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CMS Inks Credit Support Deal

CMS Energy has signed an innovative agreement with **Capstone Global Energy** and **Harvard Management** that could juice up the credit rating on its power trading contracts to single A.

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DOMINION SEEN RESTARTING ALLEGHENY MERGER DISCUSSIONS

Richmond, Va.-based **Dominion Energy** reportedly has entered merger discussions with **Allegheny Energy**, the second time it has seriously courted the Hagerstown, Md., company in two years. Wall Street bankers and analysts who have spoken to Dominion about its plans say it has set the ball rolling again now to take advantage of Allegheny's depressed share price and the general downturn in the wholesale energy market. Over the past three months Allegheny's stock price has plummeted more than 50% to around $19.

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GAZ DE FRANCE EYES U.K. POWER MARKET, PREPS BID FOR BP PLANT

Gaz de France is looking to enter the U.K. power generation market and has initiated negotiations with BP to purchase its 400 MW Great Yarmouth facility on England's East Anglian coast. A person close to the matter says Paris-based GdF is presently undertaking due diligence on the newly built combined-cycle gas turbine plant and could be ready to make a bid within the next few weeks. Oil giant BP put its Great Yarmouth facility up for sale in May and has hired **J.P. Morgan** to shop the asset (PFR, 6/13). **Colum Doyle**, a spokesman for BP's

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CLECO, CALPINE SET TO TEST MARKET WITH $575M ACADIA FINANCING

Acadia Power Partners, a joint venture between Calpine and Cleco, will put out feelers in the project finance market later this month to gauge appetite for a $575 million loan refinancing a now operational 1,160 MW plant, but it isn't expecting an easy ride. **Kathleen Nolan**, treasurer at Cleco in Pineville, La., says the structure would be a clean, straightforward mini-perm loan, but adds that tolling arrangements with Calpine and **Aquila** are likely to make credit questions key to the deal's success. "It's going to be

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AES LOOKS TO RELAUNCH SPANISH PROJECT

AES is looking to sign up banks to relaunch a stalled 1,200 MW power generation project in southeastern Spain next month. The embattled independent power producer is holding discussions with a number of lenders including **ABN AMRO**, **BNP Paribas**, **Credit Agricole Indosuez**, **Credit Lyonnais** and **Société Générale**, about financing the roughly EUR600 million deal. The strong Gallic flavor of the lineup reflects the fact that AES has signed a supply and offtake contract with Paris-based utility **Gaz de France**. One banker says non-recourse financing is likely to be structured as a club-type loan, with these banks and possibly more invited into the deal before a small syndication round.

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EdF Seen Hiring Deutsche Bank

Electricité de France is believed to have hired Deutsche Bank to work alongside **NM Rothschild** to advise on its upcoming privatization and partial floatation. A banker in London says an EdF official told him of the news last week, but said a formal announcement would not be made just yet. The banker says the threat of trade unions protesting against the privatization likely has caused EdF to adopt a low-key approach.

Late last week the French government hired **Morgan Stanley** and **Credit Lyonnais** to advise on the sale of EdF. It also selected **Credit Argricole Indosuez** and **Lazard Freres**, to advise on the sale of **Gaz de France**.

CMS Inks Deal To Juice Credit On Trades

CMS Energy has signed an innovative agreement with a specially-created limited partnership allowing it to offer counterparties to long-term gas and power trades an A rated credit profile. The Dearborn, Mich.-based player has been buffeted by revelations of round-trip trading this year and an ensuing slide in its corporate credit corporate rating to BB minus. That resulted in its trading unit chalking up a net operating loss of $18 million in the second quarter, a slide of $57 million over the corresponding quarter last year.

The agreement is with a limited partnership called **Current Capital**, which is backed by Houston-based energy and investment advisory firm **Capstone Global Energy** and **Harvard Management**. "It is basically a credit support agreement that would enable us to permit [the marketing services and trading unit] to move forward with long-term gas and electric sales," **David Joos**, president and coo, told an investor conference call last week. He characterized the relationship as an enabling agreement whereby CMS can take deals to the partnership to see if it wants to back them. He added CMS won't be going into further details until it completes a deal off the back of the vehicle. Calls to **Riaz Siddiqi**, president and ceo of Capstone, were not returned.

CMS has yet to complete a deal under the arrangement, but wants to stay in the market for long-term supply deals. "We continue to believe that wholesale marketing to the municipals and co-ops makes a lot of sense, but obviously there are concerns on the customer side about credit support," Joos said.

Aquila, Arclight Ready $200M Loan For Calif. Gas Facility

Co-sponsors Aquila and **ArcLight Capital Partners** are looking to raise a $200 million project level loan to fund the acquisition of the Lodi Gas Storage facility in Northern California. Co-bookrunners **DZ Bank** and **Union Bank of California** have begun sounding out banks on taking co-arranger slots, according to one market official. Aside from having the rarity value of gas storage paper, the twist in the deal is that it resembles a power plant financing in that it has a long-term tolling structure. These facilities typically have short-term tolling agreements, says one banker. A spokeswoman at Aquila and bankers at DZ declined comment. Calls to UBoC were not returned and ArcLight officials in Boston could not be reached.

The mini-perm is being pitched in the LIBOR plus 200 basis point range, but bankers say the deal has yet to formally launch so pricing isn't fixed. The slight premium over traditional power plant deals reflects the innovative nature of the deal, say market players. Co-arrangers will likely be signed up this month and then a formal syndication will be launched post Labor Day.

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Ex-Merrill Trading Chief Steps Aside At Allegheny

Dan Gordon, former head of the **Merrill Lynch** U.S. power and natural gas trading team snapped up by **Allegheny Energy** for $490 million last year, is stepping down from the top trading job at the Hagerstown, Md., player. Allegheny last week announced it is paring back its trading effort and will focus on leveraging its Midwest and Mid-Atlantic assets. Gordon is stepping down from his role as president of global markets and will become a strategic advisor. He will advise on downscaling the operation and also on the legal action related to the company's long-term California contracts, says spokeswoman **Janice Lantz**. California has been looking to re-negotiate a number of contracts signed at the height of its power shortage. Lantz says Allegheny is not among the counterparties that have re-negotiated. Calls to Gordon were not returned.

The Merrill team was acquired just over 18 months ago (PFR, 1/14/01) and was heralded as a deal that would allow Allegheny to transform itself into a national player in the energy trading market. The company signaled the end of that drive in a conference call last week and said it will focus on its core strengths and on maintaining its credit rating.

A successor to Gordon is being sought and the aim is to have someone in place not later than the first quarter of next year, Lantz says. She was unsure of the length of Gordon's advisory role. The change in strategy will likely see a reduction in the trading team headcount, which currently stands at roughly 100, she adds.

Reliant Plots Cross-Collateralization For Orion Mini-Perm Refinancing

Reliant Resources is looking to refinance $1.93 billion in two **Orion Power** non-recourse loans with a structure that cross-collateralizes the stronger New York project with its Midwest counterpart, say bankers familiar with its plans. Financiers involved in either of the two mini-perm transactions have been told to expect terms of the new deal to be released at the end of this month or the beginning of September. The rattled Houston power player has been looking for some time at ways to refinance the $1.2 billion Orion Power Midwest project loan, which matures in October, and the $730 million Orion Power New York facility that matures two months later. The initial plan was to refiance the debt at the corporate level, but this strategy was abandoned once Reliant Resources became embroiled in the round-trip trading scandal (PFR, 6/23).

While the mini-perm loans are separate deals, the vast majority of banks that are in one of the deals are also in the other, notes one banker. This means there are likely to be very few refuseniks from the New York deal blocking a watering down of their stronger deal's credit, he adds. The other factor that will drive bankers into the refinancing is the lack of other options. Reliant can't refinance at the corporate level at the moment so the only other way for banks to get re-paid would be to call in the security, a project financier says.

Banks Seen Looking To Restructure Damhead Deal

The banking syndicate involved in financing **Entergy Wholesale Operations**' Damhead Creek power plant in the U.K. is looking to restructure the roughly GBP500 million ($835 million) merchant deal in an attempt to stave off a full blown default on the non-recourse loan, according to market watchers. Bankers involved in the syndicate say they have formed a steering group that will work with the project sponsor to tackle problems associated with the loan.

One banker notes the loan is already in technical default, having breached covenants concerning coverage ratios, and says the banks are looking to move quickly to stop the deal from sinking further into trouble or to discourage Entergy from washing its hands of the deal. "The last thing we want to see is Entergy walking away from the problem and leaving the plant in the banks' hands," says one financier. He notes Entergy has written off its equity investment in the deal and thus has less incentive to support the plant. In an analyst conference call last week a senior Entergy official confirmed the utility had written off its investment in Damhead and was looking to restructure the loan within the next year to 18 months.

The steering group is being led by **Royal Bank of Scotland**, which is the agent bank for the deal, and also consists of **Bank of Ireland**, **Barclays Capital** and **Sumitomo Bank**. The lead arranger of the 1998 project loan, **Warburg Dillon Read**, subsequently sold its stake in the deal and is not involved in the restructuring. At least 12 other lenders have exposure to the project loan including **KBC Bank**, **Fortis Bank** and **Abbey National**, notes one banker. Officials at the above firms either declined to comment or did not return calls. Other lenders says the steering group is considering extending the tenor of the loan—thereby slowing the amortization rate—in an attempt to salvage the deal. "Improving the cashflow of the deal will make it easier for the banks and Entergy to find another buyer for the plant," notes one lender. Entergy began looking for buyers for the plant earlier this summer (PFR, 7/6).

Entergy arranged the loan in December 1988 to finance its construction of the 800 MW Damhead plant near Medway. The loan consisted of two tranches, a GBP464 million, 17-year senior piece and a GBP36 million, 12-year subordinated piece. The senior tranche was priced at 115-145 basis points over LIBOR, while the subordinated piece paid a 450 basis points spread. Entergy provided roughly GBP40 million in equity capital.

The Price Ain't Right

Tractebel Spread Meets Skepticism

Tractebel North America's initial price pitch of 1 3/8% over LIBOR on its planned $1.6 billion non-recourse plant financing is leaving project lenders unimpressed. They say the spread is out of line with where the power project finance market now stands. Indeed, they say the question isn't whether the deal will be done at that price, because it won't, but rather how much pricing will have to be jacked upwards.

One financier says the deal—which will be in the form of a club for four separate plants (PFR, 7/29)—is priced at the same level as **MidAmerican Energy**'s $875 million loan funding the Kern River natural gas pipeline expansion. But, that had a rarity value of being a gas transmission asset and was backed by steady regulated earnings, he explains. Power generation deals are nowhere near that mark in the current skittish market, he adds. Calls to **Rachel Kilpatrick**, treasurer at Tractebel North America in Houston, were not returned

One financier says lead bank **Credit Suisse First Boston** is dealing with the market perception with officials at Tractebel's European head office in Brussels. He adds those officials will likely visit the U.S. shortly to launch the deal and should get a sense that it can't be done at the current indicative price talk. Calls to CSFB officials were not returned by press time.

Innogy Honcho Adds Top RWE Trading Role

Brian Senior, managing director and head of energy trading and asset management at U.K. utility Innogy, has been allotted the top power trading post at RWE Trading. **John Wilkinson**, a spokesman at Innogy, says that following the Swindon-based utility's merger with RWE, Senior will mix his time between running Innogy's U.K. energy desk and RWE Trading's German and European power book. Senior was out of the office on vacation last week and could not be reached for comment.

Senior replaces Dr. **Jürgen Dennersmann**, managing director, who has moved to London last month to coordinate the intergration of Innogy into RWE. Among his immediate tasks is determining whether to intergrate Innogy's trading business into RWE Trading, says Wilkinson. At RWE Trading Senior reports to **Hans-Dieter Erfkemperm**, ceo. **Stefan Judisch**, managing director, remains head of oil and gas trading and energy marketing.

Latin America

Investment Boutique Seeks Latam Expansion

Franklin Park Energy (FPE), a private equity investment group in McLean, Va., focused on investing in utilities, is drawing up further Latin American expansion plans following the announcement of its purchase of **Companhia Energética do Maranhao** (CEMAR) from **PPL Global**. The deal marks FPE's first investment.

Tom Tribone, ceo, says FPE is involved in advanced discussions with several other companies in Latin America, but has yet to reach definitive agreements. FPE is looking at various countries, including Argentina, Bolivia and Peru. It is also scouring the U.S., says Tribone.

Despite the turmoil that has plagued Brazil, Tribone views the electricity business as a long-term investment and believes that the country's economic reforms will prove successful. "The macroeconomic policies are sound and Brazil has successfully executed an inflation targeting regime with floating exchange rates. So we think these policies will work," he says.

The upcoming election in Brazil also has not discouraged it from investing in CEMAR. "The front running candidates are both from the opposition, but our analysis is that no matter which candidate wins, foreign investors will be treated fairly," Tribone notes.

It is unclear when the transaction will close, but **Timothy Paukovits**, a PPL spokesman in Allentown, Pa., says CEMAR has put in a request to Brazil's **National Electrical Energy Agency** to expedite the transaction and approve it by Thursday. He declined to comment on the price tag of CEMAR, except to say that it will be nominal. Tribone also declined to discuss pricing, but says that FPE has made an initial commitment to invest BRL100 million ($34.8 million) in CEMAR. He adds that it plans to finance it with a combination of equity and debt.

According to Paukovits, PPL acquired CEMAR about three years ago and wrote off $217 million of its investment at the end of last year, $6 million in March and the remaining $94 million in the last quarter. He says that it decided to write off the investment following the drought and dysfunctional market in the energy area.

Lehman Brothers advised FPE on the deal and **Dresdner Kleinwort Wasserstein** advised PPL.

CEMAR provides electricity to more than one million customers in the northeastern Brazilian state of Maranhao. PPL owns 90% of the company and minority shareholders have the remaining 10% stake.

Mexican Financing Faces Delays

Deutsche Bank and **Bank of Tokyo-Mitsubishi** are struggling to arrange some $400 million in financing for the construction of two combined-cycle gas turbine plants being developed by Spanish utility **Union Fenosa**, says a banker familiar. The plants, dubbed Tuxpan III and IV, will have 938 MW of combined generation capacity and are located in the state of Vera Cruz, Mexico.

Financing has already been delayed once before. A project financier told *PFR* in May that the deal was originally supposed to close early last year, but due to some outstanding due diligence points closure was pushed back until this fall (PFR, 5/20). Financing may now be delayed until the beginning of next year while the project sponsor secures permits, says the financier.

The delays will probably impact the timetable for constructing the plants. "The Tuxpan projects are supposed to be operational in 2003 but since there are such extensive delays with the financing, there is a strong chance that the schedule will have to be altered because the funds won't be available," he says. In general, he says the delay is unsurprising given the instability in Latin America.

Calls to bankers at Deutsche Bank and Bank of Tokyo-Mitsubishi were not returned. Officials at Union Fenosa also did not return calls.

Iberdrola Wins Mexican Project

The **Comision Federal de Electricidad**, Mexico's national power company, has awarded Iberdrola the rights to build, own and operate La Laguna II, a $350 million 500 MW thermoelectric project in the state of Durango. The Spanish utility beats rivals **Union Fenosa**, **Electricité de France**, **Enel**, **AES** and **TransAlta** that also bid for the project (PFR, 6/3), according to a project financier familiar with the matter. Officials at the CFE and the power companies did not return calls or declined comment.

Iberdrola will finance the project entirely with equity, the banker says. Construction will begin towards year-end and the facility is scheduled to be commissioned in April 2005. Its output will be sold to the CFE under a 25-year power purchase agreement.

According to Iberdrola's Web site, the utility already owns and operates four plants in Mexico, Enertek (120 MW) and Monterrey I-III (750 MW). It also has several other projects under construction including Monterrey IV (250 MW), Femsa-Titan (37 MW) and Altamira III and IV (1,036 MW).

Over the next four years Iberdrola expects to invest $2.45 billion to double its Mexican power portfolio to some 5 GW.

Latin American Power Financing Calendar

*Following is a directory of upcoming projects and related financing in the Latin American power sector. To report new deals or provide updates, please call **Amanda Levin**, Reporter, at (212) 224-3292 or email: alevin@iinews.com*

Sponsor	Project	Project Type	Size (MW)	Cost ($mil)	Country	Advisor/ Financier	Status	PFR Issue
Alcoa	Santa Isabel	Hydro	1,087	700	Brazil	Citi	Financing delayed till 2003	7/22/02
Ceran	-	Hydroelectric	360	111	Brazil	BNDES	Will launch the loan shortly	10/8/01
Corporacion Venezolana de Guyana	Tocoma Dam	Hydroelectric	-	2,100	Venezuela	-	Expects to bring project on line by 2006	6/25/01
Duke Energy International	Pederneiras	Gas-fired	500	270	Brazil	-	Will finance with equity capital.	3/11/02
EdF, Mitsubishi	Altamira	Gas-fired	495	300	Mexico	Citi/Fuji	Expects to seal financing shortly.	7/1/02
Electricite de France	Rio Bravo III	Gas-fired	500	290	Mexico	SocGen	Arranging a $217M project loan	3/4/02
El Paso	-	Gas-fired	200	200	Mexico	-	Expects to bring project on line by 2003	4/16/01
El Paso	Araucaria	Gas-fired	469	340	Brazil	Dresdner	Financing delayed until Q4	7/4/02
El Paso	Macae	Gas-fired	400	700-800	Brazil	SocGen	Financing due shortly	7/9/02
Iberdrola	Vera Cruz	Gas-fired	800	700	Mexico	-	IADB has offered assistance to relaunch the stalled project	6/9/01
Iberdrola/Petrobras	Termoacu	Gas-fired	340	-	Brazil	IDB	IDB is evaluating the project	7/15/02
Iberdrola, Banco de Brazil, Previ	Termo Pernambuco	Gas-fired	540	350	Brazil	IDB, BBVA	Expects to bring project on line by 2002	3/26/01
InterGen	Carioba	Gas-fired	945	670	Brazil	-	Project delayed until Q1 of 2003	2/25/02
PSEG Global	SAESA	Distribution company	N/A	450	Chile	J.P. Morgan	Considering taking out a $300M loan to fund the acquisition	9/24/01
PSEG Global	Electroandes	Hydroelectric	183	227	Peru	BBVA Banco Continental/ Banco de Credito	Is planning $100m in loan and bond financing	7/27/01
Sempra Energy Resources	Mexicali	Gas-fired	600	350	Mexico	SocGen	In the process of arranging a corporate loan	3/11/02
Tractebel/Alcoa	Estreito	Hydro	1,087	700	Brazil	Citi	Waiting for enviromental permits	7/22/02
Union Fenosa	La Laguna II		450	-	Mexico	-	-	7/2/01
Union Fenosa	Tuxpan III & IV	Gas-fired	938	600	Mexico	Deutsche Bank BOTM	Expects to bring plant on line by 2003	6/4/01

Corporate Strategies

Pepco Turns To Bridge After Pulling Note Deal

Pepco Holdings, a newly created utility holding company, is tapping a $1.5 billion bridge loan to fund the merger of **Potomac Electric Power** and **Conectiv**, after pulling a private placement of the same size. The BBB rated bond (PFR, 7/29) was nixed after spreads in the wider energy sector ballooned, notes **Peter Otersen**, a credit analyst who tracks the company at **Standard & Poor's**. The loan funding comes from a syndicate headed by **Bank One** and **Merrill Lynch**, which were lined up to underwrite the private placement.

During an analyst's conference call last week **Andrew Williams**, cfo, said indicative pricing on the bond issue had widened to 300 basis points over comparable Treasuries. He said the utility considered it unwise to tap the market at this spread and instead arranged a one-year bank loan priced at 75 basis points over LIBOR. Pepco will reevaluate tapping the bond market to take out this loan in the next six months, he concluded. Williams was unavailable for comment last week.

Otersen says Pepco's inability to tap the bond market at its desired pricing doesn't impact the agency's rating opinion because instability in the energy sector was the reason for the deal's failure, rather than the condition of the company itself.

Under the merger agreement between Potomac Electric Power, based in Washington, D.C., and Wilmington, Del.-based Conectiv, Pepco acquired Conectiv for $2.2 billion, through an equal mixture of stock and cash. The new company assumed approximately $2.8 billion of outstanding Conectiv debt.

Pepco also has lined up a new $1 billion commercial paper program with a liquidity back-up via a 364-day revolving credit of $1.5 billion, which will replace all existing bank facilities of Pepco's subsidiaries.

San Antonio Muni Preps Bond Deal

The **City Public Service of San Antonio** in Texas is looking to issue $516 million of electric and gas system revenue and refunding bonds and will use part of the proceeds to pay down existing debt. **Karl Pfeil**, an analyst at **Fitch Ratings** in New York, says the proceeds will also be used to replenish its coffers after spending $150 million in cash over the last 18 months to upgrade its transmission and distribution assets. Calls to officials at CPS were not returned by press time.

Pfeil was not aware of the specific bonds set to be refinanced, but says the deal should result in cost savings between $9-10 million. He adds the offering is expected to price the week of Aug. 12 with **UBS Paine Webber** acting as the senior manager. The deal has been rated AA plus by Fitch because of CPS' solid management, strong financial performance and competitive retail rates of about 6.8 cents per KWh, which are among the lowest in the region. He says that gross operating revenues totaled $1.2 billion in its last fiscal year, of which 86% was derived from selling power.

Commenting on the bond market, Pfeil speculates that there will be more municipalities issuing bonds as interest rates are at historically low levels. "Interest rates are lower than they've been in our lifetime so we might see a lot more deals popping up. Even if they don't need to enter the bond market, munis might issue bonds anyway with the anticipation that these rates might not stay so low," he says.

CPS is a municipal utility that serves more than 560,000 electric customers and about 302,000 natural gas customers around San Antonio.

Financial Focus

Alternatives For Managing Volumetric Risk

Volumetric risk exists whenever future supply or demand for a product or service is unknown or uncertain. Few industries are as familiar with this risk as the power industry, where future demand can be especially hard to gauge. The amount of power consumed in a particular area can vary dramatically from day to day, week to week, month to month and year to year.

A great degree of this variation in demand can be attributed to the key variable of weather. Certainly, demand for power can move up or down due to the health of the economy, demographic changes, and other factors, but weather has the largest and most direct impact. The fact of the matter is, as temperatures move up and down, so too do people's thermostats.

Planning for and managing volumetric risk is critical for companies in the power industry. This is because, like many other commodities, changes in the price of electricity are tied to changes in its supply and demand equation. The price a company pays or receives for electricity will change, often dramatically, if demand levels are higher or lower than expected or shifts in demand occur at different times or in different locations than expected. Revenues, costs and earnings can all be affected as a result.

Because it has such a strong influence on demand, weather has to be accounted for if power companies are to effectively mitigate their volumetric risk exposure. There are a couple of ways they can do this.

Weather Derivatives

The use of financial instruments like weather derivatives are one alternative. In the power industry, weather derivatives are most often tied to temperature indices such as heating degree-days (HDD) or cooling degree-days (CDD). These weather derivatives, which usually take the form of swaps, collars, puts or calls, give companies protection by offering them a hedge against warmer- or cooler-than-normal weather.

For example, an electric utility could hedge against a cooler-than-normal summer by purchasing a CDD put option. If temperatures end up being cooler than normal and the number of CDD falls below the predetermined level, the utility would receive a cash payment, helping offset lost revenue. If temperatures end up being warmer than normal and the number of CDD exceeds the predetermined level, the utility would forfeit the premium it paid for the option, but capture additional revenue as a result of the warmer weather.

Besides helping power companies address revenue at risk, weather derivatives can also be useful for managing costs. A power producer, for example, can use weather derivatives to help counteract higher prices for generation fuels like natural gas.

But weather derivatives do have some disadvantages. To start, the market for weather derivatives is only a few years old and still evolving. Although liquidity is improving, price discovery can be difficult and significant price variances can exist. To a large extent, weather derivatives are still priced at the whim of traders and because of this companies may not end up getting the level of the downside protection they require.

And while weather derivatives can help companies hedge sales volumes and costs, their value when it comes to business planning and decision-making is limited.

Weather derivatives do not help a utility determine the best times to take plants out of service for maintenance. Weather derivatives do not help a company make better buying, selling and trading decisions regarding power and fuels. Weather derivatives do not help companies identify and plan for additional revenue opportunities that can arise from unexpectedly high demand. Weather derivatives do not help a company more accurately forecast future demand.

Long-Range Forecasting

The other approach that power companies can take to manage their volumetric risk involves forecasting what the weather will be in the future and projecting its impact on demand. Advances in the science of long-range climate prediction have made this possible and have greatly enhanced the accuracy of seasonal demand forecasts.

Long-range climate forecasts make no attempt to predict specific daily or hourly weather conditions and instead focus on identifying large-scale atmospheric systems that move around the earth and the sequences in which they occur. Long-range climate forecasts aim to project the degree to which temperatures and precipitation will vary from normal in the future. The goal of this forecasting approach is completely different than that of the conventional short-range forecasts, which look to make very specific temperature and precipitation projections for specific locations. Short-range forecasts are good at predicting weather over the next few days, but the data that is analyzed and the computer models that they use produce less and less accurate forecasts for each day further out in time they go. Long-range climate forecasts offer fewer specifics but they do not degrade over time.

With the emergence of reliable seasonal climate forecasts, power companies can now know—months ahead of time when, where, and by how much demand for power will change.

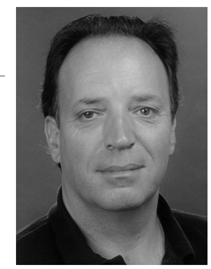
This information can help companies reduce their volumetric risk. If sales volumes are expected to be lower, costs can be scaled back to preserve earnings. If future weather conditions are likely to increase fuel costs, companies can lock in purchases now at lower prices.

A more accurate forecast of future demand can be very valuable to companies in their planning and decision-making processes.

A clearer picture of future demand will help with operational decisions such as when to schedule plant maintenance or when to bring peaking units on line. From a financial planning standpoint, this information can help companies more accurately project future revenue, cash flow and earnings. This enables companies to provide better guidance to the financial community.

This information can also put companies in a better position to take advantage of opportunities that arise out of demand volatility. A power producer, for example, could identify periods of time when additional power could be generated for sale at high market prices. It can also help companies optimize their trading and hedging activities by helping them determine the best times to buy or sell physical power, power derivatives, physical fuel and fuel derivatives.

Both weather derivatives and long-range weather intelligence can help power companies address volumetric risk. Weather derivatives act like a form of insurance. If one gets into a car accident, they will get money to help repair the damage. But it is always better to see the road ahead and avoid the accident altogether. Demand forecasts that incorporate long-range climate forecasts can provide this type of insight, giving companies options and the ability to change course while there is still time to act. In the end, this is the best way to manage volumetric risk, lower costs and maximize revenues and profits.



This week's Financial Focus was written by **Paul M. Corby**, *senior v.p. responsible for the energy industry business unit at* **Planalytics** *in Wayne, Pa. Corby can be reached at contact@planalytics.com or 610-640-9485.*

Weekly Recap

The Weekly Recap is a summary of publicly reported power news stories. The information has been obtained from sources believed to be reliable, but PFR does not guarantee its completeness or accuracy.

Asia

• The privatization of South Korea's electricity sector is likely to be delayed after U.S. power giant **Mirant**'s recent decision to ditch plans to enter the market. The Atlanta-based company last month reversed its plans to invest $300 million in the Korean power industry, and said it would sell its rights to build a 520 MW plant (*Reuters*, 8/5).

Europe, Middle East & Africa

• **Gerhard Goll**, chief executive of **EnBW**, Germany's third largest utility, has criticized plans to allow **E.on** to acquire **Ruhrgas** for $10 billion. Goll said conditions attached to the deal are insufficient to stimulate competition and was also critical of the deal being brokered "behind closed doors" (*Financial Times*, 8/7).

• **Enron Teesside Operations** (ETOL) has been put on the block three-and-a-half years after it was acquired from **ICI** for GBP300 million ($459 million). The 465 acre site, which is jointly owned by the European arm of **Enron** and U.S. financial institutions, provides utility and support services to several bulk chemical manufacturers. **Close Brothers Corporate Finance** has been appointed by ETOL's shareholders and lenders to find a buyer (*Financial Times*, 8/6).

• The **Ethiopia Electric Power Corp**. plans to establish hydroelectric power stations in the country's north and southwest at a cost of $600 million (*BBC Monitoring Africa*, 8/6).

• A German court has upheld a temporary injunction against **E.on**'s takeover of gas outfit **Ruhrgas**, stalling the utility's European gas expansion plans and casting doubt over the future of chemicals firm **Degussa**. The decision puts on ice two deals together worth almost EUR15 billion ($14.84 billion), both of which are key to E.on becoming a leading global power and gas player. E.on brokered a deal earlier this year to transfer control of Degussa, its biggest non-core asset, to coal group **RAG**, but made this dependent on closing the Ruhrgas deal (*Reuters*, 8/5).

• **Centrica** has increased its share of the U.K. power market through the purchase of **Electricity Direct**, a power retailer, for GBP 49.5 million ($77.4 million) in cash and GBP13.5 million of debt. The deal gives Centrica close to 20% of the U.K.'s commercial supply market behind **RWE**'s **NPower** and **Electricité de France**'s **London Electricity** (*Reuters*, 8/5).

• French trade unions called on Tuesday for protests on Oct. 3 after talks with ministers failed to stem their hostility to plans to partially privatize state-owned electricity and gas utilities **Electricité de France** and **Gaz de France**. French Finance Minister **Francis Mer** on Monday ended a round of preliminary talks with labor union leaders who fear that the public service and jobs are threatened by sales of stakes in EdF and GdF (*Reuters*, 8/6).

• The U.K.'s system for trading green certificates, as proof of compliance with a countrywide rule that 3% of all electricity supplied to customers be from renewable sources, went live late Monday. As part of the effort energy regulator **Ofgem** opened a Web site with an online register of renewables obligation certificates. The U.K.'s "Renewables Obligation," which came into effect in April, requires electricity suppliers in the U.K. to buy 3% of the power they sell to customers from renewable sources or pay a GBP30 penalty for each MWh that they fall short. That requirement will rise to 10.4% by 2011 (*Dow Jones*, 8/6).

• Danish utility **NESA** has bid to buy regional rival **Nordvestsjaellands Energiforsyning** for $340.6 million in order to strengthen its position ahead of the deregulation of the Danish electricity market next year. NVE has 117,000 customers. "NESA aims to reach one million end-customers from around 530,000 at present," NESA said in a statement (*Reuters*, 8/6).

U.S. & Canada

• Lenders have given **PG&E Corp**. until Aug. 16 to renegotiate around $1 billion in loans affected by the debt rating downgrade of its PG&E National Energy Group energy trading subsidiary. The San Francisco-based company said it had been granted a waiver on a provision in the loans, which required that the subsidiary maintain an investment grade debt rating with one of the two main rating agencies. **Moody's Investors Service** last Monday cut its rating on the unit to junk status. **Standard and Poor's** cut the unit's rating to junk the previous week (*Reuters*, 8/5).

• **Bruce Power** expects to restart two 750 MW units at its Bruce A nuclear power station in time to meet next summer's peak electricity demand, several months ahead of its earlier schedule. Company officials said the earlier restart was due to an accelerated hearing schedule with Canadian energy regulators (*Reuters*, 8/5).

• **Chesapeake Energy** plans to raise $250 million in the private debt market to fund acquisitions and repay debt. The company is offering senior notes due in 2012, with net proceeds earmarked to pay for three pending acquisitions totaling $132 million, plus a planned $38 million purchase of Oklahoma natural gas properties from **Williams Co.s** (*Reuters*, 8/5).

• Energy firms and California officials, in a final round of talks to renegotiate $43 billion in electricity contracts, faced a Tuesday deadline when a **Federal Energy Regulatory Commission** judge will unveil settlements or schedule an agency hearing. California wants to renegotiate long-term contracts it signed last year with more than 20 companies at the height of the state's electricity crisis (*Reuters*, 8/5).

• Power producer **Mirant** says the **Securities and Exchange Commission** has launched an informal inquiry into possible sham energy trades and its accounting practices, the latest tremor to shake the energy sector in the wake of **Enron**'s demise. Mirant, which disclosed last week it overstated the value of some assets and liabilities, also said the SEC's Atlanta office is investigating energy-trading practices in the western U.S. and asked for information on shareholder suits against Mirant (*Reuters*, 8/5).

• Independent power producer **Calpine** and a unit of **Cleco** said Monday they began operations at the 1,160 MW gas-fired Acadia power plant in Eunice, La. In a statement, Calpine said the plant, a joint venture with **Cleco Midstream Resources**, began operating in time to meet peak summer demand in the U.S. Southeast (*Reuters*, 8/5).

• **Aquila** has ditched efforts to find a partner for its wholesale energy group and will instead close its trading operation. Commodities trader **Louis Dreyfus** and Chicago hedge fund **Citadel Investments** had initially shown interest in partnering to bolster the business, but Aquila's credit woes and the departure of some of its top traders created too many problems for the potential partners (*Reuters*, 8/6).

• The **Securities and Exchange Commission** has begun an informal inquiry into $250 million in accounting irregularities at **Mirant** that took place in 2001. The Atlanta IPP said the inquiry relates to the overstatement of an $85 million gas-inventory asset, a $68 million accounts-receivable asset and a $100 million accounts-payable asset. The company received a letter from the SEC last Friday, and decided to disclose it (*Wall Street Journal*, 8/6).

power finance & risk

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PFR - JUNE 24

BofA REPORTEDLY READIES POWER TRADING; HIRES ENRON QUARTET

Bank of America is reportedly planning to establish an electricity derivatives trading desk in New York and has landed four former Enron traders to staff the operation. The quartet consists of **Rogers Herndon**, who heads the team, **Gautam Gupta**, **John Suarez** and **Paul Broderick**, according to market officials. **David Mooney**, global head of commodities, referred calls to BofA's media relations department. **Jeff Hershberger**, a spokesman in New York, says BofA is not currently a participant in the power derivatives market and does not comment on future business plans. Herndon referred calls to Mooney.

The four were recipients of retention bonuses paid to key Enron staff to keep the company's trading operation afloat prior

JUNE 28

REUTERS .com

Bank of America gets OK to trade electric derivatives

WASHINGTON, June 28 (Reuters) -

The government this week approved a request by Bank of America Corp. to trade in the vast electricity derivatives market, marking the first time that a bank has entered this market.

The Office of the Comptroller of the Currency (OCC), an arm of the U.S. Treasury Department, on Thursday issued a letter ruling that it is permissible for the Bank of America "to engage in financial intermediation transactions, where the payments between parties are based on the price of electricity."

The approval could open the door for other banks to enter this market. They would have to request permission to trade electricity derivatives, an OCC spokesman told Reuters.

A Bank of America spokesman confirmed that it intends to trade electricity derivatives, and has hired an undisclosed number of traders to man a trading desk, including some traders from now-bankrupt energy trading giant Enron Corp .

"It's an obvious next step. We've been in the commodities derivatives business for some time," including crude oil and natural gas, the spokesman said. The move is a response to a request from wholesale energy buyers and sellers, he said.

Derivatives are private transactions between companies and financial firms used to manage risks in interest rates, currencies and commodity prices.

Enron previously dominated the market for over-the-counter electricity derivatives, after it spearheaded a heavy congressional lobbying effort to leave that market unregulated by the Commodity Futures Trading Commission (CFTC).

PFR - MAY 27

MORGAN STANLEY HONCHO JOINS TOP-RANKING HEDGE FUND ...

Andy McMillan, head of European power and gas trading at Morgan Stanley in London, has left the bank to join **Tudor Investment**, one of the world's largest and most renowned hedge funds managers with more than $6 billion in assets. McMillan, a native New Zealander whose background is in oil and energy options, left the U.S. investment bank last month and has already taken

June 7

THE FINANCIAL TIMES

GLOBAL INVESTING: Hedge funds move in on distressed energy sector

By Robert Clow in New York
Financial Times; Jun 07, 2002

Smart investors love a little carnage, so it shouldcome as no surprise that some of the smartest hedge fund investors are getting into the energy market following the collapse of Enron and the admission by its competitors of bogus trades to boost revenues.

Two hedge fund giants, Citadel Investments and Tudor Corp, have started to build up energy trading teams and a smaller fund, Catequil Asset Management, is also understood to be seeking a energy trading professional.

www.iipower.com - MAY 10

NATIONAL GRID EYES NORTHEAST UTILITIES TIE-UP

U.K. transmission monopoly National Grid has been holding merger discussions with Northeast Utilities for the past few months and is planning to swoop for the U.S. utility toward the end of this year following the completion of its announced tie-up with **Lattice**, a U.K. monopoly gas pipeline business. A banker close to the negotiations says Northeast Utilities has retained **Morgan Stanley** to advise on the deal, but he declined to name National Grid's advisor.

Jackie Barry, a spokeswoman at National Grid in Westborough, Mass.,

May 13

DOW JONES NEWSWIRES

Natl Grid Merger Talks With US Utility Co-Report

LONDON -(Dow Jones)- U.K. power transmission company **National Grid** Group PLC (NGG) has been holding merger talks with Northeast Utilities (NU) of the U.S. and expects to complete a deal at the end of the year, an industry newsletter reported Monday.

A deal with West Springfield, Mass.-based Northeast Utilities is likely to go through after **National Grid** completes its merger with U.K. infrastructure company Lattice Group PLC (U.LTI) in the autumn, Institutional Investor Inc.'s Power Finance & Ris newsletter reported.

In the past two years, **National Grid** has spent $6.2 billion buying two electricity utilities in the New England market. The U.K. company says the purchases have positioned it as one of the top 10 electricity companies in the U.S.

A **National Grid**-Northeast Utilities union would create a $21 billion energy concer given the two companies' current market capitalizations, Power Finance & Risk reported.

GAZ DE FRANCE

(continued from page 1)

Gas, Power and Renewables division, and **Jeremy Wilson**, head of power at J.P. Morgan, did not return calls.

Sabine Wacques, a GdF spokeswoman, declined to comment on Great Yarmouth, but admits the state-owned gas monopoly wants to get into the power generation business. "We realize that most of the growth in gas consumption in Europe over the next 20 years will come from power generation, so it's an area we are interested in."

GdF does not own any power plants either in the U.K. or elsewhere, but is looking to both develop its own gas-fired generators and enter gas supply or tolling contracts with unaffiliated plants, says Wacques. The company is presently developing two power projects in Spain and France and has entered a supply contract with U.S. power producer **AES** for a plant it is developing in Spain (see story, page 1).

A banker in London says it is unclear which other companies have looked at, or may bid for, the BP asset. But, he argues, GdF's control of large gas fields off the U.K. coast and its ownership of gas pipelines in the area likely give it more reason than most to bid for the plant.

—Will Ainger

Financing Record (AUGUST 1 - AUGUST 8)

Bonds

Issue Date	Maturity	Issuer	Amount	Offer Price	Type of Security	Coupon (%)	Spread To Treasury	Moody's	S&P	Bookrunner(s)
08/02/02	08/09/17	EDP Finance	312.2	98.936	Fxd/Straight Bd	6.625	180	A2	A+	Deutsche/Goldman/UBS
08/06/02	02/13/04	RWE	49	100.045	Mdm-Trm Fl Nts	Floats	-	A1	A+	Lehman

M&A

Date Announced	Date Effective	Target Name	Target Advisors	Target Country	Acquiror	Acquiror Advisors	Acquiror Country	Value ($mil)
08/01/02	-	Gelsenwasser (E.ON)	-	Germany	RWE	-	Germany	-
08/01/02	-	Kraftwerk Laufenberg(Watt AG)	-	Switzerland	Enalpin	-	Switzerland	-
08/02/02	-	Blackstone Station	-	U.S.	Harvard University	-	U.S.	14.6
08/05/02	08/05/02	Electricity Direct	-	U.K.	British Gas Trading(Centrica)	-	U.K.	98.916
08/05/02	08/05/02	Thuega	-	Germany	E.On	-	Germany	-
08/05/02	08/05/02	Zeag Zementwerk Lauffen	Dresdner Kleinwort Benson	Germany	Energie Baden-Wuerttemberg AG	-	Germany	-
08/06/02	-	Nordvestjaellands Energi	-	Denmark	NESA	-	Denmark	337.664

Source: **Thomson Financial Securities Data Company**. For more information, call **Rich Peterson** at (973) 645-9701.

AES LOOKS

(continued from page 1)

Financing of the Cartagena combined-cycle gas turbine project was originally set to occur early last year (PFR, 1/8/01), but, like other CCGT projects on the Iberian peninsula, became bogged down over gas supply issues, namely the difficulty of getting gas from the coast to the plant. Turmoil in the IPP sector since the collapse of **Enron** has also hindered AES' ability to raise financing.

Credit concerns over AES—the company was downgraded two notches to a junk rating of Ba3 late June by **Moody's Investors Service**—mean the role of triple-A rated GdF has become pivotal to the deal's success, says one banker, who notes the project was originally envisaged as a merchant operation.

However, even the support of a top-notch offtaker may not guarantee the success of the deal. AES' decision to walk away from the 363 MW Fifoots Point coal-fired plant in Wales this spring (PFR, 4/1) and leave the plant's financiers and a bankruptcy administrator to restructure the deal, has left a bitter taste in the mouth of many lenders. Those lenders are facing a financial loss on Fifoots and are unlikely to be lining up for more AES paper, say lenders.

Sabine Wacques, a GdF spokeswoman, confirmed the utility has signed a contract to supply liquified natural gas to the plant, but declined further comment. Calls to **Kenneth Woodcock**, a spokesman at AES, were not returned. Lenders pitching for the deal either declined to comment or did not return calls.

—W.A.

DOMINION SEEN

(continued from page 1)

A tie-up between Dominion and Allegheny would create a $19.1 billion energy concern, given their current market values of $16.7 billion and $2.4 billion, respectively.

Calls to **Thomas Farrell II**, ceo of Dominion, were not returned. **Tom Caps**, chairman, could not be reached as he was traveling on business. **Mark Lazenby**, a Dominion spokesman, and **Janice Lantz**, a spokeswoman at Allegheny, declined to comment.

"It makes a ton of sense," says one banker commenting on the potential merger. "Allegheny has gotten beaten up in this market and Dominion is a utility in good shape. Since it was interested in Allegheny before, now would be a good time to get the deal done."

While a previous merger discussion between Dominion and Allegheny two years back never resulted in a deal being announced, bankers say the firms have held low-level discussions intermittently since then. The new round of talks have stepped up a pace, they add.

Prior to the downturn in the power sector, Dominion's strategy was to acquire generation assets primarily in the MAIN to Maine region. But officials say it has decided to expand this strategy to include acquiring an entire company in light of the current state of the market.

Allegheny has announced one merger previously. In 1997 it agreed to a tie up with **DQE**, but the parent of **Duquesne Light** terminated the deal shortly thereafter, citing a restructuring order of the **Pennsylvania Public Utility Commission** that it claimed violated the merger approval process.

—Amanda Levin

CLECO, CALPINE

(continued from page 1)

difficult," she admits.

The mandate for the financing was awarded to **Société Générale** and **Fortis Capital** in May last year, but the Eunice, La., development ran into litigation over water and emissions permits, stalling any chance of getting the deal done at the time. Earlier this year as the litigation headed toward a resolution, the partners had been hopeful of securing stronger pricing for a deal free of construction risk (PFR, 1/21). But, with the sector in a tailspin in recent months, the focus now is on dealing with credit risk within the tolling agreements, Nolan says. To counteract credit problems Acadia investigated whether insurance could be used to mitigate the tolling counterparty risk, but that proved uneconomic, she explains. Adding a guarantee from the sponsor also wasn't an option because that would have negated the non-recourse objective of the financing, she adds.

—Peter Thompson

Quote Of The Week

"It's going to be difficult."—**Kathleen Nolan**, *treasurer at **Cleco** in Pineville, La., anticipating tough market conditions for refinancing a 1,160 MW power plant (see story, page 1).*

One Year Ago In Power Finance & Risk

PG&E National Energy Group launched a $1.7 billion non-recourse loan to fund the construction of four plants. [After bagging $1.075 billion in the wholesale round, the deal only booked $385 million in retail. But, that was enough to cover all four plants and after the downturn in the fourth quarter bankers said expectations had been scaled back (PFR, 5/6).]