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2020

Energy Deals

Merger and acquisition activity in Turkey's energy market

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Contents

Methodology and terminology

Energy Deals 2020 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 2020, 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%. This document is also available at pwc.com.tr/energy-deals

Welcome

to the 13th edition of the Energy Deals, our annual analysis of mergers and acquisitions in the Turkish energy market

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In 2020, a year like no other, one word we frequently used for the global energy industry was 'upend'. Oil and gas prices first tumbled then slightly recovered, lesser known renewable energy companies topped the fossil fuel giants' market values, digitalisation gained the must status in coping with the pandemic, M&As first reeled but then came back stronger in the second half of the year…

Against this global picture, Turkish energy market got caught to the pandemic in the middle of its own structural and regulatory problems. To significant FX denominated debt crisis on the utility front, further devaluation in Turkish lira, diminishing availability of project finance, uncertainty in the renewables energy regulation, weak profitability in fuel retail and lack of progress in gas market liberalisation were added to the pandemic-led demand shock and collection problems.

However, total deal figures in 2020 managed to recover from the gloomy performance in 2019. 22 energy deals generated an estimated total value of USD 1.1 billion, marking 83% increase from USD 600 million in 2019. The considerable foreign involvement in 2019 got down to a mere 3% in total estimated deal value in 2020, amid the intensive cherry picking activity by the investors in the developing markets.

Rare in our deal reporting, the value of the oil & gas deals exceeded the utility deals in 2020. Six deals, mainly in LNG and fuel & LPG retail, amounted to an estimated USD 600 million in total. Three acquisitions by OYAK are considered a start of a new wave of consolidation in the very fragmented fuel and LPG retail markets.

16 utility deals were disclosed in 2020 with an estimated total value of only USD 500 million, 17% down from 2019. The deal segments were fairly diversified with the majority in renewable energy and the rest in thermal power generation and gas distribution. The interest in the renewable energy assets which will enjoy the feed-in-tariffs in USD until the end of 2030 was weaker than expected. We see that the story on that front rather concerns the macroeconomic challenges and the general investment sentiment undermined by the pandemic.

Looking ahead... The pandemic is still here with new mutations and the vaccine roll out may not be a quick fix to all the ills in our market. The energy companies will still perform their public duties to keep our lights on and our cars running, while trying to remain financially viable. More than ever, the stakeholders need to cooperate to keep each other afloat and ready to embrace the new shape of the post-pandemic market. Turkish energy administration needs to put extra effort to align its actions with the global best practices and be even more proactive and effective in shielding the market from further shocks.

Deal Totals

Recovery despite the pandemic...

The total deal value which had seen the bottom of the previous decade's figures in 2019 managed to recover in 2020 against all odds of Covid-19.

22 energy deals generated an estimated total value of USD 1.1 billion, marking 83% increase from USD 600 million in 2019.

The average deal value had a 83% jump from USD 27 million in 2019 to USD 50 million in 2020.

Rare in our deal reporting since 2008, the value of the oil & gas deals topped the utility deals in 2020. Six oil & gas deals amounted to an estimated USD 600 million in total in LNG and fuel & LPG retail.

16 deals were disclosed in the utilities segment in 2020 with an estimated total value of only USD 500 million. The majority of these deals concerned renewable energy, and the rest in thermal power generation and gas distribution.

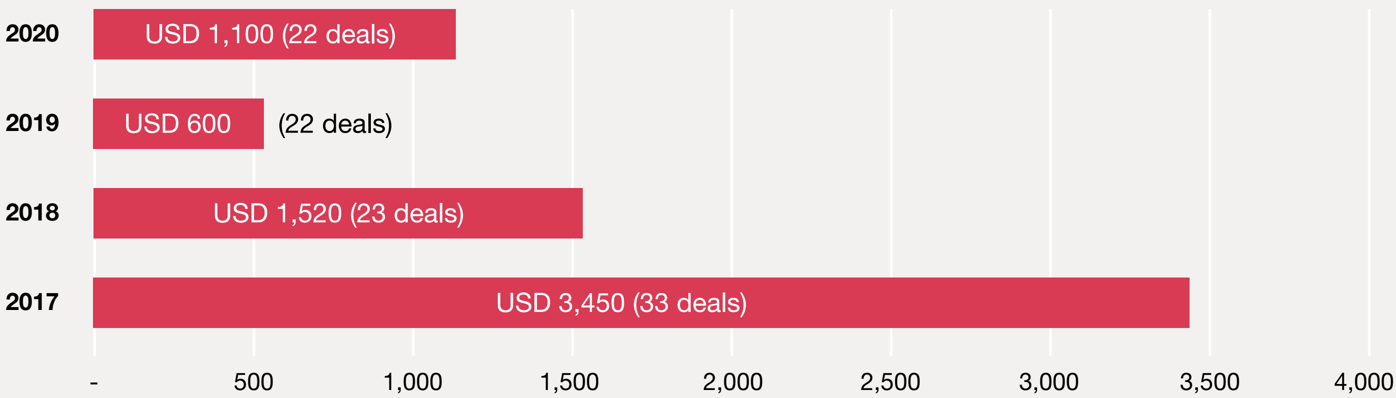
Except one privatisation, all the deals happened between the private players in 2020.

The total deal value, which had dipped in 2019, managed to recover against all odds in 2020

Figure 1: Total Energy Deals in 2019 and 2020

	FY19			FY20			YoY change	
	Number	Value (USD m)	Average Value	Number	Value (USD m)	Average Value	% number	% value
Utilities	21	600	29	16	500	31	(24%)	(17%)
Oil and gas	1	n.d.	n.d.	6	600	100	n.m.	n.m.
Total	**22**	**600**	**27**	**22**	**1,100**	**50**	**-**	**83%**

Figure 2: Total deals between 2017 and 2020 by value (USD million) and number of deals



All but one deal were among the private players in 2020

Slowed down much before the pandemic, only one privatisation took place and it was for two small HPPs.

With the changing risk perception, foreign investors almost deserted the Turkish energy deal arena in 2020

In 2020, the foreign investors were almost absent with only 3% of share in the total estimated deal value. This is a significant change after 2019, when their share was 57% vis-à-vis that of the local buyers.

3%
foreign investors

versus

97%
local investors

Utilities

Hit hard by the pandemic but not only that...

The long brewing seismic shifts in the global energy industry gained an unprecedent momentum in 2020. Growing acceptance of the need to tackle the climate crisis by cutting carbon emissions has coincided with the accelerated demise of fossil fuels due to Covid-driven plunge in demand.

M&A targeting the renewable energy sector has remained resilient globally. However, Turkey, whose renewable energy potential tops the global lists, could generate only a fraction of the global totals in utility deals. The number of deals fell from 21 in 2019 to 16 in 2020, with estimated total deal value shrinking by 17% from the already low USD 600 million to USD 500 million.

Surprisingly, falling demand for power is not among the main reasons behind. In fact, after April and May 2020 when the power demand was in free fall by around 15% y-o-y, there was a quick recovery with the ease in lockdown rules. By the date we finalise this report, the latest official demand figures belong to October 2020, which was still up by 5% y-o-y. Similarly, demand for gas has not experienced a sharp drop either and it decreased only 3.5% y-o-y during the first seven months of the year thanks to strong residential demand.

The real reasons for poor deal performance were there well before the pandemic. The players in the Turkish utility market have long been struggling with a serious FX denominated debt crisis under the intensifying risks in macroeconomy and energy market regulation. The significant depreciation in 2020 made the repayment more difficult with all the earnings in Turkish Lira (except for the renewable energy producers benefiting from the feed-in tariffs in USD).

On the regulation front, the years-long slow progress in gas market liberalisation failing to provide a reliable pricing and supply environment to power producers had been already joined by uncertainties about the post-2021 status of YEKDEM, the feed-in tariff system.

Among the most heated discussion was about the scope of the force majeure clauses in the Electricity Market Licensing Regulation. The group with the most at stake was the investors in the renewable power generation. Prior to a very recent amendment in this Regulation, those who were planning to join YEKDEM between 2020-2030 were required to commission their plants before 31-Dec-2020 to be eligible for the feed-in tariff.

Around 1.5 GW of wind PP project, 1 GW of solar PP project and USD 4.5 billion-worth of geothermal PP projects suddenly came to the brink of being left out of YEKDEM during the first 10 years of their operation as it was almost impossible to hit the commissioning deadline due to the Covid-related disruption in global supply chain. Needless to say, this would result in the cancellation of financing and eventually of the projects altogether.

Lobbying by the industry organisations gave a fruit only recently and the commissioning deadline is extended to 30-Jun-2021, however, without extending the final date of the feed-in tariff support beyond 31-Dec-2030.

And, no YEKA tenders for the 74 small-size solar PP licenses took place in 2020 and the application deadline previously scheduled to October 2020 is now postponed to March 2021.

A silver lining in the renewables story in 2020 concerns their share in the power output. The sharp drop in demand in April and May 2020 pushed the share of renewable PPs above 60% in these two months and above 40% over the rest of the year.

On the other side of the coin is the sustained drama of the gas-fired PPs, especially the ones which were commissioned over the last five years and, since then, struggling to breakeven. The challenges in 2020 were amplified with the inability to discount the local gas tariffs given the depreciation in the Turkish Lira in spite of the sharp drop in the global energy prices.

Against this background, the already weak deal momentum in the Turkish utilities market further waned and only 16 deals were disclosed in 2020. The majority of them was for renewable energy and a few in thermal power generation and gas distribution, reflecting the tougher challenges in the latter segments.

The utility deal with the largest disclosed figure in 2020 involved Silopi Elektrik Uretim, owning and operating a 405 MW asphaltite-fired PP (the only one in Turkey). The deal had GSD Holding selling its 5.4% share in the company back to Park Holding, the majority shareholder, for USD 45 million. As a result, Park Holding's stake increased to 90.4%.

Another deal with a disclosed value was also a share exchange between the existing owners. Yesil Holding converted its receivables from Ortadogu Enerji into 9.9% stake for USD 17.6 million and increased its total stake in the company to 58%. Ortadogu Enerji owns four operating waste-to-energy PPs of 60 MW in total, one operating WPP of 42 MW and two WPP licenses of 40 MW in total. We believe that more of this kind of refinance deals would exist among the undisclosed lot due to the pressure on P&Ls, as explained above.

The third deal with a disclosed value was also the only one with a foreign buyer in the utility market. Japan Energy Fund formed by Enechange and Looop invested USD 10 million to acquire joint operation rights of a 13 MW solar power plant for 10 years. The Fund confirmed that the main motivation behind this acquisition is YEKDEM, which in turn underlines the criticality of its existence in some shape for the PPs to be commissioned after mid-2021.

Among the deals with undisclosed values is stepping forth Engie's divestments of its 95% share in 770 MW Baymina CCGT and its 90% share in IZGAZ, one of the largest natural gas distribution company with around 325,000 customers in Kocaeli, an industrial city in northwest Turkey. The buyer is Palmet Enerji, a Turkish energy company with two more gas distribution companies, two small gas-fired plants of 60 MW and 62 MW, and a HPP license for 284 MW. With this double acquisition, the company is understood to increase their capacities by benefiting from the buyers' market conditions.

Moving on to another deal, 30% combined stake in Kalyon-Türkerler Rüzgâr Enerjisi Elektrik Üretim was sold to a consortium of two local energy companies, Metgün and Efa.

Together with Siemens Gamesa as the equipment partner, Kalyon-Turkerler consortium won the YEKA – RES 1 tender in 2017 to build and operate a total of 1 GW of WPPs in Turkey, with a bid of USD cent 3.48/kWh (vs the feed-in tariff of USD cent 7.30/kWh) for 15 years. Unless changed with Covid-19, the consortium is planning to commission at least 700 MW by 2022.

Another WPP deal involving a relatively sizeable generation portfolio was the 50% stake acquisition in Erguvan Enerji Uretim by Batiyel Enerji from Demirer Holding and members of the Demirer family. The target company is holding a license for a 110 MW WPP. And the acquirer, Batiyel, has a 10% stake in Polat Enerji, one of the largest WPP companies in Turkey.

In addition to these private deals, there was also one privatisation. A 4 MW HPP portfolio, Ahikoy I and II, was sold to Ergezen, a Turkish infrastructure company.

Although it is not a ‘deal’ within our definition, a transfer is worth mentioning. The 620 MW Cayirhan Coal-fired PP and the adjacent coal mines completed their Operate-Transfer concession under Park Elektrik and were returned to EUAS, state power company.

The faith of the new 720 MW Cayirhan-B Coal-fired PP project in the same region is uncertain. The construction master plan granted to build it on a wetland critical to the fragile ecosystem was annulled with a court decision upon the application by TEMA, the Turkish Foundation for Combating Soil Erosion. This court decision is very significant amid the global call to stop new coal-fired PPs.

Following these deals, now let’s have a look at what was missing in 2020…

The increase in threshold to operate an unlicensed solar PP had increased from 1 MW to 5 MW in 2019. However, our expectations for these to become a deal item failed to materialise so far due to regulatory problems including complex approval procedures, high connection fees, lack of standard legal agreements to cover all the potential issues between the investors and the EPC contractors and no stamp tax duty exemption in subcontractor agreements.

And the news about two potential deals lapsed into silence later assumingly due to Covid-19. Their significance is not only about the portfolio sizes but also the potential intention of some large foreign players to exit from the Turkish market. First came the news about the sale of Polat Enerji, one of the largest renewable energy companies in Turkey. This would mean the exit of PSP Investments, one of the largest pension fund in Canada, and EDF Energies Nouvelles, each holding 45% in the company. And then came the news about STEAG’s intention to sell their 66 MW operating WPP.

Finally, the two IPOs scheduled for 2020 did not go ahead either.

Figure 3: Utility Deals in 2020

Date Announced	Target	Stakes in %	Acquirer	Acquirer Nationality	Deal Value USD mn
17-Feb-20	Tekno Rüzgar Enerji	100%	Ziyaret RES	Turkey	n.d.
21-Apr-20	13 MW solar power plant	100%	Japan Energy Fund	Japan	10.0
15-May-20	Ortadoğu Enerji	10%	Yeşil Yapi	Turkey	17.6
8-Jun-20	Silopi Elektrik Uretim	5,4%	Park Holding	Turkey	45.0
21-Jul-20	Erguvan Enerji	50%	Batıyel Eneji	Turkey	n.d.
27-Jul-20	Kalyon Türkerler Rüzgar Enerjisi	30%	Metgün Enerji Yatırımları/ Efa Group Enerji	Turkey	n.d.
27-Aug-20	Ahiköy I and Ahiköy II WPP	100%	Ergezen Yapi	Turkey	1.5
30-Sep-20	Bomonti Elektrik	80%	Pamukova Elektrik	Turkey	n.d.
15-Oct-20	Uluder Enerji	100%	Private investors (Mesut Altan - İdris Çakır)	Turkey	n.d.
2-Dec-20	Bereketli Elektrik	100%	Deniz RES Enerji Yatirimlari	Turkey	n.d.
7-Dec-20	Solar power plant of Özyer Group	100%	Esenboga Elektrik	Turkey	13.6
23-Dec-20	Izgaz	90%	Palmet Enerji	Turkey	n.d.
23-Dec-20	Baymina Enerji	95%	Palmet Enerji	Turkey	n.d.
28-Dec-20	Akca Enerji	32%	Menderes Tekstil	Turkey	7.5
28-Dec-20	Tan Elektrik	34%	Menderes Tekstil	Turkey	8.0
29-Dec-20	A solar power plant	100%	EYN Teknoloji	Turkey	1.3
Total				≅	**500.0***

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

Oil and gas

Saving the bottom line...

After a very quiet 2019, 2020 was an unexpectedly busy year in the oil & gas deal space in Turkey.

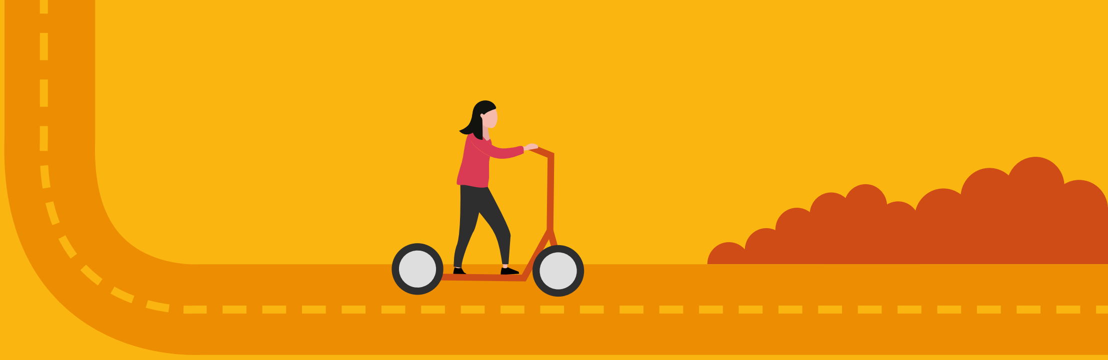
In this exceptional year where the estimated value of the utility deals fell behind, the number of oil & gas deals rose from one in 2019 to six in 2020 with a total estimated value of USD 600 million. Four of the deals were in the fuel & LPG distribution and the remaining two in gas E&P.

In the largest deal of the year, OYAK came back to the fuel distribution market 18 years after its full exit from the Turkish operations of Elf (later merged with TOTAL) in 2002. The events came to full circle in 2020 and OYAK acquired Guzel Enerji (TOTAL Oil Türkiye) and M Oil both from Demiroren Holding. M Oil is now consolidated under Guzel Oil with around 900 petrol stations in total and 6% combined market share, which makes OYAK the fifth largest player in the Turkish fuel retail market.

The unloading from Demiroren to OYAK in 2020 continued with the sale of Milangaz, the fifth largest LPG distributor in Turkey with 8.6% market share (auto LPG and bulk combined) in 2019. Turkey has the largest number of LPG cars in the world and integrating the LPG business with the rest of these new fuel retail businesses would give an important competitive edge to OYAK.

These three deals were the first disclosed large deals in the fuel retail market since the sale of Petrol Ofisi in 2017. Behind this stagnation are counterproductive regulation of the fuel retail prices and the share of the gas station owners in the total margin making hard for the distributors to cover their operational expenses.

Again in LPG, Russian company JSC Oteko sold its autogas distribution company Petgaz to BDY Group Yatirim, a Turkish company active in LPG distribution and logistics. JSC Oteko had entered the Turkish market by buying the LPG storage and distribution business from BP in 2012. It first sold the storage business in 2017 and now exited from the Turkish market with this divestment.



Turkish LPG companies were busy abroad as well. AYGAZ signed a Share Purchase Agreement for the acquisition of 50% in United LPG of Bangladesh for USD 625,000. This is not included in our figures as the deal destination is not Turkey.

Still on the distribution front, SOCAR Turkey's LNG and CNG distribution operations were acquired by Naturelgaz for USD 4.1 million.

The two remaining disclosed deals were in the natural gas E&P.

In one, the Canadian company Valeura Energy has executed a Share Purchase Agreement to sell its producing shallow conventional gas business to Thrace Basin Natural Gas Corporation and Corporate Resources B.V. (TBNG) for USD 15.5 million. With this exit from the conventional gas business, Valeura confirmed its full focus on the deep gas plays in Turkey with further investments. Equinor, the company's JV partner in the deep gas appraisal programme in Turkey had already discontinued their agreement in 2020.

The other natural gas E&P transaction was the sale by Transatlantic Petroleum of its fully owned subsidiary Petrogas Petrol Gaz ve Petrokimya to Reform Ham Petrol Dogal Gaz Arama for USD 1.5 million.

Figure 4: Oil & gas Deals in 2020

Date Announced	Target	Stakes in %	Acquirer	Acquirer Nationality	Deal Value USD mn
5-Feb-20	Socar Turkey LNG	100%	Naturel Doğalgaz	Turkey	4.1
24-Feb-20	Petrogas Petrol Gaz ve Petrokimya	100%	Reform Ham Petrol Doğalgaz	Turkey	1.5
28-Feb-20	Güzel Enerji and M-Oil	100%	OYAK	Turkey	n.d.
26-Jul-20	Petgaz	100%	BDY Group	Turkey	n.d.
25-Aug-20	Milangaz	100%	OYAK	Turkey	n.d.
20-Oct-20	Valeura Energy (Thrace Basin NG and Corporate Resources)	100%	TBNG Limited	UK	15.5
Total				≡	**600.0***

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

Looking ahead

We see six topics to shape the deal environment in Turkish energy market in 2021 and beyond: utility companies' debt problem, future of YEKDEM, green PPAs, support to hybrid power generation, consolidation in the fuel and LPG retail, developments in natural gas import.

The slow down in the restructuring efforts between the banks and utility companies to solve the **debt problem** is expected to be replaced by a momentum with relative improvement in balance sheets in 2021.

Future of YEKDEM for the renewable energy plants to be commissioned after mid-2021 is a concern for new project financing. A recent amendment in the Electricity Market Law opened the doors to the switch to TRY from USD in the next version of YEKDEM, which would end in a significant erosion in revenues. On the other hand, this switch would increase the investors' interest in the assets which will be the last beneficiaries of the current terms until the end of 2030.

Some considerations in the meantime would give food for thought about what could compensate the shortcomings in a TRY-based YEKDEM world. In that sense, the willingness in the Turkish finance circles to consider the **green PPAs** is promising. If tailored uniquely to the market and projects and if not burdened with unnecessary regulation, green PPAs would become an alternative to YEKDEM in the medium run.

Last but not the least in the renewables space, the **hybrid power generation** has been finally granted the regulatory framework in the Turkish market, now with the permit to have more than one generation technology under the same license on the same designated area and still with the option to benefit from YEKDEM. Productivity and efficiency boost with the hybrid options has the potential to create new deal attractions.

Making predictions about the oil and gas deals is not always easy as the nature of the deals over the recent years in particular were quite sporadic and not necessarily a direct reaction to the market developments. However, we can now point out to a slowly developing **consolidation trend in fuel and LPG retail** with the increasing pressure on balance sheets in a very crowded market.

In fact, a quick look at the numbers would tell that this trend has been long overdue. In Turkey, there are 96 fuel and 91 LPG distribution companies. The fuel segment is highly concentrated: the top six in 96 sells 70% of the total volume. The LPG segment is little bit more fragmented with ten in 91 sells 80%.

In both segments pre-COVID margins were hardly touching 5% and now that the demand and workforce are very hardly hit, the mid and small-size players in particular are struggling. So, we believe that the deal momentum started with three OYAK acquisitions in 2020 would continue with an intense cherry picking activity in 2021 and beyond.

The recent **developments in natural gas import** are also worth watching. In 2021, 16 bcm/year of long-term supply contracts (LTCs) with Gazprom will expire. And the LTCs with Azerbaijan and Iran are to follow.

The coincidence of this with Covid-19 is a disguised blessing for Turkey: the historical lows tested by global gas prices and the global surplus of both LNG and pipe gas provide a perfect opportunity for a transition from LTCs, oil-linked prices, ToP obligations and destination clauses to a free, open, and transparent market.

We have been always telling you about the inertia in the liberalisation of Turkish gas market and its detrimental impact on the power sector. In fact, BOTAS still holds 96% share in total gas supply volume to Turkey. This has had two main reasons until now: 1) LTCs with unfavorable terms, and 2) Turkish government's desire to control the market for economic, political and strategic reasons. The first reason is already expiring and the second is now seriously tested.

In 2020, EPDK started its auctions to allocate pipeline capacity at the Malkoclar entry point on the Bulgaria-Turkey border for spot gas import. Also, Gazprom Export held tenders for the first gas sales on its Electronic Sales Platform (ESP) to be delivered to Turkey again at Malkoclar and reached an agreement with a private gas trading company for the sale of 715,000 cubic meters.

In light of these small but important steps, we understand that the energy administration is now gearing up their efforts to transform Turkey into a regional gas hub and that they will become even more serious with actionable plans to achieve the liberalisation. Albeit not immediately, these steps would eventually bring the proliferation of sound gas trading businesses owned by the private sector and help to save the gas-fired PPs from the survival mode.

All in all, deal opportunities exist despite all odds. But the majority of these hot topics point out the delays in regulation leading to slow progress in full customisation of the best practices to the Turkish market, which are likely to keep the deal flow locked.

Now that a tumultuous and tragic 2020 will usher in a 2021 fraught with uncertainty, one thing is crystal clear: the stakeholders need to cooperate even more to keep each other afloat and ready to embrace the new shape of the market. At the end of the day, albeit undertaken by the private sector, we are talking about a public service and its continuity is even more critical now.

Therefore, the Turkish energy administration is expected to sustain its existing determination to align its actions with the global best practices and to continue its constructive communication with the market players to protect them from further shocks. The local players who think their survival depends on government support, on the other hand, should become even more creative in their investment plans, embracing the fact that the ultimate goal is to be a part of a fully liberalised market with a level playing field among technologies.

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