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The World Bank and International Finance Corporation

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Report No. 33722-UG

PROJET COMPLETION NOTE
(Guarantee No. B-003-0-UG)

ON AN

INTERNATIONAL DEVELOPMENT ASSOCIATION

PARTIAL RISK GUARANTEE

IN THE AMOUNT OF UP TO US$115 MILLION

FOR A SYNDICATED COMMERCIAL BANK LOAN

AND

INTERNATIONAL FINANCE CORPORATION FINANCING CONSISTING OF:

AN "A" LOAN IN THE AMOUNT OF UP TO US$60 MILLION,

A "B" LOAN IN THE AMOUNT OF UP TO US$40 MILLION, AND

A RISK MANAGEMENT INSTRUMENT IN THE AMOUNT OF UP TO US$10 MILLION

TO AES NILE POWER LIMITED

FOR THE BUJAGALI HYDROPOWER PROJECT

IN THE REPUBLIC OF UGANDA

October 3, 2005

Africa Region Energy Team, World Bank, and
Power Department, International Finance Corporation

CURRENCY EQUIVALENTS

(Exchange Rate Effective September 30, 2005)

Currency Unit	=	Uganda Shilling (USh)
US$1	=	Sh1740

FISCAL YEAR

Government	=	July 1 – June 30
AESNP	=	January 1 – December 31

ABBREVIATIONS AND ACRONYMS

AESNP	AES Nile Power
IDA	International Development Association
IFC	International Finance Corporation
km	kilometer
MW	Megawatt
PRG	Partial Risk Guarantee
UEDCL	Uganda Electricity Distribution Company Ltd
UK	United Kingdom
US	United States

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Project Completion Note
Republic of Uganda – Bujagali Hydropower Project (B-003-0 UG)

1. An IDA Partial Risk Guarantee of US$115 million and IFC support of: (a) an "A" loan of up to US$60 million; (b) a "B" loan of up to US$40 million; and (c) a risk management instrument of up to US$10 million for the Bujagali Hydropower Project were approved by the IFC and IDA Executive Directors on December 18, 2001. The project, originally scheduled to reach financial closure in January 2002, failed to become effective, and was subsequently cancelled when the private sponsor pulled out. The purpose of this note is to explain why the project was not implemented.

2. The main development objective of the proposed project was to promote growth through developing least-cost power generation for domestic use in an environmentally sustainable and efficient manner. In addition to mobilizing private capital, the proposed project would promote private sector ownership and management of the power sector, and sector reform.

Project Description

3. This project involved the development by the private sector of a 200-250MW hydropower plant on Dumbbell Island located on the Nile River, about 8 kilometers downstream of the Kiira Hydropower Plant. It included construction of a 100 kilometer transmission line, substations and other associated works. The project was the next component of the least-cost power development program for Uganda. Only about 3 percent of the population had access to grid-based electricity, a key bottleneck to economic growth. The AES Corporation, the private project sponsor, established AES Nile Power Limited (AESNP), a limited liability, privately owned and managed company. AESNP was responsible to develop, construct, own and operate the Bujagali Hydropower Plant, and to construct 100 kilometers (km) of transmission line.

4. Total project costs were estimated at US$582 million. In addition to World Bank Group financial support noted above, the financing plan included US$234 million of export credits, US$55 million in loans from the African Development Bank, US$3 million from Net Interim Energy Revenues, and US$115 million in equity from the project sponsor.

Events which Led to the Project's Cancellation

5. Following the joint IFC/IDA Board approval, the project encountered several difficulties which eventually led to a pull-out of AES and termination of the project with the Government in September 2003. The main issues confronting the project were threefold. The first was the withdrawal of export credit agency support due to the high level of perceived country and business risk in January 2002. This created a financing gap of about US$234 million, for which a promising option was being pursued with the Multilateral Investment Guarantee Agency. Secondly, in parallel, there were ongoing investigations in the US, Norway, the UK and Uganda concerning allegations of corruption involving one of the engineering/procurement/construction contractors, and links to another possible private power generation project under preparation in Uganda. Thirdly, the private sponsor's global financial situation continued to deteriorate following a severe downturn in the global economy after September 11, 2001, a worldwide change in market conditions, and the shrinking of investor interest in emerging markets. Following intense discussions between AES and the Government, on August 13, 2003, AES announced its intention to withdraw from the project.

6. In September 2003, the Government and AES terminated the Implementation Agreement which gave the Government the right to take ownership of the intellectual property and land. In August and September 2003, the World Bank Group sent several technical teams to discuss with the Ugandan Government its options, transition arrangements including the integrity of the project site and intellectual property, and the maintenance of a unit to monitor the project, including the environmental and social aspects. The Government has taken appropriate action on all of these matters.

Meeting Uganda's Power Requirements

7. Since September 2003, the Ugandan authorities have reviewed the country's power sector needs and options, and concluded that Bujagali is still the least-cost power generation option. In January 2004, the Government initiated a transparent and competitive process soliciting the interest of prospective private sponsors in the Bujagali Hydropower Project. This led to the selection of a new project sponsor consortium (Industrial Promotion Services (Kenya) of the Aga Khan Group and Sithe Global (US)) in April 2005. The Government also requested World Bank Group support in reassessing the scope, design, and economic, technical, financial, institutional and environmental and social aspects of the project in the context of Uganda's power demand requirements.

8. The Government has also made progress in the implementation of its sector reform program, which included the concessioning of the Uganda Electricity Generation Company Ltd, to Eskom of South Africa in 2002, and the concessioning of Uganda Electricity Distribution Company (UEDCL) to a consortium of Globeleq (UK) and Eskom of South Africa effective March 2005. The concessioning of UEDCL is central to the operational and financial turnaround of the sector, and to attracting private investment for the future needs of the power sector. Daily load shedding over the past several years, due in part to prolonged drought and reduced hydropower, has affected economic activity. As a result, the Government initiated a transparent and competitive process to procure 50MW of emergency thermal plant in late 2004. In April 2005, the Government signed a three year lease for thermal power. This has reduced regular power outages to about 80MW of load shedding at peak. Further steps are being taken to accelerate co-generation prospects and in identifying potential additional thermal requirements.

Lessons Learned

9. Due diligence for any new power generation project, including the Bujagali Hydropower project, will take note of the various issues raised by the Inspection Panel in its report of May 23, 2002, and Management's Response dated June 7, 2002, and will address them in the context of the project preparation and appraisal process. The main lessons learned from the collapse of the Bujagali Hydropower Project are the importance of: (a) a robust financing plan (the export credit agencies unexpectedly pulled out of the project one month after the IFC/IDA joint Board presentation); (b) a transparent and competitive process for the selection of the civil works and electro-mechanical equipment contractors; and (c) ensuring the efficient operations of the power sector's distribution business including improved quality of supply and access. A financially viable distribution business will over time help to mitigate the perceived risks of potential private investors since this is the primary source of the power sector's cash flow and is a crucial aspect upon which investors will assess the power sector's capability to repay new investments.