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Termopernambuco

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Latin Private Power Deal of the Year 2002

Termopernambuco

The first thermal limited recourse project in Brazil's thermoelectricity priority programme (PPT) in which both the equity and the offtaker are 100% private (or more pertinently not Petrobras-owned) ? the $410.5 million Termopernambuco power plant financing closed on 19 June 2002.

The deal, the second to close last year after the Petrobras and ABB-led Termobahia transaction, is both a measure of growing Brazilian power sophistication and a further signal that Brazil is serious about the PPT.

Termopernambuco is a 520MW combined-cycle gas-fired plant located at the port of Suape, municipality of Ipojuca, in Pernambuco State. Lead sponsor and plant operator is Spain's Iberdrola, which invests through the Guaraniana consortium alongside BB Banco de Investimento S.A.of Brazil, Previ of Brazil and Brazilian private pension funds.

EPC contractors on the plant are Brazilian construction and engineering companies Construtora Norberto Odebrecht, Promon Engenharia and Inepar S.A. Indústria e Construcoes with General Electric supplying equipment and future maintenance. The plant is expected to enter into commercial operation by 31 December 2003.

The financing package for the plant consists of $202.4 million from the Inter-American development Bank, $88 million from the Banco Nacional de Desenvolvimento Econômico e Social (BNDES) and $125 million in sponsor equity. The BNDES portion takes the form of sub-debt. $42.4 million of the IDB's portion comes directly from its books as an A loan.

The B loan of $160 million was led by SG and BBVA and syndicated at the end of June, coming in close to target. Given that at the time of syndication government 8-year bonds were trading at a spread of 1700bp, with expressions of interest from 30-40 institutions it was a strong sale.

The deal has a tenor of 11.5 years for the B loan, and pricing of 325bp over libor during construction, 362.5bp in year one, 375bp in year two, 400bp in year three, 450bp in years 4-7, and 500bp for the remainder of the loan's life. Participants were Caja Madrid, BNL, Transamerica Finance, Banesto, Fortis and CIFI.

Termopernambuco was one of the 56 plants that were designated by the Brazilian government as necessary to avoid future shortages in 2000. These shortages duly appeared in 2001, spurred by a nationwide drought and an over reliance on hydro-electric development. Nevertheless hydro financings ? Cana Brava and Dona Francisca for example ? have paved the way for the acceptance of non-recourse structures and dollar debt repayments by regulators.

The most concrete advance prior to Termopernambuco was Termobahia ? a 190MW plant financed through a $188 million Inter-American Development Bank A/B Loan. However, Termobahia had Petrobras as both the offtaker and fuel supplier, and therefore required much less robust risk allocation processes.

Termopernambuco sells direct to distribution companies, and consequently falls even more fully within the pricing remit of Brazil's energy regulators. However, the 20 year power purchase agreements (PPAs) and supply arrangements are not entirely independent of the sponsors ? Guaraniana owns the two distributors, Companhia Energética de Pernambuco (CELPE) and Companhia de Eletricidade da Bahia (COELBA) that are set to take the plant's output. The idea behind this aligning of interests is to increase comfort levels for lenders, but also so that the sponsor can hedge the outcomes of regulatory or market conditions.

Nevertheless, the offtake strategy does not remove all of the risks inherent in selling power into the Brazilian market. Brazil has plentiful hydro-electric power, and has wanted for several years to diversify away from its dependence on this source, but has found it hard to come up with a market structure that would encourage thermal generation. At issue is the ability to index tariffs under power purchase agreements in such a way that lenders and sponsors are protected against the slide in the Real.

The first effort by the Brazilian regulator, ANEEL, was the creation of a Valor Normativo (VN) formula, which would be adjusted on a periodic basis to ensure that Real revenues would remain sufficient to cover dollar-denominated payments to lenders. The initial complaint from sponsors was that the review of the VN formula was not frequent enough to protect from sudden plunges in the Real's value.

The frequency of the review, now quarterly, has been settled. Equally important, however, is the ability of the offtaker to pass on costs. This has been made the responsibility of the distribution companies. In this case the utilities buying the power are also Guaraniana affiliates, so the ultimate owners end up protected from any shift in the market framework towards either side.

The station is not supplied directly from Petrobras, but instead uses an intermediary ? Copergas ? under a mirror fuel supply agreement. The mirror agreement is designed so that the two sets of contracts, between Petrobras and Copergas and between Copergas and Termopernambuco, replicate each other's terms.

Negotiation of Termopernambuco took place amidst the uncertainties and risks associated with the evolving and incipient nature of Brazil's electricity sector's regulatory framework and a general Latin financial crisis. The deal had to be structured to mitigate tariff indexation risk (in PPAs); risk of increased costs; plant unavailability and Real devaluation risk. That the deal closed successfully, and $119 million has been drawn down to date, is a measure of the developing structural sophistication and level of confidence in Brazilian power.

Termopernambuco

Status: Closed 19 June 2002

Location: Pernambuco state, Brazil

Total project cost: $410.5 million

Description: 520MW CCGT plant

Sponsors: Iberdrola; BB Banco de Investimento; Previ

A/B loan provider: IDB

B loan arrangers: SG, BBVA

Participants: Caja Madrid; BNL; Transamerica Finance; Banesto; Fortis; CIFI

EPC: Construtora Norberto Odebrecht; Promon Engenharia; GE; Inepar

Lawyers to the borrower: Gibson Dunn & Crutcher

Lawyers to the lender: White & Case (international), Souza Cescon (local)