

Cross-Israel: A bigger ticket

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Financing for the Cross-Israel \$1.35 billion toll road project closed at the end of October. It is the largest deal in the country to date and sets a milestone for the future of project finance in Israel.

The project involves the construction of an 86km north-south highway around Tel Aviv, Israel's biggest city. The Derech Eretz consortium comprising, AGRA, Armbro Enterprises, BFC Construction Corporation, Canadian Highways International, Africa Israel Investments and Israel's Housing & Construction Holding, is developing the project. The highway will eventually be between 250km and 300km long.

In addition to \$150 million in equity, financing is split into two parts - Bank Hapoalim lead arranged an \$850 million facility syndicated within Israel, while Toronto-based Newcourt Capital lead arranged a \$250 million bond private placement to be sold within the North American market.

Syndication for the \$850 million fixed rate tranche closed oversubscribed at the beginning of October. Bank Leumi Le-Israel, Israel Discount Bank, United Mizrahi Bank and Industrial Development Bank of Israel joined as participants. An Israeli pension fund, Mivtachiz, joined the deal making it the first in the country to include an institutional investor.

Duration of the Israeli facility is between 20 and 21 years at the end of which 29% of the total costs will be recovered. Revenues from the remaining 9 years out of the 30-year long concession will pay the residual 61%. The price of the facility is set at 2% above government bonds.

Israeli banks are showing an increasing appetite for project finance. According to Dr Ehud Kaufman, senior assistant managing director in corporate finance at Bank Hapoalim in Tel Aviv: "Project finance is a word loosely used in Israel and it applies to any sort of non-recourse deals. Nevertheless financing of Cross-Israel has paramount importance for the future of project finance in the country. The project has been a good achievement for the Israeli government in terms of being able to run a very competitive bid. The project gives a splendid view of the government's achievements."

Kaufman believes there are big opportunities for local and international sponsors and financiers interested in doing deals in Israel. The most promising sector is infrastructure, with a number of rail projects due to be tendered in an attempt to alleviate some of the problems related to car traffic around greater Tel Aviv. Other plans include development of power stations and distribution of natural gas across the country's territory.

Syndication for the \$250 million tranche was launched at the end of October but has not closed yet. Signing is expected by the end of first quarter of 2000 depending on appetite in the North American market. Boston-based John Hancock Mutual Life will join at syndication level.

A source close to Newcourt Capital claims the deal is solid: "Things have improved a lot over the last 15 years with Israeli inflation declining from three digits figures in the mid-1980s to 6% in 1998 and a forecasted 5% by the end of 1999."

Legal counsel on Cross-Israel comprised Allen & Overy advising the lenders with London-based Freshfields advising the consortium. White & Case acted for the Israeli government.

Kent Rowey, partner and head of project finance at Freshfields in London says: "Cross-Israel is the first deal to involve

multi currency financing. It has not been an easy task arranging it. But unlike other countries in the region, contracts in Israel can be written under English law. It is also a country with a relatively strong capital market. Despite the initial difficulties the structure of the deal has been rock solid from the start. The Israeli government has put forward a balance concession program and Israeli sponsors and financiers have learnt pretty quickly what project finance means?, he adds.

The project started in 1995 under the Labour government led by Yitzhak Rabin. Since Rabin's assassination in November 1995 it was carried by the Likud government, under Benjamin Netanyahu, until May 1999, when Labour won again.

There was concern among foreign investors over the potential effects of changes in the Israeli political establishment. But the commitment by the Israeli government to undertake 80% of the entire traffic risk has ensured continuity.

Philip Stopford, partner at White & Case in London says: "The government of Israel has been very cooperative, with the Finance and Construction ministries believing strongly in the deal. Changes in government did not have major impacts on the project."

For those involved on the financing side the project officially kicked off in the second half of 1996, and since May 1997 arrangers have been devoting all their time to it. According to Hapoalim's Kaufman: "This has been a very costly and lengthy process and despite being totally satisfied the bank needs to be paid work fees. It is simply too risky to work three years on a project that might eventually not take off. I am not sure whether the government is prepared to do something similar in the short-term."

The winning consortium was announced in January 1998. Construction starts in the first week of November this year. It take will take four years and will be finished in 2003 when the project will be operational. The first two major sections of the project will be operational within the next two years.

Cross-Israel is part of a longer project that eventually will involve the construction of 300km long highway going from the Lebanese border in the north to the border with Egypt in the southern part of the country.

Cross-Israel is only the second project finance deal to close in Israel and follows the financing of the \$200 million Carmel tunnel project. Big projects to come involve the development of the metro in Tel Aviv.

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