

*This series provides an overview of successful public-private partnerships in various infrastructure sectors, where IFC was the lead advisor.*

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# Albania: Privatization of Electricity Distribution

In March 2009 IFC concluded its second infrastructure transaction in Albania: the privatization of Kesh, the national electricity company. The Czech Republic's Cez Group was selected as the winning bidder for the acquisition of 76 percent of the shares of the electricity distribution business for an equivalent of US\$125 million.

The Albanian government had sought IFC's assistance to help strengthen the legislation and institutional framework for public-private partnerships and to implement two transactions in key infrastructure sectors. Three years later, a new concession law is in place, the government's Concession Unit has been in operation since 2007, and the first hydroelectric power plant concession was awarded in October 2008.

The Private Enterprise Partnership for Southeast Europe Infrastructure and DevCo supported the advisory work. The partnership was established in cooperation with and with financing from the governments of Austria, Italy, the Netherlands, Norway, Switzerland, and the United States. DevCo is a multidonor program affiliated with the Private Infrastructure Development Group and is supported by the United Kingdom's Department for International Development, the Dutch Ministry of Foreign Affairs, the Swedish International Development Agency, and the Austrian Development Agency.

## BACKGROUND

At the beginning of the economic transition in the early 1990s Albania was a net power exporter, but by 1998, growing demand had turned the country into a net importer. The sector had been unable to keep up with the growing demand because of low generation capacity, over-reliance on hydroelectric production, and transmission and interconnection constraints that limited the amount of electricity that could be imported, as well as financial constraints and inflexible electricity import procedures. As a result the country had suffered from load shedding of 400 to 900 gigawatt hours per year since 2000.

To secure the supply of electricity, the government decided to undertake a series of initiatives along with policy and regulatory reforms. The initiatives aimed to address constraints pertaining to generation and interconnection systems, reduce dependence on hydroelectric production, and liberalize the electricity market. The government also decided to unbundle and privatize the electricity distribution business, which was suffering from large technical and nontechnical losses stemming from distribution, billing, and collection deficiencies and the state-owned utility's inability to deal with electricity theft.

## IFC'S ROLE

In January 2007, the government retained IFC as its lead adviser for the process of unbundling and privatization of the electricity distribution sector. IFC's participation proved critical not only for unbundling the electricity distribution sector and structuring the privatization transaction, but also for enhancing the implementation of electricity sector reforms.

Close cooperation by IFC and the World Bank in coordinating among stakeholders, achieving political commitment, and obtaining donor community consensus accelerated the reform process and was key to ensuring private sector participation. Furthermore, IFC's reputation as an honest broker increased potential investors' trust in the privatization process.

## TRANSACTION STRUCTURE

IFC presented its recommendations on the transaction and on the structure of the electricity market to the government and the regulator in December 2007. These recommendations included allowing a monopoly in the electricity distribution business to give the private partner a better chance of making a fair return on the investment needed to upgrade and develop the network. The supply business was divided into wholesale and retail components, with only the retail portion being privatized. The state-owned utility remained responsible for the wholesale component, as potential investors perceived the obligation to supply as unaffordable and unacceptable given the characteristics of the Albanian power sector.

Performance targets for the operator were set as precondition for bidding, and a partial risk guarantee (a World Bank financial instrument to backstop regulatory and political risks) was provided to mitigate the risk of noncompliance by the regulator.

In line with IFC's recommendations, a new electricity distribution company was created as a separate legal entity in early 2008 and employees, assets, and liabilities were transferred shortly thereafter.

## BIDDING

The bidding process was launched in May 2008 and four strategic investors were prequalified. The process was concluded successfully in October 2008 with the selection of the Čez Group of the Czech Republic as the winning bidder for the acquisition of 76 percent of the shares of the electricity distribution business for an equivalent of US\$125 million. The Čez Group committed to reduce the level of technical and nontechnical losses from 32 percent to 15 percent during the first five years of operations by means of investments of approximately US\$250 million.

## POST-TENDER RESULTS

The expected benefits of introducing a strategic investor with extensive experience in electricity distribution and generation are:

- long-term and sustainable electricity distribution improvements based on sound commercial principles and in line with industry best practices;
- enhanced security of energy supply because of reduced dependence on imports;
- adequate investment in upgrading the distribution system; and
- introduction of proper standards for and methods of customer billing, collection, and services management.



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