Further Americas Deas of the Year

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Latin America ? private power

Termoelectrica del Golfo I and II

The two phases of the TEG project ? strictly speaking the Termoelectrica del Golfo and Termoelectrica Penoles deals ? are an impressive alternative response to the problem of solving Mexico's power needs. Whilst unlikely to provide the entire answer as to how sponsors should structure their projects, TEG I and II have demonstrated a unique and innovative response to the needs of large corporates in the country. Moreover they have opened up a valuable new fuel source alongside gas at a time of rising prices.

The TEG deals' main impetus came from the mineral conglomerate Cemex, one of the most internationally active in Mexico, and amongst the largest cement makers in the world. Cemex has enormous energy needs, and is already a heavy user of Petcoke in its industrial processes. Petcoke is a by-product of the refining process, and state petroleum supplier Pemex has recently embarked on an upgrade programme at its refineries (which include the recent Madero and Cadereyta financings) to enable it to producer lighter crudes.Petcoke is a viable fuel when used in conjunction with the appropriate technology, and Cemex originally planned to service its growing fuel needs in a joint venture with Pemex. However it eventually put out a tender for an independent power producer to develop a power facility to satisfy around two-thirds of its energy needs. Sithe Energies and Alstom were selected to develop a 230MW plant as an inside-the-fence deal. The brief, essentially, was to supply competitive electricity to Cemex for 20 years with a 20-year fuel supply agreement. Cemex has 12 plants dotted around the country, and the plant is dependent on the CFE ?wheeling? (or transporting) the power to its destinations. The way to get lenders comfortable with the credit of the offtaker is to point out that it has a capital markets history. It also has large proportion of dollar-denominated revenues (about half of its Ebitda is in that currency), important since the health and capacity of the Mexican financial sector is belied by upbeat growth figures. TEG Phase I was financed on its own, since although Cemex had an option to buy further quantities of fuel it had no requirement for greater quantities. If an additional offtaker could be found, however, the economies of scale would be significant. The Inter-American Development Bank and Coface were lined up as the primary lenders whilst the sponsors searched for another customer.TEG I's financing breaks down into $73 million equity, $75 million 14-year IDB A loan, $102.3 million 14-year B loan and a $100 million Coface credit. Lead arrangers were Deutsche Bank and ABN Amro, who began the process of syndication in December 1999 and completed it in the second quarter of the year. Alstom carries out the EPC contract on the plant, located at Tamuin, in the state of San Luis Potosi.The second phase had, of necessity, slightly different characteristics, most importantly Penoles, the metals conglomerate, as offtaker. Penoles does not quite have the international capital market form of Cemex, aside from a structured silver revenues-backed note issue of around $100 million. Nevertheless it fits roughly the same criteria as the former. It duly signed a 20-year PPA for a further 230MW. Key to its decision was the need for reliable power since production was often interrupted at peak demand periods, much as it is in California.The key for the sponsors was to transform this extension of demand into a financing plan to meet the deadline of six months from the start of construction of the first phase. This involves substantial savings in manpower, materials and infrastructure, and both sets of lenders were made aware of the potential savings. Financing of the second phase was kept largely separate, although both sets of lenders were made aware of the potential for cross-over from the operations of the other facility.Cemex remains the fuel supplier, and although the sponsors can pass on increases in fuel costs, Penoles is held to its obligations by a put option that parentally covers the power purchases of its various subsidiaries. The finance is secured on a Mexican Business Trust, a relatively common, benign and tax efficient means of replicating the project finance structure, which in turn owns the SPV. Mexican regulations mean that as self-supply entities, offtakers have to hold stakes in power suppliers. The trust is a useful way of balancing ownership and control interests, and is bolstered by offshore account structures that eliminate most of the (minimal) currency risk.A new set of players emerged in the financing since the IDB could not assemble the necessary approvals in the available timeframe. ANZ Investment Bank was appointed as the sponsors' financial advisor, and ABN Amro and Credit Agricole Indosuez were appointed as lead arrangers. ANZ was also subsequently appointed as an arranger. This time Coface remained in the transaction (since both sponsors at the time had substantial ownership), but was joined by the Export Credits Guarantee Department (ECGD).The ECGD's involvement is under its overseas untied investment programme, and recognised that much of the subcontracting, as well as parts of the development team, were based in the UK. Coface covers half of the $239 million with pre-completion political risk insurance (PRI) and post-completion comprehensive guarantee, with the ECGD providing PRI on the remainder. Both tenors stretched to fifteen years door-to-door and equity and sub-debt was a shade higher than the first phase, at $79 million. The use of the template in the future depends to a degree on the continued supply of petcoke to Mexico. Pemex has made noises that it wants to carry out further refinery upgrades, and may even be looking for a generating partner itself. Moreover, whilst the initial capital cost of the circulating fluidised bed technology used here is slightly higher, production of the waste product in places such as the Texas coast is set to rise. Since the government wants to diversify its fuel mix, there is strong potential for a few more plants to come the market's way. One rival developer has suggested that the deals ?are an interesting footnote in the evolution of the Mexican electrical sector?. Perhaps, but they could be a very profitable niche for IPP interlopers in the country's power sector.

Termoelectrica del Golfo

Status: signed (I) 28 April 2000 (II) 26 October 2000Location: Tamuin, San Luis de PotosiSponsors: Sithe Energies, AlstomCapacity: 2 x 230MWFuel: petcoke (waste from Pemex' Cadereyta and Madero refineries) supplied by Cemex for 20 yearsOfftake structure: 20-year PPA with (I) Cemex and (II) Penoles, excess sold on to CFE at marginal cost when not requiredFinancing: (I) $73 million equity, $75 million 14-year IDB A loan, $102.3 million 14-year B loan, $100 million Coface credit. (II) $80 million equity and debt of $239 million, half covered by Coface pre-completion PRI and comprehensive guarantee thereafter, and the remainder covered by ECGD PRI.Lead Arrangers: (I) ABN Amro, Deutsche (II) Credit Agricole Indosuez, ABN AmroFinancial advisor to Cemex: Protego EnergiaFinancial advisor to the sponsors and arranger (II): ANZ Investment BankLawyers to the borrower: Latham & Watkins Lawyers to the Lenders: White & Case

North America ? power project lease

PG&E Turbine Master Trust

As PG&E Corporation struggles to avoid bankruptcy caused by the commitments of its Pacific Gas & Electric subsidiary, the timing of the award could be better. Bankruptcy threats, power cuts and politics have made for great headlines and made media stars of some ratings agency analysts. Their application to the fundamentals of supply and demand in California, and indeed to the future of PG&E's National Energy Group (NEG), are less clear. In all probability this parental credit crunch goes much of the way to explaining why this deal, from one of the industry's cannier sponsors, is such a groundbreaking move.

After all, as an accounting play, the turbine trust deal's headline figure itself has been accused of being somewhat misleading. The $7.8 billion size would win plaudits as the largest project finance deal ever if it did not come more in the form of commitments that satisfy accounting regulations. Still, if a company wants to keep assets from ever touching its balance sheet (and a bank knows that these are relatively isolated from interference from above), such a figure ? one that includes the total value of all projects for which the secured turbines are intended ? is necessary.The deal is probably not the first turbine synthetic trust to be executed in the US (and the structure may soon have an overseas progeny), but it is the first to be pitched into the bank market. Various project finance heavyweights say they have the ability not only to structure the deals (for a tidy fee), but also to hold them on their balance sheet with few ill effects. Aside from the fact that this depends to a large extent on amenable auditors or a suitable conduit, most of the other deals have not been as large as the NEG's jumbo.The financing has been structured to conform to two rulings from the Emerging Issues Taskforce, which essentially disqualify plants from synthetic treatment should its turbines ever be accounted for on the balance sheet. Synthetic leasing, which for tax purposes keeps assets on balance sheet, but for accounting purposes keeps them off, is a popular earnings management tool. The NEG has carried out a number of synthetics, including the Lake Road and (more recently, see below) La Paloma financings.The turbines to be financed consist of four 7FA and nineteen 7FB turbines procured from GE Power Systems and 21 Mitsubishi MHI501G. Queues for turbines are becoming horrendous ? even the apparently prescient Calpine has included a turbine facility in its recent portfolio deal ? with the potential to seriously snarl-up a fast-track development programme. And the NEG's programme simply waits on sufficient cash to put in as equity, cash which insiders say is already there and safe.SG was the lead arranger on the transaction, building on its experience and involvement in the earlier single plant synthetics. The $7.8 billion breaks down between two vehicles: PG&E Construction Agency Services (CAS) I and II. These are the beneficiaries of two master turbine trusts with two debt tranches (A and B) and two investors (Tranches C1 and C2) each. A and C1 are supported by a capital infusion agreement from PG&E, whilst B and C2 are collateralised by US Treasury notes deposited with a security agent.The first two are revolvers and are sized to meet the entirety of the capital requirements of all projects requiring turbines, in much the same way as the Calpine revolver might. The second two are standby capital facilities, from which development costs can be drawn up to $100 million and subject to conditions precedent. The investor tranches cover the 3% minimum equity required for lease treatment.What has been established is a separate financing vehicle for projects, where those close to market may be refinanced on a standalone basis. Given the time and structuring fees that went into making the vehicle lease friendly, a tax and/or accounting friendly structure is the most likely candidate. The vehicle, and hence the lenders would be repaid on a pro rata basis.The A tranches for Warehouse I (the GE turbines) and Warehouse II totalled $300 million and are backed by a claim on assets and a guarantee from PG&E. The B tranches, backed by the notes total $7.226 billion. These are essentially low risk, low yield backstops, although under certain circumstances, such as condemnation, the banks would have to take the risk. The C tranches come to $234 million and are secured by a second claim on the assets.SG approached institutions on all of these deals, although the B tranches were restricted to company relationship banks or those with balance sheets or acccounting practices best placed to digest them. These were ABN Amro, Commerzbank, Dresdner, Fuji Bank and TD Securities. The A tranches, most likely to be accessed first, saw in addition the presence of Chase Manhattan, BNP Paribas, Credit Lyonnais, ING Capital, BSCH, Citibank, National Australia Bank and Royal Bank of Scotland.The structure has been described as a hybrid mix of project financing and leasing of particular interest to earnings-sensitive investor owned developer/ utilities. A cloud has nevertheless been cast over the deal by the parent's troubles. This may be changing, as legal separation of the NEG continues and ratings agencies begin to assign a separate credit rating. However, the holding company has put over $400 million into the NEG in various forms since its creation as the USGen joint venture with Bechtel. Continued rosy outlooks depend upon either the parent (or, ultimately, another) being capable of injecting sufficient equity to realise projects.PG&E's stock has, understandably, slumped to leave it with a market capitalisation of around $3.9 billion. Resolution of the California crisis is too much of a tangled and changeable process to go into in depth, but it remains worth noting that a buyer for the NEG would not be hard to find ? and CAS would probably survive.

US Power ? single plant

La PalomaIn a market dominated by portfolio acquisitions, turbine warehouses and construction revolvers it is easy to forget that sponsors can continue to surprise when assembling finance for a single plant. PG&E, a name better known for a $7.8 billion warehouse and a parent with cashflow difficulties, concluded the largest ever single plant financing during the hectic March period. The La Paloma plant has a price tag of roughly $730 million and features a combination of a synthetic lease and a portion of its debt placed with a securitized commercial paper conduit. The ease with which the deal, arranged by Citibank, went through suggests that the ?cookie cutter? approach beloved of National Energy Group may be paying off in financing time and cost savings.La Paloma did not, strictly speaking, create the template, and followed the late 1999 Lake Road financing. This $460 million deal confronted the market with a genuinely new financing blend, and was seized upon by market observers that investor-owned utilities could find a way to install new capacity and post the earnings figures that analysts demanded. Since then synthetics have not taken off to the extent that might have been expected, but the recent rash of warehouse deals, whose sole purpose is to continue to make these forms of plant financings attractive, give some idea as to the potential ahead.La Paloma is a 1048MW power plant located 40 miles west of Bakersfield, California, in western Kern County on an industrial site previously used for oil production. At the time of financial close it was destined to become a merchant producer within the state's lucrative electricity market, clearing its power through the California Independent System Operator (CalISO). The plant is fired by natural gas and uses Alstom combined cycle gas turbines. It is slated to enter service in the middle of 2001.PG&E has been assiduous in making the most of tax and accounting efficiencies, partly to extract the best earnings profile from each asset, but also as a way of demonstrating to the lending community that, despite being a utility spin-off, it is as canny a developer as the next. It is prepared to use its balance sheet (in altered form) to support projects, although the mechanics of this may have to change in light of recent events.Perception of the benefits of synthetic leasing is now widespread, especially amongst generators who wish to lower their tax burden whilst at the same time reporting higher earnings to the stock market. The synthetic is an off balance-sheet loan that is styled as an operating lease for accounting purposes (and therefore does not take into account depreciation), but as a financing for tax standards, with PG&E indirectly listed as the owner of the asset. More bluntly, the synthetic is an effective way of exploiting the gap between GAAP accounting standards (those figures presented to the analysts) and those used to report to the IRS.La Paloma is not a pure synthetic lease, since almost half of the financing has been syndicated to the traditional project finance bank market. The $730 million financing includes a $25 million debt service reserve facility, $15 million working capital, $21 million in certificates and a $295 million term loan B tranche. This loan is priced as follows: 137bp for the construction phase, 150bp for the end of the construction through year five, 225bp for years six through ten, 237.5bp for years 11 through maturity. Co-arranger level syndication brought in Deutsche Bank, SG, BNP Paribas, Dresdner Kleinwort Wasserstein and Credit Lyonnais.Lease equity is provided by placing a further $374 million of commercial paper into a Citibank-managed conduit, similar to its CXC trade receivables conduit. This 364-day paper comes cheap, at least in part because the parent, PG&E Corp., backs it. This situation has, apparently, changed, with the PG&E Gen rating of BBB now backing the paper, given its parents effective D status. Citibank's conduit managers will now be ensuring that the proportions of rated debt in CXC are robust enough to maintain its own viability. If the conduit falls through, however, the banks have the funding backstopped. The CP paper takes on the characteristics of a bridge loan, designed to come out at completion. The bank piece syndication went well, even for eleven-year merchant debt. At least one reason was the post-year-seven cash-sweep, a powerful spur to refinancing. For a merchant plant, such clauses are now the norm, even for a favoured client like PG&E. Moreover PG&E's backing for the plant is substantial, and the California siting makes it attractive given the bare fact of capacity shortages in the state, if not in terms of a preponderance of iron-clad offtakers. La Paloma, in addition to being one of the largest single-plant financings ever, and certainly the largest single-plant merchant financing, is one of the earliest merchant plants operating in California. Early indications are that it will be well placed to pick up a number of prime bilateral contracts should the spot market there irretrievably break down. It is an indication of the division between the two units that the one was prepared to get the highest price possible out of its sister utility. Either that or, more cynically, PG&E has discovered a benefit to keeping the unregulated generation business in the same hands as the regulated parts. La Paloma will complete construction in the next quarter of this year, possibly in time for the hot summer that everyone in the state is hunkering down for. The plant is one of several recent approvals that Governor Davis points to as evidence of his commitment to ending the energy crisis. Recent reports suggest that 2000MW of new capacity will come online this year.The cookie-cutter may need to be bent into a slightly more unusual shape in the future, as commercial paper liquidity looks set to become more expensive in the near future. This is because banks may be forced to treat liquidity facilities as a greater charge on their balance sheet, up from zero to a figure nearer 20%. These new Basle Rules, which have yet to become definitive for projects, will be exercising the structural experts at Citibank and the NEG over the coming months. The NEG, sitting on a $7.8 billion turbine facility and 13 planned facilities over the next three years, should now have the breathing space to look into the issue more closely.

North American Power ? hybridCedar Brakes LLC

Cedar Brakes is probably one of the less tangible recipients of an award for project finance, as a refinancing that does not even concern itself with an asset. It carries a guarantee from its parent and essentially consists of a brass plate in Delaware. The El Paso Energy-sponsored deal, however, marks the start of an IPP developer's equivalent of stranded costs ? the liberation of capital to compete in a deregulating market.Cedar Brakes is the first use of the public bond markets to securitize a power purchase agreement (PPA). It means that there is now a public market that can understand the risks associated with captive marketing arms and size up the willingness of utilities to obtain lower rates for its power. Utilities locked into above market PPAs that were struck in the early 1990s (of which there are, according to a deal insider, ?an awful lot?) should take note.The $320 million deal is a recognition of the fact that few of the majors player in the US electricity market can afford to view their plants as standalone assets, and that a cast-iron PPA can be as much a hindrance to sponsors as a tool in gaining finance. El Paso, however, has ambitions that go beyond even becoming a full-service energy provider and into the power finance business.The PPA was agreed between the Newark Bay Cogeneration Company (controlled by El Paso, or EPE) and Public Service Enterprise & Gas, more familiarly known as PSEG. PSEG, after a lengthy court battle, has been given the go-ahead for a securitization of its stranded costs. To gain approval for this move, which monetises government-backed revenue streams from utility customers for uncompetitive assets, PSEG wants to demonstrate its own commitment to becoming leaner to its regulatory overlords.The Newark Bay Cogeneration facility is a 137 MW gas-fired cogeneration plant, which sells power to the aforementioned Public Service Electric & Gas and steam to various local industrial customers. PSEG and ENMEX originally owned it, before the plant was sold to EPE in 1999. The facility is located in a high-value, transmission-limited market in New Jersey, part of the Pennsylvania-New Jersey-Maryland (PJM) regional pool. The area has been a hot development prospect, although various cautious noises have been made about the possibility of overbuild by consul-tants recently.Cedar Brakes is the entity that has taken over responsibility for the power purchase agreement. The securitization pays for the purchase of this agreement from Newark Bay Cogen, and therefore helps to deleverage the asset. Cedar Brakes is owned by El Paso and the Limestone Electron Trust, and off-balance sheet financing vehicle that assists in slimming EPE's tax and earnings profile and forms the core of its ambitious Power Finance Company. The new company has started offering equity, development capital and sub-debt, much of it channelled through here.The ownership structure here has more to do with El Paso retaining operational control but at the same time a diluted equity interest that boosts its earnings per share and reduces its tax liability. EPE has made some commitments with regard to the vehicle, most importantly an unconditional guarantee that it will maintain the SPV's obligations to PSE&G under the restated PPA. This guarantee means that investors need to get comfortable with the ability of the El Paso Merchant Energy Group to find the power to meet this, and (a timely point) in PSE&G's ability to pay up.Credit Suisse First Boston was the financial advisor, underwriter and bookrunner on the $320 million bonds issued in September 2000. The bonds have a 13.5-year maturity and a yield of 8.5%. Moody's Investors Service rated them Baa2, based in part on the PSEG credit of Baa1, but also upon various liquidity reserves and backstops. It is difficult to find any losers from this restatement, unless EPE suffers from a catastrophic increase in gas prices, something that marketers are there to mitigate. The ratepayers of New Jersey will benefit from the deal to the tune of $74 million, and if regulators are beginning to swing back towards the retention of bilateral agreements between producers and utilities this could well become a template.There are a few prerequisites to getting deals of this kind done, including above market PPAs and willing utilities. The structure works well with singly-owned facilities and may cause some conflicts with traditional project finance facility covenants. Certainly CSFB thinks that there is a pool of knowledgeable investors to take up any paper. El Paso alone estimates that 50% of its generating base can be deleveraged this way.

North American Power Portfolio
Calpine Construction Finance II

Calpine does not buy up utilities. Calpine does not develop plants outside the United States. Calpine does not let banks say ?Project Finance? to its face. Having avoided some of the more common pitfalls to have afflicted power sponsors this year, its stock is now more popular than dozens of the Internet shares that have lost more than 90% this year. And Calpine is a voracious user of capital, searching for pockets of liquidity in unlikely places ? preferably with no strings attached.

Calpine stunned the market in 1999 (and picked up a Project Finance Magazine Deal of the Year in the process), with the first Construction Finance revolver. This $1 billion deal exemplified the corporatization of the development financing game like no other. The San Jose-based generator was selling to lenders a hefty dose of faith in its own management's ability and vision. It has so far been able to back up this faith with startling profits and several audacious takeovers and joint ventures. Two of these, a partnership with Panda Energy and the acquisition of SkyGen, spurred the second, much larger revolver announced in the middle of this year.Of course, the days of summer when generators in California could name their price (and were confident of being paid) will have provided a useful earnings boost. 26 plants in Calpine's operating portfolio are located in the state. But, as its management protests, it is now a national player, with 50 plants present in around 15 states. At the end of the current announced generating cycle it will have 50GW under its control, and looks to be one of the few developers who can be taken seriously when they say that they can respond quickly to the Californian shortages.The revolver suits Calpine's purposes, not simply as a means of persuading its so-far amenable lenders to front previously unheard-off cash commitments. The guiding rationale of bringing new projects into the portfolio as and when they are announced means that financing and the large inventories of spares and manpower held by Calpine can be flexibly co-ordinated. It lowers the cost of capital by avoiding leaving resources idle and exploiting economies of scale but at the same time avoids the ratings impact that corporate level funding would bring.The bare details of the deal is that it is a four-year revolving credit, involves $2.5 billion of commitments from banks and a $500 million equity injection from Calpine. Additional equity would be contributed on a pro rata basis, and the loan also includes a now-fashionable turbine financing facility. This last facilitates cashflow, creating a useful backstop to the order book of over 100 turbines it holds with the major suppliers.Calpine takes the risk for project completion, overrun and performance guarantees, rather than tie itself into the comparatively expensive EPC contracts that characterise vanilla project financings. This flexibility within the portfolio also means, however, that individual projects can collateralise each other until taken out of the SPV. Additional plants, of which 30 have been mentioned, conform to the banks' technical committee's specifications. These include the use of gas as a fuel, acceptable technology, US location and geographical diversity within the country. The financing covers 12 projects (with location, capacity and approximate costs): Los Medanos (Pittsburg, CA, 508MW, $406 million), Baytown (TX, 722MW, $332 million), Carville (St Gabriel, LA, 441MW, $287 million), Oneta (Coweta, OK, 954MW, $516 million), Santa Rosa (Milton, FL, 221MW, $154 million), Delta (Pittsburg, CA, 813MW, $535 million), Freestone (TX, 1022MW, 498 million), Channel (TX, 537MW, $344 million), Broad River (Gaffney, SC, 342MW, 150 million), Corpus Christi (TX, 386MW, $279 million), Decatur (AL, 657MW, $320 million) and Morgan (Decatur, AL, 669MW, $326 million).The loan is interest-only, carrying a bullet maturity and therefore a powerful spur to refinancing at the earliest opportunity. The business available to the banks, whether from arranging single-asset bank, lease and bond financings, or from corporate level cash-take outs, will be considerable. In 2000 alone, senior debt issuance has amounted to $877.5 million in convertibles preferred, $1 billion in senior notes and a $400 million corporate revolver. August saw a well-received IPO of $800 million ? the stock has now found favour with US private traders and institutions alike.The project facility also sold well outside of its traditional markets, with European institutions taking a disproportionate slice of the commitments. This suits bookrunners and sponsors alike well, since such participation rarely comes with strings attached and four years is an easy maturity to swallow for long-term lenders. The original CCFCI paid out a margin of 150-212.5 basis points of libor ? if CCFCII pays out anything near this margin and power assets continue to fetch what they have in the US markets, much of the risk taken by lenders lies in refinancing.Past experience suggests that Calpine has been able to weather less power-friendly times and still bring with it a devoted bank following. The lead arrangers, Credit Suisse First Boston and Scotia Capital, are long-standing acolytes who also led the CCFCII deal. Co-arrangers and joint lead underwriters were CIBC, ING (US) Capital, Bank of America, TD Securities, Bayerische Landesbank and Dresdner. CCFCII will have given some of these banks useful nudges up the project finance league tables, but quite a few names will also be bumped up the fixed income and equities tables as a result of their loyalty.The structure that has emerged shows that the construction revolver is now approaching somewhere near maturity. Tellingly, Calpine is currently in talks with CCFCI lenders about grafting some of the developments onto the original revolver's documentation. Moreover, the possibility of buying bankrupt or distressed generating companies (letters of the year: P and E) may force a new giant financing. And the urge to maintain double-digit growth means that Calpine's US confinement will not be indefinite.The only real query (outside the only semantically fruitful ?is it project finance?? argument) is how replicable the deal is for other, possibly more established companies. Building up a development history and having a sufficient size to raise capital is possibly becoming less unique as every other utility spins off its generation interests. The arrangers have made much of ongoing talks with other corporates, but an imitator has yet to emerge. Ratings pressures and a respected management may change this picture.