

# RCOB: Certificates spark Farac 1

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19/10/2009

ICA and Goldman Sachs Infrastructure Partners have completed a Ps8.55 billion (\$627 million) recapitalisation of their Farac 1 toll road portfolio. The centrepiece of the process is an issuance of new equity by the portfolio using a new instrument called Certificados de Capital de Desarrollo de Infraestructura, or development certificates. These instruments take the pressing need of the Farac sponsors – to deleverage – and marry it to the more general policy aspiration of Mexico's government – to encourage more pension fund interest in infrastructure assets.

Santander led the issue of the certificates, and was also the lead arranger for the debt financing backing the acquisition of the roads portfolio. Santander and the other lenders to Farac 1 will be the recipients of the proceeds of the equity sale, and will see their exposure to Farac substantially reduced.

The Farac 1 acquisition marked – in retrospect – the top of the market for infrastructure valuations in Mexico. Even at the time, rival bidders and banks that stayed out of the deal questioned how ICA and Goldman reached their valuation, and how banks would digest such a commitment.

ICA and Goldman submitted a bid of Ps44.051 billion (\$3.23 billion at today's rates, but then more like \$4 billion) for the package in July 2007. They closed on the acquisition, and Ps37.1 billion in bank debt, in October of that year. Joining Santander as bookrunner, were Banorte, HSBC, Nord/LB and Dexia, while Banobras, Inbursa, ING and WestLB also participated.

Sponsors and arrangers planned to refinance some or all of this debt in the domestic bond market, and in late 2007 this goal looked possible. However, the first sign of trouble came when the bond insurers, a central part of this effort, teetered, and a plan to get the Overseas Private Investment Corporation to backstop a wrap of the bonds by MBIA faltered. By late 2008, bond markets in the US and Mexico were closed, and with it Farac's refinancing window.

The sponsors realised that the levels of leverage on the project were too high, and even with a refinancing of some of the senior debt in the bond market, even if this were possible, would remain too high. Since capital markets have recovered sponsors, most notably IDEAL, have enjoyed access to the bond market. IDEAL, however, has refinanced sponsor equity with its Credit Suisse-led bond issues.

Both ICA and its infrastructure fund partner had to raise more equity, but going to its shareholders and limited partners at the bottom of the market would make them very unpopular. At which point Mexico's regulators intervened.

The country's securities regulator, the Comisión Nacional Bancaria y de Valores and its pension funds regulator, the Comisión Nacional del Sistema de Ahorro para el Retiro (CONSAR), had been looking for ways to allow Mexico's pension funds, or Afores, to gain a greater degree of exposure to infrastructure assets. Before GSIP bought into Farac 1, financial investors of any sort were rare in Mexican infrastructure, its power sector excluded. Strategic investors, both domestic and foreign, dominate the country's roads market. Listed infrastructure markets exist only in the UK, Australia and the US, and all of these have had patchy success in the last two years.

The new securities are flexible enough to cover a variety of asset types including infrastructure and real estate. One operator of fast-food franchises is also thought to be considering an issue. They also might encompass everything from common equity to convertible, preferred share and subordinated debt issues. One reason for the high profile enjoyed by

the new instruments is the presence of Luis Tellez, secretary of state for transportation and communications between 2006 and March 2009, as chief executive of the Bolsa Mexicana de Valores, Mexico's stock exchange.

The financing is structured as the issuance of a new class of equity, series B equity, to a trust, which in turn issues the development certificates. Each certificate is equal to 100 Series B shares, and was priced at Ps77 each, or a 23% discount to the implied equity value of the portfolio. The Series B shares have identical rights to dividends as the existing Series A common equity. Reports indicated that the sponsors considered structuring the deal as a preferred share issue, though, says Gabriel de la Concha, ICA's head of concessions, "we weren't looking to increase the leverage on the project. We looked at issuing a zero-coupon bond, but were able to convince the regulators that structuring the deal like this was complicated and unnecessary."

To get the issue closed, GSIP and ICA promised to contribute additional Series A equity of the same amount as the largest single ticket written during the Series B sale. After the sale closed, they had to contribute an additional Ps2 billion in equity. Following the deal's closing, GSIP had a 54.5% interest in the assets, ICA 13.6% and the trust issuer 31.7%. The certificates will trade using the symbol RCOB, after Red de Carreteras de Occidente, the name of the Farac holding company, but ownership of the certificates is restricted to eligible investors, mostly the large public and private pension funds.

Development certificates served very well as a solution to the top-of-market leverage that afflicted the sponsors of the Farac 1 portfolio. But the deal will not be a one-off. According to Tellez' reported comments, Macquarie is interested in leading a certificate issue, though it does not yet own any infrastructure assets in Mexico, and has shown greater interest in recent months in bulking up its corporate finance advisory capabilities. The Farac 1 issue sold because it had operating assets, limited construction risk, and no bidding risk. Its successors will need to jump a much larger number of hurdles.

ICA, which owns a number of single-asset concessions on top of its stake in Farac, looks like the best-placed candidate, though OHL and IDEAL also have assets that might be attractive to the Afores. A winner announcement is due shortly for the frequently-delayed follow-up to Farac, a slimmed down package of roads, also in the west of Mexico, dubbed Farac 2.

### **Red de Carreteras de Occidente**

Status: Trading began 2 October 2002

Size: Ps8.55 billion

Location: Mexico

Description: Equity offering by holding company for 557km toll road portfolio

Sponsors: Goldman Sachs Infrastructure Partners, ICA

Bookrunner: Santander

Sponsor legal counsel: White & Case

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