Pagbilao 3, Philippines

Thomas Blott

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The Ps44.09 billion ($1 billion) project financing for Pagbilao power plant phase 3 is the largest ever project financing in the Philippines funded exclusively by local lenders. Local banks, liquid in both US dollars and pesos, are slowly edging out competition from international lenders in the Philippines energy market, which are increasingly struggling to compete on both pricing and tenor.

The Pagbilao expansion project was also one of the first notable projects to be developed following the phasing out of energy conversion agreements (ECAs) with state-owned National Power Corporation (NPC). This dynamic, which has pushed more projects into the wholesale market, also plays into the strengths of local banks since the cash flows are denominated in pesos.

Banking on the Philippines

Pagbilao Energy Corporation, a joint venture between Aboitiz (50%) and TeaM Energy Corporation (50%) signed the financing in May this year and closed the deal in June after finalising all of the conditions precedent (CPs). TeaM Energy is a joint venture between Marubeni and Tokyo Electric Power Corporation, which was previously branded as Crimson Power.

The project entails the development of a 735MW coal-fired thermal power plant in Quezon, the Philippines. It is the third unit to be built at the site. TeaM Energy acquired the first two units when it bought Mirant’s portfolio of power projects in 2007. Aboitiz is the independent power producer administrator (IPPA) for the first two units and handles the procurement of fuel and sale of energy, although it does not have a stake in the project company.

TeaM Energy financed the acquisition of the first two units using international bank debt in a $1.62 billion 17-year deal led by JBIC, but two years ago the sponsor closed a $220 million 12-year mezzanine loan to refinance a portion of the debt in a deal led by SB Capital, which also brought in Metrobank and EastWest Bank, which demonstrated the increasing weight of local lenders.

The sponsors had held talks with several international lenders including the Japan Bank for International Cooperation (JBIC) about financing the third phase, but opted for local banks instead. The Philippine bank market has always been relatively liquid and is now able to match international banks in tenor also, which has all but eliminated the need for offshore tranches in project financings for projects without access to hard currency revenues.

The financing comprises two 15-year tranches and comes from a group of seven local lenders. Tranche A is fully amortising and is being provided by a single lender, SB Capital, which joined the deal as co-lead arranger. Tranche B included a repricing mechanism at year seven and was underwritten by the following mandated lead arrangers:

- BDO Capital
- BPI Capital Corporation

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- First Metro Investment Corporation

The following lenders joined during primary syndication:

- Philippine National Bank
- Philippine Savings Bank
- China Banking Corporation

The financing also includes roughly Ps11 billion in equity and shareholder loans from the sponsors plus a small debt reserve facility equivalent to around Ps2 million.

Merchant moment

The financing for the third unit also played into the strengths of local banks because of the absence of a long-term offtake agreement. For the first two units TeaM Energy sells 700MW of capacity at the power plant under an ECA with NPC (which includes a guarantee from the government of the Philippines), and sells the remaining 35MW capacity in the merchant market.

Aboitiz was appointed IPPA for the first two units after winning the rights to purchase the capacity from government following an auction. Aboitiz pays the government a regular payment to use the capacity of the plant and is responsible for handling the procurement of the fuel and the dispatching of energy, although from the sponsor's standpoint the counterparty for the deal is still the government and dispatch instructions flow through NPC.

Since the ECA was signed for the first two units, securing long-term offtake contracts has become very challenging in the Philippines and the government has stopped issuing government-guaranteed power purchase agreements. For the expansion project, the sponsors are selling the output instead into the market, although they do have some bilateral arrangements in place with customers.

The inclusion of an all Philippine cast of lenders provides a natural hedge against foreign currency movements since the revenues from any sales in the merchant market will be denominated in pesos. The inclusion of a long-term offtake contract is also often a requirement for international lenders since this usually includes features, which insulates the project against dispatch, currency transmission and other risks.

Trend setter

Pagbilao phase 3 is likely to be one of several large power projects to tap domestic funding in the Philippines. EGCO and Meralco, advised by HSBC recently approached the bank market for the 460MW San Bueneventa coal-fired power project and are said to be favouring local banks. Even for those projects with long-term offtake contracts the preference among sponsors for local banks is strong.

Mitsubishi, Daelim Industrial and DESCO have formed a consortium for the engineering, procurement and construction of Pagbilao 3. ING was financial adviser to the sponsors, while Latham & Watkins and Puno & Puno were the international and local legal advisers. Abuda Asis & Associates was the legal adviser to the lenders. Aon was insurance adviser to the sponsors, while JLT advised the lenders.

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