Poland A1 motorway project

Edward Berry

26/10/2005

Many say that Poland's A1 DBFO road project – only the country's second PPP scheme to close to date and one of the largest project finance agreements in Central and Eastern Europe this year – represents another significant landmark for PPP in the EU Accession countries

However, having taken more than a decade to reach financial close, others see the €660m (US$797m) highway project – selected by the European Commission as a quick-start TEN Project – as another scheme that has suffered at the hands of a country where political support for delivering PPPs is wavering.

Furthermore, it remains to be seen whether the second tranche of the first phase of the highway scheme – which is due to secure its financing package early next year – is given the green light by the newly-elected, centre-right government.

Poland's PPP market has always been a touchy political issue and it will take time for the new conservative coalition - which took over power last week - to decide whether or not the flurry of PPP projects represents the best means to tackle the country's infrastructure financing black hole.

Needless to say, the project, although not technically demanding, is significant both nationally and internationally. Once complete it will form an integral part of the North-South Trans-European Corridor No VI, linking the Baltic Sea in the north with Czech Republic, Slovakia and Austria.

Rationale

Like many of the EU Accession countries, Poland set out a large-scale investment programme to upgrade a significant proportion of the country's ageing road network, much of which will be aided by EU funding.

Following the launch of Poland's first privately-financed expressway - the 180km A2 motorway from Swiecko, on the German border to Konin - it was the turn of the A1 to come on stream, having been highlighted as an integral route for the strategic development of Poland's motorway network.

Jan Stylinski, head of PPP at the General Dictorate of National Roads (GDKiA), the government body responsible for the country's road programme says: 'The project is extremely important because [when all phases are completed] it will link the disconnected industrial port of Gdansk, in northern Poland with the southern part of the country.

'It will act as a North-South backbone and will also converge with the redeveloped A2.'

A number of other PPP projects are at pre-approval phase but the A1 and A2 schemes have had the lion's share of the market thus far.

Following hot on the heels of last month's tender notice for the second 180km phase of the A1 between Strykow and Pyrzowice, the €1bn (US$1.2bn) second section of the A2 has also been launched.

In total, GDKiA has plans for 1,535km of motorways to be put into operation by 2013 - with 122km of new roads planned for 2006 alone.

Outside the transport sector however, PPP is showing few signs of any significant movement.

Earlier this year, Warsaw city council pledged US$70m towards a stadium PPP, an initiative that will see the construction of a 30,000-seat facility to host athletics, concerts and Warsaw's two football teams. However, commitments from Poland's sports bodies have been thin on the ground. The same cannot, however, be said of the transport sector.

Background

The A1 upgrade was first mooted in the early 90s and was tendered in the latter stages of 1995 as a single-phased project. After a three-stage tendering process the Gdansk Transport Company (GTC) was selected as preferred bidder by the Polish transport ministry in 1997. The consortium included:

- Bechtel
- Skanska BOT
- Intertoll – South African road operator
- GPRD – Polish construction firm
- BGZ – Polish agricultural bank
- NDI – Polish property developer

Shortly afterwards, the scheme ran into major financial difficulties which, according to Jan Stylinski of GDKiA was primarily due to a flaw in the country's toll road policy.

Stylinski explained that certain clauses of the Polish Toll road act of the late 90s deemed it impossible for the government to provide a guarantee of more than 50 per cent of the scheme's senior debt facility, a proponent that prevented the scheme's players from reaching a financial agreement.

The political will needed to get the scheme up and running again ebbed and flowed over the next few years as the Polish government experienced further shifts in power.

A senior industry source told IJ News: 'The process was very slow, painful and expensive - and subject to political whim. If the country's PPP programme is to be a success story, a proper financing package and a consistent approach across the deals will be needed.'

While the Polish authorities took time to work on securing a financing structure for the project, GTC suffered a number of set backs. Firstly the Polish agricultural bank BGZ and domestic construction firm GPRD dropped out of the group.

Bechtel, a leading member of the consortium, then walked out of the scheme in 2003 for what it labelled 'commercial reasons'.

It was down to the co-leader of the consortium – Skanska – to find a suitable replacement for the American construction giant, a task that the Swedish firm had no hesitations in resolving.

Coran Carlberb, project director for Skanska, said: 'Our immediate choice was Laing Roads, a joint venture partnership that has worked very well in the past. We knew from our combined experience that working together would save us valuable time on the project.'

By 2004, almost 10 years since the project first came to market, amendments to the toll road act had been made and finalised and the government finally committed to co-financing the payment of credit.

Project

Having originally been mooted as a single-phase project, the A1 scheme was split into two to facilitate the project's financing and delivery.

The first phase - which is already in construction - entails the building of a 90km motorway from Gdansk to Nowe Marzy in Northern Poland.

The four-lane stretch of motorway will have additional safety lanes and will feature the construction of 80 small bridges and flyovers.

The scheme's second phase will include the building of a 60km extension at the southern end of the motorway to the city of Tourin.

Skanska and NTL are the project's EPC contractors while Intertoll will operate the motorway until 2039.

Skanska's Goran Carlberg says that as the only technical difficulty facing the three-year construction phase, the high percentage of clay underfoot should not adversely affect the progress of the project

Carlberg says: 'The design and ground conditions do not expose the contractor to risks that are uncommon to road construction in Northern Poland where the EPC contractors have proven experience.'

According to concessionaire forecasts, between 11,000 -17,000 cars will be using the motorway by 2015.

The deal

In August 2004, GTC signed a concession agreement with the Polish Ministry of Infrastructure for the US$680m concession for the first phase of the A1 Motorway.

After the transfer of Bechtel's stake in GTC was finalised, Laing paid €250,000 as initial consideration for its 30 per cent share upon satisfaction of conditions.

The breakdown of shares within the consortium are as follows:

- Skanska BOT - 30 per cent
- Laing Roads - 30 per cent
- NDI - 25 per cent
- Intertoll - 15 per cent

Almost a year after signing the commercial agreement, the scheme's financing package was closed on 29 July 2005.

According to Citigroup's Christopher Blin - financial adviser to the sponsors - there was a great deal of appetite among international banks to finance Poland's second PPP deal.

The competition was won by the European Investment Bank (EIB) which along with the Nordic Investment Bank (NIB) provided the project's senior debt funding of €640m.

EIB is contributing €500m (US$601m) towards the senior debt facility - which has a tenor of 30 years and is priced at 4 per cent - while NIB is providing €140m (US$125m).

The debt comes with a grace period of 10 years.

Acting as sole funders for the project, without any commercial bank guarantees, the multilaterals are taking on real project risk.

The payment mechanism for the project is predominantly availability based with a minority shadow toll element.

Blin says that the contractual arrangements have provided a certain amount of protection for the debt structure and GTC will use an element of the availability payments to service the debt facility.

The total amount of equity pledged for the first phase of the project amounts to €21m (US$24.1m) – Laing's commitment is €11.5m and Skanska's is €9.5m.

Skanska BOT's Coran Carlberb, said: 'Although the equity stake in the project isn't huge, from a contractors perspective it's a huge project to be a part of.'

According to a senior source close to the deal, the financing package and negotiations between all those involved in the deal took so long because they wanted everything to be water-tight, knowing that the project would face fresh scrutiny following the expected change in government.

CMS Cameron McKenna acted as legal adviser to the sponsors, while Citigroup was its financial adviser.

White & Case was drafted in to provide legal advise to the banks and Polish law firm Wardynski & Partners advised the Polish government.

Conclusion

With the A1 project receiving renewed criticism in the Polish press recently, concerns have been raised about whether or not the government will support the delivery of PPPs in the future, let alone give the go ahead for the financing for the A1 second tranche.

It is imperative that Poland commits to a long-term PPP future, otherwise projects like the A1 which need continued investment as part of the TEN-T network, will remain unfinished.

It is high time the Polish government worked out legislature to ease the passage of projects. Part of the nation's reluctance to commit to PPP is driven by the lack of a framework, the rest of the cause is lack of example.

Now that the second road PPP has closed successfully, perhaps Poland will follow in Greece's footsteps and implement the laws necessary to drive its adoption.

The Polish sector can only take off once this happens. In the meantime the industry will continue taking a long time to close projects.

Project at a glance

The project at a glance

Project Name	A1 Toll road
Location	Poland – Gdansk to Torun
Description	Two phases: First phase: 90km highway from Baltic sea port of Gdansk to Nowe Marzy in northern Poland finish in November 2008 Second phase: 60km extension at the southern end of the motorway to the city of Torun
Sponsors	Gdansk Transport Company Laing Roads (30 per cent) Skanska BOT (30 per cent) Intertoll (15 per cent) NDI (25 per cent)
Operator	Intertoll
EPC Contractor	Skanska BOT
EPC Sub Contract 1	NDI
Project Duration (Including construction)	34 years -2039
Construction Stage	2005-2008
Total Project Value	€661m
Total equity	€21m
Equity Breakdown	Laing Roads €11.5m Skanka €9.5m
Total senior debt	€640m
Senior debt breakdown	EIB €500m NIB €140m
Senior debt pricing	4 per cent

Debt:equity ratio	95:5:
Mandated lead arrangers	European Investment Bank (EIB), Nordic Investment Bank
Legal Adviser to sponsor	Cameron McKenna
Financial Adviser to sponsor	Citigroup
Legal adviser to banks	White and Case
Legal adviser to government	Wardyski & Partners
Financial adviser to government	PwC
Date of financial close	29 July 2005