www.pwc.com/tr/energy

Energy Deals

Merger and acquisition activity in Turkey's energy market

2011 Annual Review

In Turkey for 30 years

pwc

Contents

Methodology and terminology

Energy Deals 2011 includes analyses of cross-border and domestic deal activity in the oil, gas and electricity markets in Turkey. The analyses are based on publicly available information and encompass announced deals as of 31 December 2011, including those pending financial and legal closure. Deal values are the consideration value announced or reported while the figures relate to actual stake purchases and are not multiplied to 100%. All presented totals of deals include estimates for deals with no reported value. This document is also available at *www.pwc.com/tr/energy*.

Welcome
to our fourth edition of Energy Deals, our annual analysis of mergers and acquisitions in the Turkish energy market

Faruk Sabuncu
Energy, Utilities and Mining Leader

Engin Alioğlu
Partner, Deals

In our Energy Deals 2010 report we warned that debt financing would be more difficult to secure in the wake of the global financial crisis, and investments would require more equity. Indeed, it is not surprising that the M&A activity in 2011 was significantly lower than that recorded in 2010, at a total deal value of US$ 1.2bn, going back to levels that we have not seen since 2007.

The troubles that prevented successful closure of power distribution privatisation tenders haunted the utilities deal environment in 2011. The reasons behind these problems were the high deal values and difficulties with financing. The privatisation of generation assets also did not start in 2011 as planned due to the delays with the closure of distribution tenders as well as regulatory uncertainties. The tender for the Hamitabat plant was cancelled when it received only one bid. We see the successful deal closure of a generation privatisation in 2012 to be unlikely, but regulators can turn these delays into advantages by taking the necessary steps to eliminate regulatory uncertainties.

On the gas distribution front, the privatisation tenders of Başkent Gaz and IGDAŞ may have greater chances of success due to reported foreign interest, but financing may still constitute to be a problem.

Fuel distributors have been facing shrinking margins due to a ruling by the Competition Authority in 2010 as well as the EPDK's repeated calls urging them to align their margins with the European average. These pressures will not subside any time soon. We expect a greater preference for the COCO and CODO model among distributors in 2012. However, the high investment need for the popular spots and the high cost of available land remain as important obstacles to rapid expansion through this model.

Looking into the future, we by and large see tighter market liquidity translating into tougher financing. Coupled with regulatory uncertainties, financing difficulties render deal expectations for 2012 more conservative. However, the growing domestic demand and investment need as well as the large portfolio of energy assets lined up for privatisation give us some hope for a livelier deal environment and greater deal totals in 2012.

Deal totals: 2011 far behind 2010

The deals in 2011 did not come close to reaching the record-breaking deal values announced in 2010.

The total deal value in 2011 was $1.2 billion as opposed to $17.2 billion in 2010. Furthermore, fewer deals took place in 2011, only 29 versus 53 deals in 2010. The average deal value declined from $325 million in 2010 to $43 million in 2011. 2010 is probably not a healthy benchmark given that some of the large power distribution privatisations and the sale of Baskent Gaz could not be finalised subsequently. We have not restated our figures for 2010, as our methodology rests on announced deals regardless of whether they are financially and/or legally closed. Nonetheless, even if we take into account only the value of the 2010 deals that have been closed, we land at a figure of $6bn, approximately five times the 2011 deals total.

Twenty-four deals in the utilities sector had an estimated total value of $1 billion, and an average value of $42 million. Delays in the privatisation of power and gas distribution companies created a backlog. Tenders for power generation companies and IGDAŞ, the Istanbul gas distribution company, were also delayed. The tender for the first generation asset in the privatisation portfolio, the Hamitabat plant, had to be cancelled when it received only one bid.

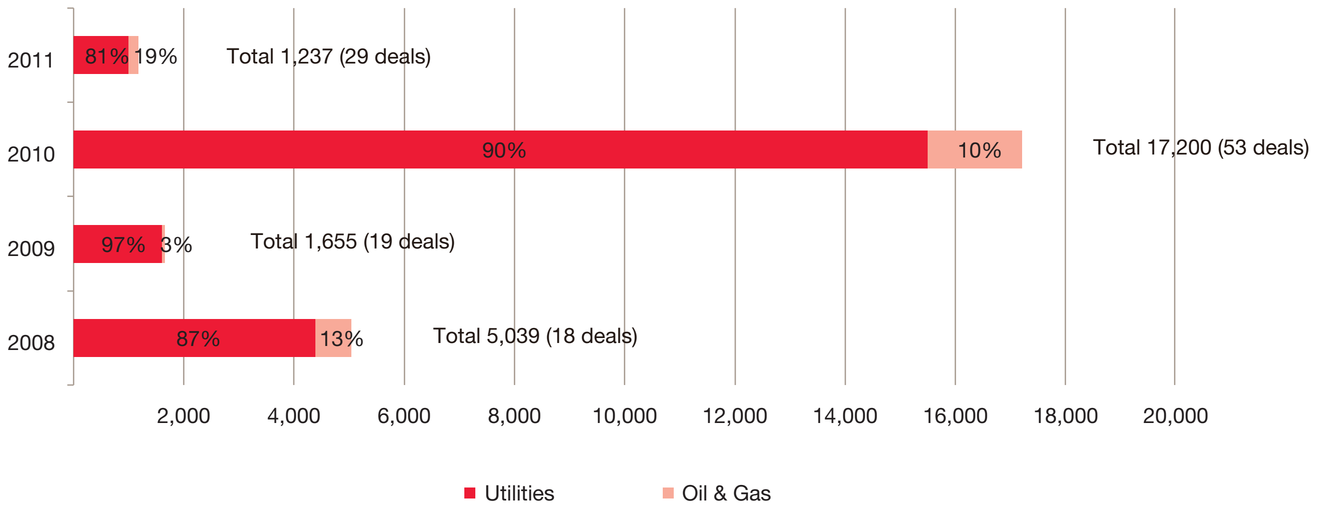
The oil and gas sector hosted five deals with a total deal value of $237 million in 2011. Although the consolidation and vertical integration activity we were expecting in the downstream fuel sector did not occur in 2011, deal activity in this segment is more likely going forward. Instead, we observed deals in the downstream LPG and E&P segments. Transatlantic Petroleum increased its presence in Turkey even further with the acquisition of Thrace Basin Natural Gas Türkiye Corporation and Pinnacle Turkey Inc.

Even if we take into account only the value of the 2010 deals that have been closed, we observe that 2011 was a much slower year than 2010

Figure 1: Total Energy Deals in 2010 and 2011

	FY10			FY11			YoY change	
	Number	Value (US$ mn)	Average Value	Number	Value (US$ mn)	Average Value	% number	% value
Utilities	48	15,500	323	24	1,000	42	-50%	-94%
Oil and Gas	5	1,700	340	5	237	48	-	-87%
Total	**53**	**17,200**	**325**	**29**	**1,237**	**43**	**-45%**	**-93%**

Figure 2: Total deals between 2008 and 2011 by value ($ mn) and number of deals



As no new privatisation tenders took place in 2011, the public-private deals split shifted completely in favour of private deals. The share of private deals by value increased from 18% in 2010 to 95% in 2011. The most anticipated private deal of the year was the sale of Akenerji, but the owners of the company, Akkok and CEZ, have recently announced that they are calling off the sale.

95% value generation for private deals versus **5%** for public deals

42% local involvement versus **58%** foreign

Foreign interest in the Turkish energy sector, although at a higher weight than in the last two years, remained limited in terms of value due to regulatory uncertainties and difficulties in the global financial markets. Foreign deals were fewer in number but higher in value compared to local deals. On the utilities front Goldman Sachs, Ansaldo Energia and Hot Rock invested in Aksa Enerji, Yeni Elektrik Üretim and Enda Enerji, respectively. Transatlantic Petroleum increased its presence in the upstream oil sector by acquiring two Turkish companies.

Utilities: Broken dreams

Privatisation tenders for power distribution companies made 2010 an exceptional year. Most of these deals, however, could not be finalised in 2011.

Out of the eleven privatisation tenders for power distribution companies in 2010, only Uludağ, Çamlıbel, Fırat and Vangölü were transferred to their new owners in 2011. The transfer of Trakya to IC İçtaş was announced in the first days of 2012, whereas the process is ongoing for Istanbul Anadolu Yakası, Toroslar, Boğaziçi and Dicle. A new privatisation tender will need to be held for Akdeniz and Gediz. Not all news was bad news, though: An exceptional transaction in 2011 was the transfer of Göksu to AKEDAŞ 13 years after the privatisation tender was held.

Prospects of power distribution deals still unclear

Figure 3: Remembrance of bidders in the power distribution tenders

Distribution company	Bidders withdrawn from the process	Bidder in the process	Current Bid ($ mn)	Who is next?
Akdeniz	1. Park Holding 2. EnerjiSA 3. EMKAT Ortak Girişim Grubu	-	-	-
İstanbul Anadolu Yakası	1. MMEKA 2. Yıldızlar SSS Holding 3. EnerjiSA	Aksa	1,459	Cengiz-Kolin-Limgaz
Toroslar	1. Yıldızlar SSS Holding 2. Park Holding 3. Türkerler	Cengiz-Kolin-Limgaz	1,952	EMKAT
Gediz	1. Eti Gümüş-Söğütsen Seramik 2. EnerjiSA	-	-	-
Boğaziçi	1. İş-Kaya - MMEKA 2. Aksa	Park Holding	2,496	-
Dicle	-	Karavil-Ceylan	228	1. Çalık 2. Eti Gümüş - Söğütsen Seramik

In our report last year, we warned that debt financing would be harder to secure than it was before the financial crisis, and investments would require more equity. Indeed, difficulties with financing and US$ appreciation against TL over 2011 turned out to be the main reasons behind bidders' inability to follow through on their commitments. The strategic preferences of bidders also played a role in the progress of some tenders, as bidders gave up on one distribution company to increase their chances of acquiring another.

As previously, two tenders will be organised for Başkent Gaz: the Privatisation Administration is putting 80% of the company up for sale and the deadline for bids has been announced as 27 January 2012. The Ankara municipality has organised a separate tender for the remaining 20% stake in the company, with the bid deadline set for 16 February 2012. If Başkent Gaz tenders are finalised successfully, next in line for privatisation is IGDAŞ, the Istanbul gas distribution company. One important factor for the privatisation of these two – the two largest gas distribution companies in Turkey – will be the new tariff methodology that is being drawn up by the EPDK. The methodology will be used to determine the components of the gas distribution tariff after the first eight years following the privatisation of gas distribution companies.

Figure 4: Utilities deals in 2011

Date Announced	Target	Stake %	Acquirer	Acquirer Nationality	Deal Value US$ mn
1-Jan-11	Göksu EDAŞ	100%	AKEDAŞ	Turkey	60.0
14-Jan-11	Ata Elektrik	68%	Verusa Girişim	Turkey	n.d.
20-Jan-11	Energaz	47%	Enerji Yatırımları Holding	Turkey	n.d.
1-Mar-11	Aksu Temiz Enerji	70%	Ayen Enerji	Turkey	6.7
4-Mar-11	IBA Elektrik Uretim	100%	EnerjiSA	Turkey	n.d.
5-Apr-11	BND Elektrik Uretim	67%	Metem Enerji	Turkey	7.6
5-Apr-11	Ayres Ayvacik	99%	Aksa Enerji	Turkey	2.2
18-Apr-11	Alpaslan II Enerji	100%	EnerjiSA	Turkey	8.9
23-May-11	Naturelgaz	50%	Enerji Yatırımları Holding	Turkey	10.8
24-Jul-11	Yeni Elektrik Uretim	40%	Ansaldo Energia	Italy	122.2
25-Jul-11	MMEKA	50%	Mehmet Kazancı	Turkey	n.d.
26-Jul-11	Galata Enerji	20%	Global Enerji	Turkey	n.d.
2-Aug-11	Mersin Kojenerasyon	>30%	Soda Sanayi	Turkey	n.d.
4-Aug-11	AES Entek	25%	Koc Holding	Turkey	74.8
5-Aug-11	Tekkale	100%	Nuh Cimento	Turkey	0.1
5-Aug-11	Kuyuma Elektrik	51%	Enso Hydro	Austria	0.1
22-Aug-11	Alenka Enerji	76%	Aksa Enerji	Turkey	2.4
19-Oct-11	Bordo Mavi Enerji Elektrik	100%	Trabzonspor SK	Turkey	n.d.
28-Oct-11	Aksa Enerji	15%	Goldman Sachs	USA	268.0
31-Oct-11	Aksa Goynuk Enerji Üretim	100%	Aksa Enerji	Turkey	0.7
22-Nov-11	Ortadoğu Enerji Sanayi	20%	Kapital Yatırım	Turkey	24.6
21-Dec-11	Metem Enerji	25%	Turkraft Holding	Turkey	21.5
22-Dec-11	Meltem Enerji	87%	Gurtas	Turkey	2.9
23-Dec-11	Enda Enerji	100%	Hot Rock	Germany	143.6
Total					**≈ 1,000***

n.d. not disclosed
** Includes estimated deal value for undisclosed deals*

As the closure of distribution deals proved out to be more complicated than expected, the privatisation of state-owned power generation portfolios were further delayed in 2011. The Privatisation Administration cancelled the tender for gas-fired Hamitabat (1,120 MW) in October when the plant attracted only one bid. According to the strategy announced by the Privatisation Administration in early 2010, the privatisation of generation assets is a big enterprise: The overall portfolio consists of 27 hydro plants with a total capacity of 3,677 MW and 18 thermal plants with a total capacity of 11,769 MW. After Hamitabat, lignite-fired Soma A-B (1,034 MW), Can (320 MW) and Seyitomer (600 MW) are expected to be privatised. The remaining 41 plants, which range between 356 MW and 2,795 MW, are divided into nine portfolios. Portfolio companies will hold the operating rights for the hydro plants and ownership of the thermal assets.

In last year's Energy Deals we highlighted the opaque regulatory landscape as a potential obstacle for generation privatisations. Unfortunately no steps were taken in 2011 to eliminate regulatory uncertainty. Currently state-owned power plants under EUAS hold contracts with Turkish Electricity Trade and Contracting Co (TETAS) and distribution companies, but these will expire at the end of 2012 and it is unclear what will replace them. There is also uncertainty regarding fuel supply options and possible limitations as well as modernisation and expansion commitments that investors will be required to undertake.

Failure to launch the long-awaited power generation privatisations

Oil and gas: Calm before the storm

Just like the utilities sector, 2011 was a relatively quiet year for oil and gas companies.

The deals in 2011 were representative of the trends we witnessed in 2010. Following the Amity Oil and Zorlu Petrogas deal in 2010, American Transatlantic Petroleum increased its presence in the Turkish E&P market further by acquiring Thrace Basin Natural Gas Türkiye Corporation and Pinnacle Turkey Inc. Aygaz, the largest LPG retailer in Turkey, acquiring Totalgaz assets was yet another indication of the long-term contraction in the bulk and cylinder LPG sectors.

Fuel distributors are still trying to reposition themselves following the Competition Authority's 2010 ruling to limit to five years the duration of usufructs and rental contracts between distributors and dealers. This decision, alongside the EPDK's repeated calls to market players urging them to align their margins with the European average, has led to shrinking margins for distributors. We still expect some level of consolidation and a greater preference for the COCO and CODO model among distributors since amendments to the Petroleum Market Licensing Regulation have relaxed the 15% limitation for self-owned stations. However, high investment need for the popular spots and the high cost for available land remain as important obstacles to rapid expansion through this model and as such may necessitate convergence toward creative structures for property ownership.

Figure 5: Oil and gas deals in 2011

Date Announced	Target	Stake %	Acquirer	Acquirer's Nationality	Deal Value (US$ mn)
10-Feb-11	Thrace Basin Natural Gas	100%	TransAtlantic (35%) Valeura Energy (40%) Pinnacle (25%)	Bahamas Canada US	154
21-Mar-11	Totalgaz (assets)	100%	Aygaz	Turkey	23
21-Apr-11	Arar Petrol & Gas	5%	Niche	U.K.	11
28-Dec-11	SOCAR & Turcas Enerji	25%	SOCAR	Azerbaijan	44
28-Dec-11	SOCAR & Turcas Rafineri	19%	Turcas	Turkey	5
Total					**237**

We expect a greater preference for the COCO and CODO model among distributors

Looking ahead

2012 will provide no clear break from 2011. While financing problems continue to bother domestic players, ongoing difficulties in the global and in particular European financial markets as well as regulatory uncertainties will constrain foreign interest in the Turkish energy arena.

Following the successful transfer of Trakya to IC İçtaş and the recent news on EnerjiSA's, Türkerler's and EMKAT's decision to drop their bids to take over Ayedaş, Toroslar and Akdeniz respectively, it is likely that not many of the four pending power distribution tenders will reach successful closure and that new tenders will have to be organised, as in the case of Akdeniz and Gediz. This also raises question marks regarding how power distribution and retail companies will be unbundled as planned at the end of 2012 if the privatisation tenders are not completed by then.

Timing of the power generation tenders will continue to depend on the progress of the distribution deals, and a successful closure of a generation privatisation in 2012 is unlikely. Similarly, the privatisation tender for IGDAŞ is likely to be delayed until the completion of the Başkent Gaz tender. Regulators can turn these delays into advantages by taking the necessary steps to eliminate regulatory uncertainties that will undermine the prospect of successfully privatising power generation and gas distribution companies.

The outlook is brighter for the upstream petroleum market, as most of the onshore and offshore reserves remain untapped. Although no deals took place in the downstream sector in 2011, going forward we still expect fuel distribution companies to resort to consolidation and vertical integration in the face of shrinking margins. While the latest regulatory amendments make distributors' lives easier by relaxing the 15% limitation for self-owned stations, distribution companies still face a high investment need due to the scarcity and high cost of available land.

All in all, current developments do not allow us to expect high deal totals in 2012. Nevertheless, the large portfolio of energy assets on the privatisation agenda, together with the growing domestic demand for energy, give us some hope for a livelier deal environment in 2012.

While financing problems continue to bother domestic players, ongoing difficulties in the global and in particular European financial markets as well as regulatory uncertainties will constrain foreign interest in the Turkish energy arena

Contact us

Our core energy deals team

Faruk Sabuncu
Energy Utilities and Mining Leader
Tel: +90 (212) 326 6082
E-mail: faruk.sabuncu@tr.pwc.com

Murat Çolakoğlu
Partner, Tax Services
Tel: +90 (212) 326 6086
E-mail: murat.colakoglu@tr.pwc.com

Engin Alioğlu
Partner, Deals
Tel: +90 (212) 376 5304
E-mail: engin.alioglu@tr.pwc.com

Ediz Günsel
Partner, Assurance Services
Tel: +90 (212)326 6090
E-mail: e.gunsel@tr.pwc.com

About this report

The main authors of and editorial team for this report were Engin Alioğlu, Irmak Bademli and Murat Silahtaroğlu of PwC Turkey.

Ready to accelerate your growth process?

PwC firms provide industry-focused assurance, tax and advisory services to enhance value for their clients. More than 161,000 people in 154 countries in firms across the PwC network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

PwC, operating in Turkey since 1981, has five offices (two in Istanbul, and one each in Ankara, Bursa and İzmir), with 31 partners and 1,200 professional staff.

www.pwc.com/tr/energy