Birmingham Hospital: Benched

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The £650 million ($1.2 billion) financing for the Birmingham hospital PFI closed on 15 June. It broke the record for the lowest pricing yet for an index-linked PFI bond, set in February by the M1/Westlink motorway in Northern Ireland and matched in April by the Capital Hospitals issue.

Issued through the SPV Consort Healthcare (Birmingham) Funding PLC, the project's sponsors raised £400 million, including £55 million in variation bonds, at a price of just 51.4bp over inflation-linked gilts, compared to 51.5bp for M1/Westlink and Capital Hospitals. Consort has also taken out a £225 million EIB loan (with a £25 million variation facility) due in 2039. The senior notes mature in 2044.

Birmingham's sponsors are Balfour Beatty, which holds a 40% equity stake in the project, Royal Bank Project Investments (30%) and HSBC Infrastructure Fund Management (30%). Together these form Consort Healthcare, which is now the concessionaire on five acute hospital PFI projects.

FGIC is the monoline guaranteeing the financing, which is wrapped up to AAA from an underlying BBB- S&P rating, while RBS managed the issue.

University Hospital Birmingham NHS Foundation Trust and Birmingham & Solihull Mental Health NHS Trust together award the concession for the project. It involves the design, building, financing and operation (DBFO) of a 1,213-bed super hospital and a new psychiatric facility on the site of the existing Queen Elizabeth Hospital site in Edgbaston. Consort Healthcare will also deliver a 32-bed mental health unit at Showell Green Lane.
Under the base-case model, the project's average annual DSCR is 1.22x and the minimum DSCR is 1.20x. The project's gearing is 92%.

Apart the record pricing, the project is notable for being the first PFI bond issue for an NHS foundation trust hospital, since previous projects in Cambridge and Sheffield were both financed using bank debt. This caused some complications for the project, because the original monoline, MBIA, pulled out last year.

NHS foundations trusts are granted a large degree of autonomy over how they run their budgets, and the fears that led to MBIA's departure concerned what would happen if the trust were to run into financial difficulties. In such an eventuality, a Department of Health guarantee promises to cover the trust's PFI liabilities, but MBIA, whose legal adviser was Clifford Chance, was worried that this guarantee could be deemed ultra vires if challenged in court. While the S&P report concedes that such an outcome is possible, it considers it unlikely.

Another complicating factor was the Department of Health suspending acute hospital PFI projects in December, pending a review of costs. This review ended up having little direct effect on the Birmingham project, and was targeted more at the St Bartholemews and Royal London Hospitals PFI – the projects funded by the Capital Hospitals issue. However, the net effect was to cause a bunching of projects, whereby investors were pitched three acute hospital projects at once.

Birmingham closed just one week after the £327.7 million St Helens & Knowsley Hospitals PFI, a 41-year DBFO concession for two acute hospitals with a total capacity of 927 beds.

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FSA was the monoline wrapping that deal, which consisted of a £151.2 million issue (including £25.3 million of variation bonds), maturing in 2047, and a £176.5 million EIB loan with a 32-year tenor.

Sponsored by a consortium of Taylor Woodrow and Innisfree, with the issue managed by Barclays Capital and Dresdner Kleinwort Wasserstein, St Helens & Knowsley priced at 52.7bp over RPI-linked gilts.

Large PFI banks engaged in asset swapping bought approximately 70% of the St Helens issue, minimising the role of traditional investors like pension funds and insurance companies. They were also the dominant buyers of notes in the Birmingham issue, and Capital Hospitals before that.

Asset swappers have become a major force in the PFI bond market over the past year, with one buyer, thought to be RBS, snapping up the entire £320 million Central Nottinghamshire Hospitals issue in October 2005.

Banks are buying the notes to exploit arbitrage opportunities created by swapping them into floating rate assets; one banker estimates he can get 35bp over Libor or more for an asset originally priced at 55bp over RPI. Thus the banks are able to match assets with floating rate liabilities while getting a good price for AAA-rated notes.

This has resulted in a highly liquid market for index-linked bonds and helps to explain why Birmingham is the second project this year to set a new pricing record for the sector. Birmingham was also able to beat the pricing on Capital Hospitals – where St Helens & Knowsley was not – because of the four big monolines, FGIC is the one with the least paper already in circulation. The small difference in pricing between Birmingham and Capital Hospitals, however, suggests that margins may now have bottomed out.

Although no more Department of Health reviews are pending, deal flow is likely to remain lumpy as the spotlight begins to shift away from big acute hospitals and towards smaller LIFT clinics. The next wave of hospital projects should arrive at the end of this year or the beginning of next, and is expected to include the £761 million Leicester hospital PFI. However, if the NHS trust awarding the concession is granted the foundation status that it has applied for, things could become interesting, as the monoline working on that deal is MBIA.

Consort Healthcare (Birmingham)
Status: Closed 15 June
Size: £705 million
Location: Birmingham
Description: Wrapped RPI-linked bond and EIB loan for DBFO hospital concession.
Sponsors: Balfour Beatty, Royal Bank Project Investments HSBC Infrastructure
Debt: £650 million
Lead manager: RBS
Monoline: FGIC
Borrower legal: Tods Murray
Monoline legal: Allen & Overy
Concession awarder legal: Pinsent Masons

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