European Telecoms deal of the year

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The growth of bank financings of start-up telecoms business took its cue from the Jazztel transaction. Jazztel signals that operators can find ways to make banks comfortable, and that project finance lenders can adapt themselves to the fast-moving European Telecoms market.

Spain's first Competitive Local Exchange Carrier (CLEC) is a capital hungry operator, keenly aware that first entrant status alone would not bring them the subscriber base they needed to survive. Large expenditure on rolling out their E1-4U network was required and the feeling was that the high-yield market's ability to fund this debt was not unlimited.

Jazztel was formed by ex-Viatel entrepreneur Martin Varsavsky in late 1997, and since then has been aggressively marketing its services in a country with one of the lowest fixed-line penetration rates in Europe. Jazztel wants to create a broadband, branded proprietary network throughout the Iberian peninsular with substantial Internet interests bolted on. Signs are that its success in attracting customers is forcing a faster rate of capex than the business plan envisaged.

Given the uncertain rate of expansion, Jazztel decided to replace vendor financing arranged through Nortel with a formal contract for supply with a Nortel/Sainco venture, UTE Norsanet, worth $212 million. Jazztel required rapid access to capital, and banks were looking at expanding their telecoms competence. The s300 million credit facility that emerged was a real test for the lenders- how to set conditions for a company with no operating history and whose future flows were dependent not only on their own marketing efforts but also the state of competition within a rapidly deregulating market.

The facility comprises two tranches of s100 million and s200 million, available between November 1999 and December 2000, and until June 2002 respectively. Draw-down, however, is conditional on senior debt/revenue multiples and that five cities are connected to the network, with the second tranche meeting more stringent tests in both regards. More importantly, a comprehensive charge on Jazztel's assets and shares was also established to increase bank comfort.

The facility was put together in a very short time and closed in August oversubscribed, lead arranged by Argentaria, Chase Manhattan, Barclays Capital, Dresdner Kleinwort Benson, JP Morgan and Lehman Brothers. It was priced on a relative value basis and linked to an Ebitda grid, bringing the average blended margin to 312.5bps over Euribor, considerably lower than the coupons offered on the telecoms staple the high yield.

Jazztel has, however, also enjoyed great success in gaining funding on the high yield and equities markets, raising s200 million in an April bond issue and a further s200 million and s400 million in an IPO and high yield issue respectively. Jazztel believes that the financing agreed, even if not yet used, provided a useful symbol of confidence for investors even in the telecoms friendly markets of 1999.

Jazztel's current expenditure levels have come down, it says, to being a victim of their own success ? high capex is needed to connect their rising band of subscribers. It would be unable at present to use the facility, but some of the more ambitious parts of the business plan, including ?Project Carmen?, a subsea cable to the UK, might require a great deal more. And, in a business where operators need to get their hands on money as quickly as possible, and banks have learnt to put the necessary structure in place to provide this, it's likely to become a staple of financings in the year ahead.