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A28: First index

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July saw the first ever index linked euro-denominated project bond successfully sold down into the capital markets. Project company Autoroute de Liaison Seine-Sarthe (ALIS) has raised Eu460 million to fund buildout of the A28 toll road project in France. It follows a Eu256.5 million fixed-rate issue by the Portuguese road project, Algarve, in August 2001 but sets a new precedent for being index-linked.

ALIS was awarded a 62-year build-own-operate-transfer (BOOT) concession by the French government in December 2001. The contract entails construction and operation on a real toll basis of 125km of the A28 road between Rouen and Elencon. This section is the missing link in the Trans-European-Network that connects Northern Europe with the Iberian peninsular. The rest, a mixture of real and shadow toll roads, is already built.

ALIS is dominated by Bouygues Construction's subsidiaries, which together hold 44.84% of the project's equity. The remainder is made up by CDC IXIS, HBOS, EGIS and French public sector-owned concessionaire SAPN. The Bouygues subsidiaries have the contract for construction, due to commence in the first quarter of 2003 and featuring a completion guarantee from the parent. The operation and management will be carried out by a joint venture between EGIS and SAPN. The road should be up and running and collecting revenue in December 2005.

CDC IXIS was appointed financial adviser in 1999, just prior to the beginning of bidding. At this time the plan was a traditional package using banks and private placement. EIB funding was also considered, an option favoured by the A28's toll road predecessors in Portugal. However, by the time the deal had closed, a market for index linked project bonds was emerging in euroland. Given the project's long concession period and the index-linked nature of toll revenues, a decision was made that this route offered the best value solution.

The project has a significant boost from additional funds in the form of a non-repayable grant. Half each of Eu343 million is put up by the French state and regional government. At a fairly late stage, the sponsors opted for a sub debt tranche to supplement the senior debt bonds. HBOS stepped in to put up this Eu37.9 million over 17 years.

The bonds split into three tranches of differing maturities, all wrapped by FSA and thus boasting a AAA/Aaa rating. A Eu200 million issue with a 30-year tenor came in at 85bp over Oati (the French government inflation linked bond) with a coupon of 4.3%. A Eu180 million tranche maturing in 25 years has a spread of 81bp over Oati with a 4.25% coupon. Finally, a Eu80.5 million issue maturing in 15-years came in at 60bp over the Oati with a 3.99% coupon. CDC IXIS' subsidiary CDC IXIS Capital Markets acted as sole lead manager and bookrunner.

With no euro-denominated index-linked issue preceding this deal, there is no real frame of reference for gauging pricing. Inflation linked debt in France is usually issued by state and public entities and generally carries much shorter maturities. So there is no real domestic benchmark either. However, the A28 bonds are said to have sold down with great ease. Almost 80% of the investors were French and the Caisse d'Epargne network took 80% of the 15-year tranche. The remaining participants were insurance companies, asset managers and banks from Austria, Germany, the UK and Scandinavia.

All three tranches are repaid as bullets on maturity. The staggered structure is designed to ensure that debt is cost-effective from day one whilst minimising negative arbitrage at the end. The FSA wrap guarantees these payments but additional comfort is gained from a cash sweep mechanism. If revenues fall below previously agreed targets, monies are siphoned off from the project and kept for debt repayment.

Market players point to the significance of this deal, saying other European projects will follow suit. Specifically, where infrastructure projects collect inflation-linked revenues over long periods of time, such as toll roads, index linked bonds are well suited. This trend is already evident in other markets, namely the Australian dollar and sterling. The A28 sees euro-denominated projects heading the same way.

The FSA wrap was said to be crucial to success. Even with this, participants highlight a number of attributes that lent this deal well to pioneering index-linked bonds. Primarily, the unusually long concession period and proven traffic flow on existing sections of the Trans-European network considerably mitigated risks normally associated with toll roads. Moreover, French motorists are no stranger to paying tolls. Deals that can not boast such a degree of comfort, particularly greenfield projects, may have trouble attracting funds from a source so new to the scene. It is often suggested that bonds are only really suitable for refinancings.

Having said this, as the euro bond market matures, the utilisation of index linked project bonds will undoubtedly become more widespread. FSA has stated that it is looking at a number of projects across Europe, both greenfield and refinancing. The main driver behind growth of the euro bond market is a growing interest amongst investors. The advent of the euro has removed currency trading as a source of yield for the region's investors and they are having to look elsewhere. In addition, small local banks who were previously restricted to domestic deals can move all over Europe and finally, a growing number of pensioners on the continent means an increasing number of investors in the form of pension funds.

Autoroute de Liaison Seine-Sarthe
Status: Closed August 2002Size: Eu900 millionLocation: FranceDescription: Bond financing of a greenfield real toll roadSponsor: Bouygues Construction subsidiaries (namely Bouygues Travaux Publics, DTP Terressement and Quille), HBOS, CDC IXIS, EGIS and SAPNMonoline: FSALead manager and bookrunner: CDC IXIS Capital MarketsSenior debt: Eu460 million senior debt bonds, broken down into three tranches with bullet maturities at 2017, 2027 and 2032Subordinated debt: Eu37.9 million mezzanine facility put up by HBOSFinancial adviser to sponsor: CDC IXISLegal adviser to CDC IXIS and FSA: Freshfields