

PROJECT ABSTRACT

Project number	HO-0125
Project name	Electricidad de Cortes, S.R.L. de C.V. ("ELCOSA")
Country	Puerto Cortés, Honduras
Sponsors	Wartsila Diesel Development Corp. ("WDD") Honduran Electric Company, S.A. de C.V. ("HECO")
Total project cost	US\$93.4 million
IDB participation	IDB A-Loan: US\$10.5 million
Department	Private Sector Department
Status	Approved by the Board of Executive Directors
Date	April 26, 1995

I. PROJECT DESCRIPTION

The US\$ 93.4 million project consists of the construction, installation and operation of the first private power plant to be connected to the national grid. An 80 MW diesel power plant, ELCOSA will be located in Puerto Cortés, on the Atlantic coast. The primary sponsors are a group of well-established Honduran businessmen who formed the Honduran Electric Company ("HECO") interested in securing a reliable source of energy for their export-related businesses in the San Pedro Sula area, and Wartsila Diesel Development Corporation ("WDD"), an U.S. private power developer with experience in developing private power projects in the region as well as being a subsidiary of the world's largest medium-speed diesel manufacturer.

Other investors in the project include Illinova Generating Company, a subsidiary of Illinois Power, the International Finance Corporation, Scudder Latin American Trust of Independent Power (a power fund with IFC and CAF each 25% investors), and a private U.K. investor.

II. PROJECT COST

Project Costs (US\$ MMs)	
	Total
Turnkey Construction Contract	67.2
Fuel Pipeline, Vehicles and Furniture	.3
Import Duties and Taxes	7.2
Legal, Engineering and Development	2.6
Contingencies	.6
Transmission Upgrade & Land Lease	3.6
Insurance Premium, Interest and Financing Fees	5.4
Escrow Account	4.0
Working Capital	2.5
TOTAL PROJECT COSTS	93.4

III. PROCUREMENT

Procurement procedures for the project has followed Bank procedures for private sector projects, and are consistent with the Bank's criteria of economy and efficiency. Capital goods forming part of the turnkey contract will primarily be from the Netherlands. Auxiliary equipment will be sourced from Germany, Denmark, France, and the U.S. Construction and civil works will be subcontracted to Honduran companies under the supervision of Stork-Wartsila Diesel B.V., the turnkey contractor.

IV. FINANCIAL PLAN

ELCOSA - Financial Plan (US\$ MMs)		
	Total	Percentage
Shareholder Equity	26.9	28.8%
Quasi-Equity (IFC/FMO)	4.5	4.8%
Total Equity	31.4	33.6%
Senior Loan		
IDB	10.5	
DEG	5.7	
IFC A Loan	10.5	
IFC B Loan*	35.3	
Total Senior Loans	62.0	66.4%
Total Financing	93.4	100.0%

*B Loan Participants: ING Bank, KOP, Mees Pierson, FMO

V. IDB's ROLE

A. Additionality

Complementary Support. The Bank's participation in ELCOSA complements the Bank's existing program and provides direct financing support to the first private power plant connected to the national grid. This project will increase the country's generation capacity by approximately 15%.

Providing Scarce Long Term Resources. The Bank will be providing long-term financing not available in the country at reasonable rates. The participation of the Bank will support the balanced distribution of terms between the shorter term private sector providers of financing and the longer-term official sources of financing.

Providing Comfort to Private Sector Investors. The Bank's presence in ELCOSA provides the private investor with a financial institution experienced in the policy dynamics and supports the cooperation necessary between the private and public sectors.

Addressing the Infrastructure Deficit with Private Sector Support. The regional deficit led the Bank to create a special program targeted towards increasing private participation in this sector, traditionally limited to the public sector. The ELCOSA project represents the initial step by the Bank to address the enormous infrastructure deficit. The participation of the Bank in this project sends a strong signal to the region of the Bank's commitment to respond quickly to the needs of the region.

B. Developmental Criteria

Supporting a Government Priority. Honduras is undergoing a severe energy crisis due to its deficit in installed capacity, reliance on hydro and technical problems in the Francisco Morazan dam. The Government of Honduras estimates that approximately 2% potential of the national GDP was sacrificed as a result of electricity shortages. The government declared the resolution of this situation a government priority. The Bank through its participation will be supporting the government meet its goals of increased and diversified sources of energy through the ELCOSA project.

Demonstration Effect. The project represents the first privately owned power facility in Honduras to be connected to the national grid. Other attempts by the sector to encourage private sector participation have encountered obstacles which did not allow their implementation. The successful establishment and operation of the ELCOSA project could serve to encourage other private investors to participate in the future development of the Honduran power sector and to promote competition in the sector.

Support the Honduran export industries. The ELCOSA project will directly support the Honduran sponsors of the ELCOSA project by providing a consistent source of electricity to maintain the standards necessary to compete internationally and will be indirectly supporting other Honduran industries through the provision of increased electricity to the state utility, ENEE.

Technology Transfer. The project will use state-of-the-art engines, which are specifically designed to combine high fuel efficiency with low emissions in spite of burning heavy fuels. The turn-key contractors and the operator of the plant, will provide technical and power plant management training to the employees of the project.

C. Bank's Strategy for Private Sector Operations

The Bank's objective is to channel long-term financing to infrastructure projects in the region, facilitating investment carried out by the private sector. As a new program, the Bank has decided to proceed carefully, seeking projects with the presence of institutions in infrastructure finance, with experienced well-established firms with the financial resources and management capability to successfully complete and operate a project. The presence of the International Finance Corporation as financial advisor, and of Wartsila Diesel International, a company with over 150 completed turnkey operations, provides the Bank with experienced partners. Further the analysis carried out by the Bank has shown the project to meet the following tests: a) the presence of an adequate macroeconomic environment; b) the presence of a regulatory environment providing appropriate support to private sector projects; c) soundness in technical, financial, and economic criteria; d) managerial soundness; e) the international financial community standards in terms of viability, security, and legal structure.

VI. PROJECT BACKGROUND AND CONCEPT

The Honduras electricity sector has not kept up with growth in demand. There have been no new generating plants added to national grid system since 1985, and thermal plants of the National Electricity Company ("ENEE"), which can provide more stable power during the dry summer months, are in general state of disrepair.

In 1994, as a result of a severe drought and lack of installed capacity, Honduras suffered electricity rationing over a 9 month period of up to 12 hours per day. Specific steps by the Government of Honduras to alleviate the country's power shortage include: a) privatization and diversification of the power sector through the inclusion of private power producers particularly in thermal plants; b) the rehabilitation of existing thermal plants through private concessions; d) reforms directed towards strengthening the institutional structure of the ENEE; and e) repairs to the Francisco Morazan dam ("El Cajón"), the primary source of power in the country.

In December 1994, the Bank in recognition of the Honduran crisis approved a US\$36.9 million financing package (Energy Sector Hybrid Loan HO-0112) to support the Government of Honduras in its efforts to address technical problems and to institute sectoral reforms directed toward alleviating the situation, including steps to encourage private sector participation and diversify energy sources.

Project Concept

The project entails the installation and operation of an 80 MW diesel- engine-powered electric plant in Puerto Cortés on the Atlantic coast of Honduras. The plant will be built by Stork-Wartsila Diesel B.V., Netherlands ("SWD") under a fixed-price turnkey construction contract. Operations and maintenance of the plant will be provided through the Cortés Operating S.A. de C. V. ("Cortés") which will be a joint venture of WDD and North American Energy Services. Fuel for the plant will provided under a 15 year contract with Texaco, which imports and distributes through Puerto Cortes.

The project will sell electricity to the national grid based on a 15 year power purchase agreement with ENEE, the Honduran government utility. ENEE has committed to purchase all capacity not allocated to HECO and all the delivered energy not consumed by HECO. HECO has been allocated initially 6 MW of capacity (growing .5 MW per year) and is expected to consume about 10% of ELCOSA's electricity production. Each HECO customer has signed a 15 year power purchase agreement with ELCOSA.

As an emergency measure, Wartsila Diesel installed a temporary 24 MW plant during the construction of the permanent plant to respond to the immediate need for additional generation capacity in Honduras. The temporary plant is owned by WDD and its cost is not included in the Project costs. Delivery of energy started with the emergency plant in May 1994, and as of February 1995, three of the permanent engines and generators had been installed and were being tested.

The project was appraised and structured by the International Finance Corporation ("IFC") which acted as financial advisor to ELCOSA. The IFC identified a group of international commercial banks, multi-lateral and bi-lateral agencies to finance the project. The project was initially conceived as a 60 MW plant, the Government of Honduras (GOH), under the National Decree of Energy Emergency requested that the project be expanded an additional 20 MW to better meet the immediate needs of the country. The Bank was approached by WDD one of the primary sponsors, in October 1994 to participate in the 80 MW project. The Bank has been requested to provide up to \$10.5 MM in long term financing.

The project brings together strong local and experienced international sponsors, and financing. This private sector project responds both to the country's short-term need for additional electric supply through the installation of an additional 15% capacity and the long-term need to diversify its sources of power.

VII. ENVIRONMENTAL CLASSIFICATION

The project environmental brief was presented to the Environmental Committee on February 21, 1995 and was classified as a Category 3 project. ELCOSA's environmental mitigation procedures and worker safety program meets IDB and World Bank. As such ELCOSA is exemplary in its environmental program. As a result of this project, the adjacent ENEE plants will also improve their environmental mitigation program.