European Airports Deal of the Year 2008

06/02/2009

BAA Funding: Window planes

The £15.54 billion ($22 billion) refinancing of the BAA airport assets exploited not one but two business windows. The first was the comparatively benign credit market conditions in the early part of 2008. The second was in lender and rating agency perceptions of the UK's airport regime. BAA had to take a financing structure – the whole business securitisation – and make it conform to the needs of the bank market. Other regulated utilities in the UK may need to follow its lead, depending on how the country's capital markets recover.

Ferrovial, as lead sponsor, brought to market the largest airport financing ever, and 2008's largest infrastructure deal. It needed to overcome a series of objections – from the rating agencies, but also BAA's pension fund trustees, the UK's competition authority, and public perception of BAA's performance. BAA opened a new terminal 5 at its flagship Heathrow airport to very public teething troubles, and has recently been caught up in the debate over the addition of a new runway at Heathrow.

Ferrovial (62%), Quebec's CDPQ (28%) and Singapore's GIC (10%) took BAA private for £10.26 billion in 2006 and have since faced persistent speculation about how they planned to finance both the purchase price, set after a bidding war, and the group's capital expenditure needs. BAA, which had been privatised in 1987 as owner of London's three largest airports, faced investigation from the UK Competition Commission and its Civil Aviation Authority.

Refinancing the almost £9 billion in acquisition debt would require diligent attention to the needs of the ratings agencies, which assumed outsized importance on a transaction this size. In fact while the whole of the period since July 2007, when BAA sat down to work on the financing, has been overshadowed by the credit crunch, the crunch's vicissitudes account for much less of the time it took to close the deal than the agencies.

At the heart of the process were two decisions. The first was to split the airports into regulated, or designated, and non-regulated, or non-designated, airports. The second was to use a whole business securitization structure to maximise the leverage that buyers could achieve on the regulated assets. A shared services provider owned by the BAA parent company conducts the operations for both airports, and could be replaced in the event of a default by that parent. Once the agencies were comfortable with the structure of the financing, and the fundamentals of BAAs business, the sponsors planned to use bonds to refinance the acquisition debt.

The capital markets, however, have not been accommodating. Banks stepped up to provide the refinancing when the bond market looked inhospitable. The lead arranger group for the designated airports – Heathrow, Gatwick and Stansted, as well as the Heathrow Express rail link – is Banco Santander, BBVA, BNP Paribas, Caja Madrid, Calyon, Citigroup, HSBC Bank, Royal Bank of Canada, and RBS. For the non-designated airports – Edinburgh, Glasgow, Aberdeen and Southampton – Citigroup, Export Development Canada, HSH Nordbank, ICO, ING, La Caixa, and RBS are arrangers.

The designated airports senior debt breaks down into a £7.15 billion, of which £4.4 billion is a A-rated (Fitch) refinancing facility and £2.75 billion is a BBB-rated capex loan, a £440 million European Investment Bank loan, also for capex, £600 million in liquidity facilities, and £4.5 billion in existing bonds, which have been brought into the new issuing vehicle in exchange for a fee to bondholders. The A-rated debt is priced at 175bp over Libor, and the BBB-rated debt at 225bp. The margins are based on the amount of bank debt outstanding, giving BAA an incentive to refinance some of this in the bond market.

The senior debt retired £400 million of £2 billion in existing subordinated debt, whose holders, after considerable and vocal griping, agreed to move to a holding company for the regulated airports, also for a fee. The seven-year non-designated airport debt consists of £1 billion in term loans and £255 million in capex and working capital facilities. It is believed to be priced at a slightly higher level than the designated airport debt, and has not yet syndicated.

BAA had to convince agencies and lenders that the financing would survive a recommendation from the UK Competition Commission that it sell some of its airports. Indeed, after the financing closed, BAA retained RBS and HSBC to explore a sale of Gatwick airport, the second-largest of its assets, which is now going ahead. According to a report from Fitch, a sale of one of Gatwick or Stansted would not have a material effect on its ratings, although it says that a sale of two, as the CC has recommended, might spark a revision. The proceeds from any sales would be used to pay down debt, with the outstanding bank debt being paid down first.

The securitisation structure measures debt issuance as a percentage of the designated airports' regulated asset base (RAB), much as a water utility securitisation would, though the RAB is calculated yearly rather than every five years, as happens in the water industry. If the borrower exceeds set thresholds, then dividends are trapped. The Civil Aviation Authority sets caps on the passenger fees that the airports can charge, with the most recent review covering the period 2009-13. The review also covered capital expenditure during this period, for which BAA will need to issue additional debt.

There are tentative signs of a thaw in European capital markets, particularly for the continent's larger multi-utilities. BAA, even with the publicity its runway and terminal have attracted, should, with the £50 billion funding programme documented, be able to move fast if the opportunity presents itself. If not, then the UK's water utilities, several of which have imminent financing requirements, will look to follow BAA's lead in accommodating bank lenders.

BAA Funding
Status: Financial close 20 August 2008
Size: £13.3 billion
Description: Refinancing of BAA leveraged buyout by Ferrovial in 2006.
Sponsor: Ferrovial, CDPQ and GIC
Lead arrangers designated airports: Banco Santander, BBVA, BNP Paribas, Caja Madrid, Calyon, Citigroup, HSBC Bank, Royal Bank of Canada, RBS
Lead arrangers non-designated airports: Citigroup, Export Development Canada, HSH Nordbank, ICO, ING, La Caixa, RBS
Sponsor financial adviser: Macquarie
Borrower legal counsel: Freshfields
Lender legal counsel: Clifford Chance