with other lenders. Another, potentially grave, handicap is that 20% of the cost of BNDES debt reflects the high margin that BNDES pays to borrow on the international capital markets. For a properly structured financing, therefore, accessing dollar debt at a more reasonable rate can be economical.

The sponsors were able to persuade BNDES that it would lend R550 million of the total R1.2 billion (\$403 million) project cost. And BNDES agreed to only charge the project the 80% of the rate, that tracks the Brazilian interbank rate. The remainder they would borrow from the Inter-American Development Bank (IDB), using an A/B loan structure.

This breaks down into an A-loan of up to \$30 million and B-loan of up to \$36 million - the latter of which comes from BBVA. Before disbursement, the sponsors have been looking to bring SG in as a provider, although at press time this was not confirmed. The A loan has a 12-year tenor, while the B is one year shorter. The pricing on the A loan is between 312bp and 507bp over Libor over the life of the loan, while that on the B portion is between 200bp and 525bp.

The totals will likely be lower than the full amounts approved by the IDB, since devaluation since October 2003, when the loan was approved, will decrease the size of these funds. The arrangers are also understood to be looking at raising a currency hedge for their participations.

BNDES' R500 million will also have a commercial element - while R430 million is from its own books, a further R119 million will be lent through ABN Amro and ItauBBA. The two banks, while not providing the funds, will take on project risk. Since the line is now operational, this largely consists of regulatory risk - that transmission owners will be adequately compensated.

The potential of the transmission market is huge, since a country as large as Brazil with such a dependence on hydro needs robust transmission capacity. Different parts of Brazil can suffer from droughts while others have plentiful rainfall. And there a number of further transmission projects up for bid - 11 in total. Market observers expect that two or three of these may require dollar debt.

The biggest worry for investor-owned sponsors is whether they will be able to win any further concessions. President Luiz Inacio Lula da Silva's government let the private sector's involvement in transmission project's stand, but allowed the subsidiaries of state-owned companies to bid. These companies, once candidates for privatization, bid discounts to the government's valuation that few felt to be economic - on average 38%. Signs are that these discounts are not sustainable, but September's round of bids will see how long the state-owned players' nerve will last.

Novatrans

Status: closed August 2004, set to disburse shortly

Size: R1.2 billion (\$403 million)

Location: Brasilia to Maranhao, Brazil

Description: 1,278km transmission line.

Sponsor: Terna

Debt: R750 million

Providers: BNDES, IDB, ABN Amro, ItauBBA, BBVA, SG (provisionally)

IDB loan tenor: A - 12 years; B - 11 years

Technical consultant: Mott McDonald

Insurance: Willis

Environment: Sargent & Lundy

Lenders' legal: Latham & Watkins

Sponsor's legal: Allen & Overy

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