Turkey: Inkenderun - birth of the BOO

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Late June ushered in the encouraging financial close and signing of Turkey's first Build-Own-Operate (BOO) power deal at Iskenderun. The 1210MW bituminous coal-fired plant is being developed by the German power firm Steag whose 90% stake in the project company, Iskenderun Enerji Uretim ze Ticaret AS (Isken), is subtly complemented by Siemens' stake of 10%.

Of late, the BOO projects have been much vaunted by Turks and international developers alike. ?There has been a change in the Turkish attitude,? argues Marc Gruenewald, Steag's managing director. ?They have realized that they can't match their energy demand domestically. So the desire for foreign investment has increased accordingly. And the BOO projects, with their internationally bankable structures, are the easiest way the fit these needs.?

This, the first completed act of the BOO performance ? a scheme that should see the successful completion of four other projects ? introduces a format that profits from its ample merits.

Primary among these is the highly competitive pricing formula that offers a downward trending tariff profile. In contrast, the Build Own Transfer (BOT) projects betray a different tariff structure which, from the viewpoint of many power markets, is simply insufficiently competitive.

Further, a project that remains in the hands of the operators is, by some accounts, more favorable than, say, one transferred back to the government. Claims Ali Alpacar, Chase's vice-president, Global Investment Banking, in Istanbul: ?From the government's perspective, BOO's have been preferred over BOT's because, at the end of the operation period, the government doesn't get them back ? in line with the government's plans to ultimately privatize energy generation and distribution activities.?

?To be clear,? says Gruenewald, ?it is a simple philosophy: The project benefits from its highly competitive energy price. It remains in the developer's hands and there are no problems in financing it.?

At $1.37 billion, this is one of Turkey's heftiest power deals to date, trailing last years's Afsin Elbistan. Financing fits a 75/25 debt-equity split. Steag fronts $350 million in equity, with $1.02 million in loans sourced from a blend of bank debt and ECA financing, a fact that allowed for non-recourse project financing.

Lead arranging the deal are Dresdner Kleinwort Benson, Kreditanstalt fur Wiederaufbau and WestLB. The debt divides into four tranches, three of which boast the same consortium of predominantly German banks, comprised by Bayerische Landesbank, Hypovereinsbank, Bank Austria, Deutsche Bank, Hessische Landesbank, BHF-ING, ANZ, Credit Agricole, Sumitomo, Barclays, Commerzbank, Industriebank, WGZ Bank, DG Bank, and Westfalenbank. The tenor on all tranches is 15 years, including a 41 month construction grace period. Repayment is scheduled according to 24 equal semiannual chunks.

The first ECA tranche, guaranteed by Hermes, is priced at $372 million and sustains a margin of 75bp over Libor. Of this figure, a $124 million KfW financed portion rests at a commercial interest reference rate (Cirr) of 7.74%.

The OeKB tranche notches $136 million and cuts a margin of 80bp over Libor. This block is expected to break into syndication shortly.

More interesting, however, is the $131 million CGIC tranche, lead arranged by the South African ABSA Bank. The domestic market public issue is linked to CGIC's Cirr, with a fixed rate margin of 8% per annum. Says Boris Westphal, Steag's Financial Engineering Manager, ?South Africa has been deeply committed to the project since its inception.? German RAG Trading and Rheinbraun Brennstoff is leading the fuel supplier consortium, which will supply annually 2.9 tons of predominantly South African coal for the project's life span. South African coal is not only competitively priced but also provides the quality necessary for optimal performance, says Steag.

Equally interesting is the GkA tranche. German Government support, according to Steag, has been tremendous. Their commitment to the $356 million portion provides political risk cover, the subordinateed character of which allows it to defer for up to one year. The margin hits 215bp.

German support runs deeper still: Siemens is acting as turnkey contractor, while Babcock-Borsig will supply the two 605-MW Benson steam generators. Civil works, however, will be tackled by a joint-venture between Turkish contractors Gama and Tekfen.

The project is based on a 20-year take or pay power purchase agreement (energy sales agreement) between the Turkish project company Isken, managed by Steag, and the Turkish public utility TEAS. Payment will be in US dollars and TEAS' obligations under the agreement are fully propped up by a Turkish Treasury guarantee. Says Gruenewald, ?the treasury is unconditionally backing the financial strength of TEAS.?

This point is pivotal. TEAS currently suffers from a notoriously delicate balance sheet. At the same time, the Turkish government, on IMF insistence, is moving towards limiting the number of guarantees (contingent liabilities) it issues. However, the BOO scheme enjoys treasury guarantees for all five projects, which ?are thus significantly more financeable,? contends Alpacar. Adds Westphal, ?without the guarantee, the project would not have been accepted by the banks.?

By the end of 2003, when the project comes on line, Steag expects it to churn out annual revenues of approximately $400 million.

?We want to demonstrate to our Turkish partners that we're as reliable as we promised. Since we're talking about a 20 year contract, confirming our reliability is key. So of course, our highest priority is superior performance,? says Westphal.

Finance packages for four other BOO plants worth $4.2 billion are set to close soon. In sum, the BOO scheme envisages more than 40 billion KWh of electricity to be produced annually from a total power capacity of 5,740 MW. Intergen's plants in Gebze and Adapazari are expected to sign any day, with the final Izmir project still in the planning. National Power/ Bayinder Ankara project is the other BOO-in-waiting.