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A Chilean Pure Play

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As a first-time bond issuer in Chile last year, the Canadian utility Hydro-Québec International lacked a track record with investors who typically buy Chilean paper. But by aggressively marketing the low- risk and high-cash flow features of Transelec, its Chilean transmission company, HQI managed to set the pace for corporate bond issuers when it raised $715 million in a simultaneous offering on international and local markets.

The local offering was the largest-ever corporate bond issue in Chile and the international tranche was two times oversubscribed. In addition, Transelec's dollar-based and Chilean peso revenues neatly hedged the new loan's payment structure. The revenues from the bond took out an acquisition bridge loan that HQI had secured to buy Transelec.

In mid-April, Transelec placed a $465 million, 10-year, 144a bond with a 7.875% coupon priced at 309 basis points over US Treasurys. It also issued the local currency equivalent of $265 million in inflation-linked bonds in two series - a six-year, $180 million series and a 21-year, $3.2 million series - each carrying a 6.2% coupon. The local issue remains the largest financing for a Chilean utility to date and has become a benchmark for Chilean corporate bond investors. This, and the bond's innovative dual currency structure make it the winner of LatinFinance's local currency corporate bond of the year.

HQI issued the bonds to help take out the acquisition financing for its $1.06 billion purchase of Transelec in November 2000 from the Chilean subsidiary of Endesa Spain. Transelec needed to replace a $724 million, 364-day term loan with a debt package that reflected its revenue stream, 72% of which is in Chilean pesos and 28% that is dollar-linked.

Dollar investors liked the bond's strong credit rating - all three major rating agencies assigned it an investment-grade rating. They were also attracted by Transelec's concentration in energy transmission, considered the least risky part of the energy business.

"It represented value and relatively low risk, and we were compensated for whatever risk there was," says Violet Osterberg, director of private placement, for Pacific Life, an insurance company that bought $11 million of Transelec bonds.

Transelec's strong local cash flow also gave it an edge. Transelec had a pre-tax earnings margin of 85% in 2001. "The bond really distinguished itself as a pure play in Chile," says Christopher Gilfond, managing director and co-head of Latin debt capital markets at Citigroup. "From an international perspective, this bond was sold in the context of a fairly solid environment for Chile but there was a lot of noise in the region, especially in Argentina."

In addition, just days before Transelec issued the bond, Standard and Poor's lowered the currency ratings of Transelec's main customer, Endesa Chile, because of the company's earnings volatility in non-Chilean countries. Investors shrugged off the news and the bond attracted $1 billion in orders. "Transelec is a very stable generator of cash flow, with assets in the least-risky part of the energy business and it benefits from operating in a good regulatory framework that is sound and allows you to earn a decent return," says Paul Robillard, treasurer of Hydro-Québec.

Chilean pension funds, mutual funds and local banks bought the $180 million, local currency six-year bullet series. Robillard says the Transelec bond provided an opportunity for local investors to diversify their energy credits. "They had been exposed to the distribution and generation sides and this was a chance to be exposed to the transmission side," he says.

Chilean banks were keen to participate in the sale as well since they were eager to cultivate a relationship with HQI as a potential bank customer. "There was a lot of appetite from banks that came into the short series," says Juan Carlos Cavallini, vice president and co-head of corporate finance at Citigroup Chile. "They wanted to be visible to HQI for cross-selling opportunities."

Cavallini says that the successful local placement has encouraged other issuers to float bigger deals. "It was very good for the market in terms of developing the size of deals," says Cavallini.

Transelec could have upsized the international portion of the deal, but the issuer wanted to maintain a loan structure that mirrors its revenues and preserve the currency hedge.

Another notable corporate bond issue last year that preceded the Transelec issue was Telefonos de Mexico's five-year, $1 billion global offering in January. The debut bond transaction for Telmex, joint lead managed by JP Morgan and Merrill Lynch, was the largest-ever straight bond issued by a private-sector Latin American company.

Coming in late in the year was a $500 million December issue from the Brazilian beverage company Companhia Brasileira de Bebidas (CBB) underwritten by UBS Warburg. The bond was backed by a political risk insurance policy, and a reserve fund and was guaranteed by Companhia de Bebidas das Américas (AmBev), the parent company of CBB.