IJGlobal
A Green Street Company

Alto Maipo: good hydro, gone bad

Juliana Ennes

03/10/2018

(Originally published in the Summer 2018 edition of IJGlobal)

The Alto Maipo hydropower project in Chile makes people cagey. If you request to talk to those involved about its tangled history, you are likely to be told it "is a strict no-comment deal."

If all you knew about the project was the announcement on 8 May (2018) by AES Gener about the financial restructuring of the 531MW power facility, you would be missing the full picture.

The recent financing is seemingly a happy ending for a project which had appeared to be drawn in to a perfect storm. This was the third major financing for the project – and the second restructuring in a little more than a year.

It was completed amid billion dollar cost overruns; changes of equity ownership; modifications to the list of original lenders, huge haircuts on the debt book; and a technical default.

This is despite the underlying asset have many attractive features: it is located just 50km southeast of Chile's capital, Santiago, reducing transmission costs; its waterways towards the turbine rooms are in great part underground, reducing flooded areas; and it has received support from the government to supply zero-emission electricity to the country's center of power.

The equity

There are plenty of important details which were missing from the May restructuring announcement. For one is a vastly inflated project cost, rising from an original construction budget of $2 billion to a cost of $3.4 billion.

Equity is now divided between AES Gener (93%) and Strabag AG (7%). Strabag has entered the project as an EPC contractor, but the contract has peculiarities. It became the minority sponsor as it received shares of the project as part of its payment for its EPC contract.

More bizarrely, Strabag has also become a lender on the project. Its Chilean subsidiary was initially awarded a contract to build part of the hydropower complex in 2012. After difficult technical conditions and the withdrawal of a contractor, Strabag got an additional contract valued at €800 million ($930 million), increasing its contract size to a total €1.5 billion.

The civil works agreement includes the construction of 73km of tunnels on a lump sum fixed price contract that covers both the work that has already been undertaken as well as all future work provided by the contractor, which reduces geological and construction risk associated with the project for AES Gener.

The total required equity contribution has increased from $800 million to $1.45 billion. Part of that amount is said to be already available for the repayment of part of the debt.

According to AES Gener, up to $400 million of equity commitments will be funded with cash from operations, reducing the pressure on sponsors.

The debt

Around $2 billion in debt was closed in May 2018, including Strabag's participation as a lender. The EPC contractor will back-up its obligations with standby letters of credit totaling $300 million in addition to a corporate guarantee provided by its parent company Strabag SE.

Bank-syndicated debt was increased from around $1.3 billion to $1.6 billion.

Originally agreed with IDB, IFC, OPIC, KfW, DNB Bank, BancoEstado, BCI and Itaú CorpBanca, the second restructuring saw this list of participant lenders shrink.

IJGlobal has confirmed with different sources that IFC and KfW have both dropped the project and that Itaú CorpBanca and BancoEstado have reduced their share in the transaction. Deutsche Bank and Vial subsidiary Santana saw the opportunity to acquire the participation on the debt book from the four players for a bargain and helped the sponsors close the deal with the remaining financial institutions.

Before leaving, IFC's participation in the programme was estimated at $150 million, while IDB had $200 million and OPIC $245 million. Other tickets have not been disclosed.

Mizuho had already withdrawn from Alto Maipo even before the second restructuring. The Japanese bank left the project in September 2017, writing-off about $20 million it had already disbursed. The bank feared the project's financial viability, after several cost overruns.

In January (2018), IDB had "recommended an investigation" about whether the institution should continue to participate in the project or not. The analysis focused on environmental and social impacts, and ultimately it remained.

The new debt package will be repaid in 20 years after completion of the project, which is expected for 2020.

History

To understand the importance of some items from the second restructuring package, such as risk allocation and construction deadlines, you have got to know the history of the project.

The developers originally submitted an environmental impact statement for the plant in 2006 but had to resubmit a revised version following complaints in 2008. It received approval in 2009, but a larger investigation into Alto Maipo's water rights agreement with Aguas Andinas by the National Sanitation Service Authority was still pending – and only approved in 2012.

A first financing package was signed in 2013. At that time the project sponsors were AES Gener (60%) and Antofagasta Minerals' Minera Los Pelambres (40%). In the initial structure, Gener committed $562 million in capital, while the minority shareholder committed $334 million. Of the overall sponsor contributions, 30% corresponded to equity and 70% to subordinate debt.

After several delays, cost overruns and engineering challenges, Antofagasta, owned by Chilean conglomerate Luksic, dropped out of Alto Maipo in January 2017, after having already invested around $350 million towards construction.

Gener assumed Los Pelambre's 40% equity stake for a symbolic amount. In return, the cost of electricity produced at Alto Maipo to be sold under a power purchase agreement (PPA) to the Los Pelambres mine was reduced by 15%. The 20-year agreement was amended to remove all termination options.

With costs mounting and with the exit of a large sponsor, Alto Maipo was restructured for the first time in March 2017.

But it was not the end of its problems. The hydropower project's future was put into serious jeopardy when AES Gener fired its contractor Constructora Nuevo Maipo (CNM) in June 2017. The cancellation of CNM’s contract put the project into technical default.

That situation, coupled with lower productivity than required by construction contracts, led to further cost increases for a project already well over budget.

At that point, however, the power plant was 54% complete and faced debt liabilities of $613 million. It made more sense to move forward than abandon Alto Maipo completely.

Strabag, who was already in the project, got CNM’s share of the construction, a move that helped close the second restructuring on 8 May 2018, despite the cost overruns going from an additional 10-20% expected at the first restructuring to an extra 60%.

With increased financial requirements, sources told *IJGlobal* that, in parallel to the negotiations with lenders and new EPC contractor, AES Gener was still looking for equity relief.

State-owned Empresa Nacional del Petróleo (Enap) started conversations with AES Gener at the end of 2017 to provide gas to gas-fired power stations from the electricity company. These discussions evolved to a possibility of Enap joining Alto Maipo as a minority sponsor.

It never materialized, however. On 29 May (2018) – after the second restructuring had closed – Enap officially gave up the idea, allegedly to focus on core investments related to oil & gas exploration and production, although rumors say it is still involved with other energy projects.

Advisers

With so many players involved, the project has also seen quite a troupe of legal advisers.

Baker Botts has advised Alto Maipo SpA. Claro & Cia has advised AES Gener. When still on the deal, Antofagasta Minerals used the services from Bofill Mir & Álvarez Jana Abogados.

On the banking side, Carey has worked from Chile with IDB, IFC, OPIC, Banco de Crédito e Inversiones (BIC), BancoEstado, Itaú Corpbanca, KfW IPEX Bank and DNB Bank. From the US, the institutions worked with Chadbourne & Parke.

EPC contractor Strabag was advised by Eyzaguirre, in Chile, and by Pepper Hamilton as NY counsel.

The problems

Alto Maipo includes two run-of-river facilities, the 275MW Alfalfal II in the Colorado River sub-basin and 256MW Las Lajas on the Maipo River, west of Santiago. Even with delays, it has progressed and, to date, reached 65% of completion.

The project includes a vast array of tunnels running deep under the Andes Mountains. The biggest problem the project has faced is that the geological formation of rock these tunnel pass through is different from that anticipated in the pre-construction studies. This means the tunnel would take longer and cost more to build.

Market conditions in Chile have also changed since the beginning of the project, with energy costs dramatically dropping in the country.

Already facing delays, increased costs and lower projected revenues, an exit of sponsors and lenders added insult to injury.

From the financing perspective, bankers believe that one of the main mistakes on this project was to allow geological and construction risks to be taken by the developer and, as a consequence, by the lenders. It should have had an EPC contractor taking construction risk, as now Strabag is doing, from beginning.

Additional delays are now protected as well, by a corporate guarantee in letters of credit amounting to $300 million. The restructuring has also included incentives for early completion of the project.

Financiers also regret not being more firm about the necessity of having the project fully contracted with long-term PPAs – only a fraction of total capacity is contracted with Los Pelambres.

While bankers try to make their *mea culpa* and understand what they would have done differently, some people involved with the sponsors say that the banks didn't take any exposure they wouldn't take in other competitive markets. Part of the game or not, the project that is taking more than 10 years to become a reality has certainly left behind some traumatized bankers.

One of them is not completely convinced that this second restructuring will sustain the project long-term. He believes that, after construction completion, Alto Maipo will have to go the market for debt once again.