

# Corredor Sur: Panama unwrapped

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01/06/2005

ICA has completed a refinancing of the Corredor Sur road concession in Panama – a rare, and daring, issue of bonds in the dollar market to finance an emerging markets toll concession.

The \$150 million bond financing, led by Merrill Lynch, is the first dollar-based financing of a Latin American road asset since Chile's Maipo financing in 2001. It gives an indication of the degree to which assets that are well structured can access long-dated capital.

The most obvious advantage that a Panamanian road has is the country's dollarised economy which eliminates currency and conversion risk. However it does not eliminate some of the legal and economic disadvantages of lending to an emerging market. In particular the bondholders have to be comfortable with a concession that relies upon the health of the Panamanian economy to maintain strong traffic revenue.

Corredor Sur is a 19.5km toll road linking Panama City's financial district to the Pan-American highway and the city's main airport. It has four lanes and runs parallel to a free route. The free route is so congested that a trip to the airport can take up to two hours. At peak time the road is converted to running in one direction.

The project company for the concession is ICA Panama, which has assigned its rights under the concession to the issuer, the Corredor Sur Trust. ICA Panama's owner, via Florida-registered holding company ICATECH is Empresas ICA, one of the largest construction firms in Mexico. ICA won the 30-year concession from the country's Ministry of Public Works in 1995, and funded the road's construction using bridge loans. The first section of the road was complete in June 1999, and the second in February 2000.

In September 1999, ICA closed a \$70 million financing with the International Finance Corporation (IFC). This consisted of A loans and C loans and a B loan through WestLB and Banco Santander. The new bond issue refinances the loans, which have \$52 million outstanding, funds reserve accounts and transfers funds up to ICA.

The concessionaire primarily makes a return on the road from optimising toll levels and maximising revenue. But it also makes a return from the development and reclamation of land that is included in the concession. The government has transferred 25.4 hectares out of the 29.5 hectares of land promised under the concession and 23.4 hectares out of 35 hectares of fill-in rights. ICA has so far sold 48.3 hectares of this land, but the remaining land is not among the concession rights assigned to the issuer.

The timing of the refinancing is driven more by the performance of the concession than any financial exigencies. The IFC debt was due in 2011, but the road has been performing well even in the aftermath of a rise in toll levels in 2002.

The toll increase is presented by Gabriel de la Concha, director of project finance at ICA, as an exercise in measuring the elasticity of demand on the road. The toll rates for travelling along the length of the road are \$2.40, \$4.15 and \$6.05 for cars, buses and commercial trucks, respectively. Toll revenues were \$17 million in 2004 and \$4.3 million in the first three months of 2005. The recovery from the toll increase, which took place in June 2002, convinced the sponsors that the road could support the revenues necessary for a larger long-term financing.

ICA spoke to several bond and bank debt providers as well as to several monolines, and Merrill Lynch was able to convince ICA that the uncovered risk was something that bondholders and ratings agencies could accept. The latest of several studies – in this instance from Halcrow – suggested a number of scenarios:

- A base case assuming toll increases of 25% in July 2005 and July 2007 with the growth rate of background traffic declining at 1% per year from 2006. This showed revenues reaching 34.9 million in 2029, a 2.9% average annual increase in revenues from 2004.
- A no toll increase case with the growth rate of background traffic declining at 1% per year from 2006. This would produce revenue of \$28.9 million in 2029, a 2.1% average annual increase from 2004.
- An optimistic case assuming two 25% toll increases in real terms and with the growth rate of background traffic declining at 0.5% per year from 2006.

This forecast depends on there not being a prolonged recession in Panama, the inability of the government to construct a fast and free alternative route, and road users maintaining the same attitude to tolling that they had in June 2002.

The macroeconomic indications are promising. The solid growth of the Panamanian economy and the recent re-election of a centre-right government promises a friendly atmosphere for the operator.

In December 2004, ICA settled arbitration with the Panamanian government over additional works on the concession. It was awarded a payment of \$25 million, although ICA has not yet collected. That brought the total value of the concession up to \$207.4 million.

The bond indenture contains restrictions on the upstreaming of dividends to the sponsor if the concession does not meet certain debt service coverage ratios. It also calls for a \$10 million debt service reserve account, a major maintenance reserve account, and a \$1.8 million litigation reserve account. These structural provisions, combined with the strength of the road, allowed Fitch to give the debt a BBB rating.

The bookrunner Merrill Lynch priced the bonds as planned on 20 May, and the issue, due 2020, has a coupon of 6.95%. There are few concessions offering the advantages of a dollarised economy, and few with as strong fundamentals available. But those at the top end of the range should look carefully at ICA Panama's reception.

### **Corredor Sur Trust**

Status: Closed 20 May 2005

Size: \$207 million

Location: Panama

Description: Refinancing of 19.5km toll road

Sponsor: ICA

Bookrunner: Merrill Lynch

Maturity: 2020

Coupon: 6.95%

Lawyers to the underwriter: Mayer Brown Rowe & Maw (international), Arias Fabrega & Fabrega (local)

Lawyers to the borrower: White & Case (international) Galindo, Arias & López (local)

Traffic consultant: Halcrow

Onshore trustee: BG Trust

Offshore trustee: Bank of New York

Auditor: Deloitte

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