

Armenian Infrastructure Fire-Sale Is Blocked

by Vigen Hagobian

Editor's note: On April 25, the Armenian Parliament voted to suspend the tender for the privatization of four electric power companies, which would come under the control of foreign investors. The World Bank continues to demand the privatization, as a precondition for disbursement of a previously negotiated \$45 million Structural Adjustment Credit to cover half of Armenia's 2000 budget deficit. The following report on the arguments around the planned privatization, is adapted from a recent article in the Armenian newspaper Iravunk, titled "Shall We Learn From the Mistakes of Others?" Iravunk is published by the Union for Constitutional Rights, whose members in Parliament were among the leaders of opposition to privatizing the electricity grid.

The recent discussions within various Armenian institutions, particularly the Parliament, on the privatization of four national power distribution systems, were not only scandalous but also very natural. The matter arose as a question of economic policy, but it subsumes social and political problems, as well as even geopolitical nuances.

The geopolitical element is introduced by the identity of the two main competitors for this takeover. They are AES Silk Road, a branch of AES Corp. (U.S.A.), and Itera, a Russian-American subsidiary of the Russian natural gas giant, Gazprom, which has recently formed a consortium with the company Rosatomenergo. The arguments of each side were presented some time ago: The American side threatened to postpone credits from the World Bank, while the Russian side made a point, from time to time, about Armenia's huge debts to Itera, threatening to stop supplying natural gas to Armenia.

Recent pronouncements by Minister of Energy David Zadoyan, however, to the effect that Itera would soon be out of the game, indicated that the higher-ups were prepared to decide in favor of the American company. At the same time, sources report that representatives of the two main competitors are negotiating for a peaceable resolution, a mutually beneficial solution, which suggests that AES and Itera will try to divide up spheres of control over the Armenian energy market.

Before discussing the privatization of the national power distribution systems, it might be worth it to analyze previously privatized enterprises, which are now considered unsuccessful. (The ruination of ArmenTel and our major cognac plant come to mind.) In this case, it is also vital to study the privati-

zation of facilities in other countries, previously carried out with the participation of AES. The data cited below come from AES Corp.'s official reports and press releases, made available to the public in open documents.

The Experience of AES Corporation

The company now attempting to enter the Armenian electric power market, is one of the biggest such firms, the owner of over 44 gigawatts of generating capacity, worldwide. It has gained control, including through privatization, of 940,000 kilometers of power transmission lines. AES supplies 11,000 gigawatt-hours of electricity to its 15 million-some customers. Active in power production, distribution, and retail, AES has become a major owner in the United States, Argentina, Australia, Bangladesh, Brazil, Canada, China, El Salvador, Georgia, Hungary, Mexico, Pakistan, Panama, and Great Britain. Its home office is in Arlington, Virginia. Its scope and ramified structure is shown in the names of its regional subdivisions: AES Americas, AES Americas South, AES Pacific, AES Central US Group, AES Orient, and so forth. For operations in the post-Soviet energy market, AES Silk Road was formed, and it now intends to become the owner of at least one of the two pairs of electricity systems of Armenia.

After the collapse of the U.S.S.R., AES made its move into the former Soviet Republics. In 1993-94, the company began to focus on one of the biggest power systems in the region, namely, Kazakstan's. The process of privatization was preceded by propaganda from the international creditor organizations. In 1995, the results of the international financial organizations' offers (or, rather, conditionalities), were the following: In Kazakstan, AES privatized some of the biggest systems in Central Asia—the Ust-Kamenogorsk Thermal Power Station, with a capacity of 4 GW; the Ust-Kamenogorsk Hydroelectric Power Station, 332 MW; the Shulbim Hydroelectric Power Station, 702 MW; the Leninogorsk Thermal Power Station, 50 MW; the Sogrinisky Thermal Power Station, 50 MW; the Semipalatinsk Thermal Power Station; the Ust-Kamenogorsk power distribution system; and others.

Naturally, privatization was going to solve all problems of supply and, naturally, there were great hopes connected with the investment projects and obligations assumed by AES, but the Ust-Kamenogorsk Thermal Power Station was closed immediately after privatization. Since major enterprises and factories were concentrated in this area of Kazakstan, it is not difficult to imagine the dramatic results of such a privatization process. All these plants and factories were depreciated in value, only then to be privatized by big American and European concerns at very low prices. After these sales, the power plant was cranked up again, at its previous capacity.

The question had to be asked: What were the real goals of this American firm in Kazakstan? Was it working only for its own economic goals?

The Fortunes of AES in Georgia

In 1996-98, the people of Georgia received electricity only a few hours per day. During the winter months, power was supplied in the capital city, Tbilisi, for only seven to nine hours each day. People were desperate.

The same scenario was played out, as in Kazakstan. First, the international financial organizations worked to create a similar atmosphere around the privatization of the Tbilisi power system. As the only way out, the idea of privatizing the Telasi distribution system was put forward, and welcomed by the exhausted population. AES Silk Road came on the scene, as the only available savior for Tbilisi's power grid. Seventy-five percent of the utility's shares were sold for \$25.5 million, creating AES Telasi, which enjoyed major post-privatization concessions, such as low purchase tariffs, the right to have a monopoly, and others. The new American owners promised to supply electricity round-the-clock very soon, to upgrade the equipment, and to stabilize the fees. These promises have remained unfulfilled. More than a year had passed since privatization, but if we compare this past winter's energy supply with the previous years, it becomes clear that the situation worsened. International creditor organizations proposed more structural changes to ease the situation, and then finally began to argue that all the misfortunes were the result of problems at the power plants, and that it was necessary to begin the second stage of privatization.

In Georgia, just as in Armenia, it was initially declared, on the eve of privatization, that only the Tbilisi distribution system would be privatized, not the power-producing stations or the high-voltage networks. In 1999, however, in this "second stage of privatization," AES privatized the Tbil Thermal Power Station (acquiring 80% of its shares), with its two 300 MW units, while the electricity distribution system in Rustavi and the hydroelectric power stations Khrami 1 and Khrami 2 were given to AES for 25 years. According to the Georgian government, these enterprises needed serious investments, without which the system would be destroyed. (Members of the Armenian government have repeated the arguments of their Georgian colleagues, word for word.) When the deal was done, the American side had to pay only \$11 million for its acquisitions around Tbilisi. The president of AES Silk Road, Garry Levesley, noted, "We are very glad to have this deal, as Tbil HPS is in excellent shape and is one of the main stations in the region." The happiness of the American representative is clear, because about \$100 million was invested in this power station alone, in recent years, while almost \$40 million was put into Khrami 2 by the Japanese government.

There was one more element to make Levesley happy. AES Silk Road has acquired the right to supply electricity from Georgia to Turkey, which means entry into another big market.

Compare data on the enterprises privatized by AES in

Georgia, with other countries. In 1999, for example, AES paid \$3 billion for the Drax Thermal Power Station in Great Britain, with a capacity of 3,960 MW. The same year, it acquired the 826 MW San Nicolas Hydroelectric Power Station, near Buenos Aires, for \$448 million. In May 1999, another British power plant cost AES \$195 million. Thus, it is clear, that the value of the Georgian station was understated at sale approximately by a factor of 60!

Let us turn to another interesting fact, which bears directly on the future privatization process in Armenia. During the first stage of privatization in Georgia, AES obtained from the World Bank and the European Bank for Reconstruction and Development about \$60 million, of which \$11 million was used for its purchases in Georgia, and the remainder would presumably be used to purchase the Armenian distribution systems. The Armenian government would sell a controlling packet of shares in the four power systems, for \$50-60 million. Evidently the World Bank is interested not just in privatization, as such, but in becoming co-owner of the Armenian electricity grid.

The arguments of the Armenian government and the creditor organizations about privatization as the only way to save the system, are more than suspicious. This can be demonstrated by the examples of Kazakstan and Georgia. But, will this experience be taken into consideration during the privatization process in Armenia? And why do those responsible for this process hide the real picture? It is clear that AES is very much interested in the privatization of the Armenian power systems. It has proven quite profitable, to privatize any unit of strategic importance, at a very low price. The Armenian nuclear power plant would become dependent on AES. The company would be poised to get the right to export electricity to Turkey, a factor fraught with serious economic and political consequences, which would also reshape the electricity market of the whole region.

The Armenian government understands all that. But, there is every indication from current processes, that the danger to Armenian economic interests is real. It has become clear, that upper echelons of the government do intend to hand over a controlling interest in the electricity grid to the foreign investors. The hope remains, that the scenarios, played out in Georgia and Kazakstan, will not be repeated in Armenia. The methods of the creditor organizations are obviously the same.

Was it really only by chance, that during the discussions about privatization, the level of payments for electricity in Armenia was reduced from 80% to 60-61%? Or, was it to show the inefficiency of a state-run power system? One would think we had learned nothing, from the lessons of the past. It will come as no surprise, if a year from now Armenia has the same sad picture as in Georgia.

As this article went to press, in late May, it was learned from a member of the privatization committee, that Itera is out of the running.