Altamira II: where eagles dare

01/11/2002

The Altamira II financing has been one of the most hotly-anticipated closes this year in Latin America. Not so much as a quality asset, although tightly-structured non-US assets are very much in demand, but because of what it means for future independent power projects in Mexico. Altamira looks to have proved to the country's prospective sponsors that the fuel supply issues that have dogged progress of new deals can be put behind them.

Altamira II is a 495MW gas-fired combined-cycle plant located in Tamaulipas, and has a 25-year power purchase agreement with the Comision Federal de Electricidad (CFE), Mexico's state electricity monopoly. This specification could apply to any one of the successful financings in the sector. What marks it as a first is that it is financed with gas provided directly from state gas monopoly Pemex Gas y Petroquimica Basica.

The $246 million financing for the Altamira II power project has been 12 months in the making and should create a viable framework for other projects that are stalled while they resolve fuel supply issues. But Altamira's sponsors, Electricite de France and Mitsubishi Corporation, have been able to create a workable compromise with the government that lesser producers will need to improve upon to gain attractive financing.

Earlier independent power plants used the CFE as an intermediary in fuel purchases, meaning that it took on most of the fuel supply risk, and bought this only when it needed to dispatch a plant. No longer. Now the CFE and Pemex are presumed to operate independently, albeit as monopolies, and relish this state of affairs. Plants, therefore, now have to make separate bids for the gas that they will require and bid for offtake contracts for the long-term, without knowing whether they will be called on to use this gas. And they cannot sell this on.

There appeared to be little way out of this impasse, although the mandated leads had been suggesting a financial close towards the end of 2001. The bid documents on which Mitsubishi won the concession (EdF came in at a later date, but bought a controlling 51% stake) had mentioned a way to get lenders comfortable with the economics of the mechanism, but not the best way of defining defaults under the two contracts.

Under the gas supply agreement, the project company must sign up to an agreement with a mixture of fixed and flexible capacity. Should the project company not use the gas for which it has contracted then it must pay (at the end of the year), a penalty expressed as a percentage of the shortfall. The lower the level of firm capacity, the higher the penalty percentage.

However, the difficulty for lenders is that neither Pemex nor the CFE is prepared to recognize, much less allow for, a default under a contract with the other. The definition of a force majeure default event under the contract has been made slightly stricter, so that lenders can gain at least a degree of recourse to the sovereign. However, in the event of a willful non-performance event, then the project company would not be made whole under a contract. This provision, however, would only be reasonable if alternative sources of gas can be found. The only slim comfort is that such behaviour is prohibited under Pemex's regulations.

The financing's mandated lead arrangers are Citibank and Mizuho Corporate Bank, and they were joined by ING and Bank of Tokyo-Mitsubishi as underwriters. The ultimate take for the commercial banks is just $78 million, in contrast to $118 million in 12-year money from the Japan Bank for International Co-operation (JBIC). Moreover, 97.5% of the

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commercial piece is covered by political risk insurance from NEXI, so given the size and solidity of this 10-year piece a sell-down is unnecessary.

The balance of the $246 million debt comes from the two sponsors in the form of a subordinated loan that covers their equity contributions. Another $40 million is injected upfront. But the most important aspect of the support from the sponsors is the provision of contingent equity to cover the possibility that the plant is left stranded through non-performance by Pemex. The exact structure through which this has been provided, as well as its size, has not been released. However, such a level of sponsor support would be a clear demonstration of the limits of the solution to less well-capitalised sponsors.

With the exception of plants close to the US borders or El Paso properties (El Paso being the only outside supplier of any note), working with Pemex is vital. Since the provision of contingent equity (even backed by letters of credit) tends to depress internal rates of return, this will be something that few sponsors would agree to. Another solution ? the purchase of insurance ? is prohibitively expensive, and the multilaterals are essentially full up on Mexican exposure.

JBIC is not a bad partner to have, however, even if it lacks some of the multilaterals' clout. For the Japanese ECA and sponsor, the deal is also an opportunity for Mitsubishi Heavy Industries to gain a turbine contract. JBIC has also made loans to Mexican institutions such as a $250 million untied export promotion loan to Banco National de Commercio Exterior, and ¥5 billion to Banamex. Solid support to the country's banking system should create an incentive for the Mexican government to resolve any serious faults.

Electricidad Aguila

de Altamira

Status: Signed 15 October 2002

Size: $296 million

Location: Tamaulipas, Mexico

Description: 495MW gas-fired plant

Sponsors: Mitsubishi Corp (49%), EdF (51%)

Debt: $78 million 10-year commercial piece, $118 million 12-year JBIC credit, $40 million subordinated sponsor loan

Lead arrangers: Mizuho, Citigroup

Lawyers to the borrower:

Milbank Tweed, Hadley & McCloy

Lawyers to the lenders:

Shearman & Sterling

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