Indiana Toll Road: Giant step

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Macquarie Infrastructure Group and Cintra have reached financial close on the acquisition of the lease of the Indiana Toll Road. The deal is the largest PPP financing in the US to date, and one of the largest globally in 2006. Most significantly, it has adopted some of the innovative swap technology that featured on the refinancing of the Chicago Skyway concession.

The lead arrangers of the $4.063 million in debt for the concession are BBVA, BNP Paribas, Caja Madrid, DEPFA, Dexia Credit Local, Royal Bank of Scotland and Banco Santander. The seven are all joint bookrunners for the financing, although an inner group of three – RBS, BNP and BBVA – are understood to be taking the most active role in syndication, which launched at a London bank meeting on 5 July, since they are most interested in bringing down their final hold positions in the debt.

The Indiana Toll Road is a 175-mile toll road running across the northern part of the state of Indiana.
The lease, for which the state raised $3.8 billion, has a shorter term than Skyway's – 75 as opposed to 99 years – and has a provision that the state cannot build a similar competing road within 10 miles of the existing route. It also has a provision within the concession agreement that the concessionaire must build expansion capacity on the road should traffic reach pre-agreed peak traffic levels. The state, however, would be ultimately responsible for the acquisition of land for this purpose.

The terms – particularly those governing the financing and lender step-in rights – were substantially unchanged from Skyway. The request for proposals went out on 28 September 2005

Macquarie and Cintra's winning bid was $3.8 billion, while second-placed Babcock & Brown bid $2.8 billion, but said that if the triggers for the expansion work changed from those based on peak traffic to those based on average traffic, it could bid $3.25 billion. Itinere bid $2.52 billion, and Morgan Stanley bid $1.9 billion.

The winning bidder, which was selected on 23 January 2006, would note that the price was based on what it thought, based on traffic studies, the road was capable of producing (the state used a Wilbur Smith study, produced before the bid, while Cintra and Macquarie used Maunsell). However, the amount of revenue available over the entire 75-year concession would comfortably cover the bid – the winners would also be those with the best access to long-term financing.

The concession features a large amount of capex – $573 million in maintenance and $525 million in renewal, replacement and expansion over the first 25 years. It also includes some increases in tolls, although fewer than initially envisaged, so that long-term wrapped bank or bond solutions would need to contend with potential revenue volatility. The ratings agency verdict may also have been unfavourable, although sources close to the deal say that they were not formally approached for such a deal.

What the sponsors have achieved, however, is a much more impressive initial level of gearing than the first Skyway bank deal. Skyway went from a 60:40 debt:equity ratio to an 83:17 ratio between a December 2004 bank deal and the August 2005 bond refinancing. The Indiana deal features gearing of 81.3%, more if one includes additional capex and liquidity facilities. Macquarie estimates that it can achieve a 13% internal rate of return, and a 15-year equity payback period.

The two sponsors contributed $374 million in equity each, while the banks provided an acquisition facility of $3.24 billion, an undrawn capex facility of $665 million, and an undrawn liquidity facility of $150 million. The banks split the debt equally, and funded on 29 July, while the state received the lease payment on 30 July.

The debt featured a step-up swap, which mirrors in its effect the accreting swap of the Skyway refinancing. The result of the swap, a combination of an asymmetric swap and an interest rate hedge, is that the project company – ITR Concession Company LLC – defers some interest payments on the nine-year acquisition debt until maturity, thus increasing the amount of debt that the project can support. As one banker at the arrangers put it "the deal is a nine-year miniperm, so we're exposed to refinancing risk anyway." The swap, however, which resembles an additional loan commitment, still requires a liquidity facility to ensure repayment in the early part of the concession.

In fact, the deal does feature some spurs to a refinancing – including cash sweeps later on in the life of the loan – and a refinancing is extremely likely, either in the bond market or the wrapped bank market. The banks are not understood to be eager to extend the swap product to any and every infrastructure deal, but long-term concessions for existing assets may have a chance of bringing them round.

The deal is understood to be priced notionally at between 95 and 125bp over Libor, although the swap arrangement allows for prearranged increases in a fixed coupon over time. The initial interest rate is 3.15%.

The deal should achieve a strong response in subunderwriting, and later bank meetings are planned in September for New York and Madrid. Less positive has been the response of the Indiana public and some of its legislators. Daniels won approval for the sale in the state legislature on the back of toll freezes. Until the project company installs electronic toll collection, rates for two axle cars will be frozen, with the state government making up the difference to the project company. Thereafter, drivers will apply directly to the state for a refund until 2016. Many politicians, however, have been able to appeal to xenophobia in denouncing the road's sale to a Spanish company and an Australian-managed (the key here being managed, rather than owned) fund.

The impact of the toll freezes on state finances, however, have been described by one source close to the state as "a financial footnote." While the elections in Indiana may be altered by sentiment against the lease, other states, which currently have sales of the table, may follow Indiana's lead once the November 2008 elections across the US are over.

ITR Concession Company LLC
Status: Closed 29 June, currently in subunderwriting
Size: $3.8 billion
Location: Indiana
Description: 75-year lease of a 157-mile toll road
Sponsors: Cintra, Macquarie Infrastructure Group
Debt: $3.24 billion acquisition facility, $665 million capex facility, $150 million liquidity facility
Arrangers: BBVA, BNP Paribas, Caja Madrid, DEPFA, Dexia Credit Local, Royal Bank of Scotland and Banco Santander
Sponsor legal: White & Case
Lender legal: Orrick
Seller legal: Mayer Brown Rowe & Maw and Ice Miller
Seller financial adviser: Goldman Sachs