H3G Italia SpA

01/02/2003

European Telecoms Deal of the Year 2002

Hutchison Whampoa's last 3G financing, for its UK operation, gained plaudits as one of the few third generation mobile licence winners to gain finance in a souring market. That £7 billion deal featured a bullet maturity, leaving lenders and sponsors exposed to refinancing risk. The solution to its Italian operation's financing needs, in an even more depressed market, was a fully amortizing deal, and the largest one in the sector this year.
Hutchison finds itself in a similar position in the Italian market as it was in the UK. It is a new entrant to a very competitive, mature and well-penetrated sector. Italy, moreover, came third, after Germany and the UK, in the sum of money it was able to extract from prospective 3G licence holders.This adds up to a considerable challenge in building out a network in Italy, with the added context of a decline in vendor willingness to put together substantial sums for this purpose. For this transaction, therefore, banks were forced, or rather able, to rely on the corporate credit of Hutchsion Whampoa. Since Hutchison is one of the largest and most cash-rich corporates in Hong Kong (its ability to cash out of Orange at the height of the telecoms boom leaves other operators envious), this was no great burden.Indeed, Hutchison is far more in control of its Italian venture than it was of the UK project. Its partners are NHS Investments S.A. (5.639%), Bernabè Mobile Investments 2 S.A. (2.256%), CIRtel International S.A. (1.825%), HdP SpA (1.128%), Gemina SpA (0.564%), and Tiscali Finance S.A. (0.360%). Over 88% of the equity, therefore, is in Hutchison's hands.Banks, however, were wary of taking on further 3G risk, especially as the Mobilcom transaction, a bridge financing for France Telecom's German 3G ambitions, began to unwind. In this atmosphere, lenders wanted to see their principal back on a telecoms deal. Since the prospects for the take-up of 3G service, and the likely revenue per consumer, are still a matter for conjecture, an amortizing structure would require some enhancement.The deal is, therefore, best seen as a limited recourse deal, since much of the debt carries a guarantee from Hutchison corporate. Of the total Eu5.2 billion debt package, Eu2.2 billion commences with a full guarantee and Eu1 billion comes in the form of subdebt provided by Hutchison. There is also a Eu1 billion vendor tranche, and the project's network equipment suppliers are Ericsson and Siemens. In recognition of this, participants on the vendor piece include EKN, KfW, Nordea and HSBC. NEC, Alcatel and Motorola are also supplying the project.The final portion is a Eu1 billion non-recourse tranche. The use of this debt, like the degree to which the recourse portion is guaranteed, is linked to various performance milestones. These have been used on telecoms financings for some time, and were perfected on the competitive local exchange carrier (CLEC) deals of 1999-2000. These linked drawdown on facilities to such factors as network rollout, subscriber numbers and Ebitda. As a result, when the CLECs went bust, very few lenders were hurt.In the case of H3G Italia, the non-recourse tranche cannot be drawn down until certain subscriber numbers, revenues and coverage standards have been achieved. These are broadly similar to the tests that must be passed before Hutchison Whampoa can relieve itself of the Eu2.2 billion debt burden. As its CFO, Frank Sixt, pointed out last year, however (see Project Finance, July 2002, p.17), he expected that the corporate's net debt to capitalisation would probably be below 10% for 2002.Since the sponsors have put Eu5.1 billion into the deal, it is very conservatively leveraged. Nevertheless, the syndication of the project's debt conformed to the ? inverted pyramid? structure common to telecoms deals. Lead arrangers were ABN Amro, Banca Antoniana Popolare Veneta, BOCI Capital, China Construction Bank, Centrobanca, Crédit Agricole Indosuez, Deutsche Bank, Development Bank of Singapore, HSBC, IntesaBCI, JP Morgan Chase, Royal Bank of Scotland, Société Générale., Unicredit Banca Mobiliare, and WestLB. The participant list is much smaller, and comprises Bank of China (Hong Kong), San Paolo IMI,

Bank of China, Singapore Branch, Skandinaviska Enskilda Banken, Nanyang Commercial Bank, Limited, Bank of China (Canada), Bank of China, Sydney Branch, and Chiyu Banking CorporationThe deal has a 9.5-year tenor, and all of its tranches, with the exception of the subdebt, rank pari passu. The make-up of the bank list gives some clue as to the strengths of the transaction ? Chinese banks are extremely comfortable with Hutchison corporate risk, and willing to extend themselves in its service. Italian and wider European banks will be looking for ancillary opportunities if and when H3G grows into a dominant player.The word the lenders like to stress on the deal is flexibility ? an important attribute for a deal that is dependent on the ultimate unproven technology. H3G Italia's strategy is to go after opinion formers and early adopters, and it was able to persuade the Italian prime minister, Silvio Berlusconi, to accept the country's first 3G mobile number.

H3G SpA

Status: signed June 2002

Size: Eu10.3 billion

Location: Italy

Description: Greenfield financing of a UMTS network

Sponsors: Hutchison Whampoa (88.228%), NHS Investments (5.639%), Bernabè Mobile Investments 2 (2.256%), CIRtel International (1.825%), HdP (1.128%), Gemina (0.564%), and Tiscali (0.360%)

Debt: Eu5.2 billion, of which Eu1 billion comes from vendors, Eu1 billion in Hutchison subdebt, 2.2 billion has a corporate guarantee, and Eu1 billion is non-recourse, subject to drawdown conditions.

Arrangers: ABN Amro, Banca Antoniana Popolare Veneta, BOCI Capital, China Construction Bank, Centrobanca, Crédit Agricole Indosuez, Deutsche Bank, Development Bank of Singapore, HSBC, IntesaBCI, JPMorgan Chase, Royal Bank of Scotland, Société Générale., Unicredit Banca Mobiliare, and WestLB

Vendor finance: Nordea, HSBC, KfW, EKN

Lawyers to the lenders: Allen & Overy (banks), Clifford Chance (vendors)

Lawyers to the sponsor: Freshfields Bruckhaus Deringer

Technical consultant: Arthur D. Little