# Limerick road tunnel

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Limerick road tunnel is one of the largest infrastructure projects to close to date in Ireland and has set a benchmark for global transport projects for an interesting financing structure involving the first use of a conduit facility

This was an outstanding deal on a number of different levels. Apart from the innovative HBOS conduit facility, it sees the close of the first rated transaction in the Irish PPP market and the first monoline-guaranteed PPP in Ireland.

The €258 million (US$330m) project - €430 million (US$545m) including the Irish government construction grant of around €180 million (US$228m) - closed last month.

The preferred bidder - DirectRoute consortium - closed the deal with two banks, a Luxembourg-based infrastructure fund, European Investment Bank (EIB) and a monoline.

The successful consortium DirectRoute includes:

- Strabag
- John Sisk
- Lagan Holdings
- Roadbridge

Trevor Sturmy and Anne Andrieux of CIT acted as financial adviser to DirectRoute - the second deal they have advised the consortium on - the first being the Fermoy deal.

The Strabag-led team is due to start construction in spring 2007 on the 900m-long tunnel that runs under the river Shannon. It is a landmark project for more than its financing structure in that it is Ireland's second under-river tunnel after the Jack Lynch Tunnel in Cork.

The project delivers the NRA's fifth road development as part of the Irish government's overall PPP programme for the improvement of national infrastructure, which is contained in the Irish National Development Plan (NDP), 2000-2006.

The tunnel will link all national routes converging on Limerick from Dublin, Tipperary, Cork, Kerry, Waterford, Ennis and Shannon airport. It is expected to remove 40,000 vehicles per day from Limerick city.

**Financing**

The project involves the first use of an asset-backed commercial paper (ABCP) conduit structure that has been developed by HBOS Treasury Services (HBOSTS) and Bank of Scotland Corporate to fund PPP projects.

The pricing benefit for the project company is generated through the use of low cost ABCP funding via a conduit which has purchased privately placed fixed-rate (construction phase) and Irish CPI-linked (operations phase) notes.

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The financial structure additionally provides flexibility for equity bridging notes allowing the shareholders to defer injection of subordinated shareholder loans until construction completion and standby variation notes, as is typical in traditional bank financing structures. Backstop liquidity lines for the structure are provided by Bank of Scotland Corporate.

The Limerick Tunnel project saw an impressive debut for Meridiam Infrastructure, the fund that has already pulled in committed investments from Crédit Agricole Group which has provided €180 million through Prédica and Crédit Agricole Private Equity and €10 million from engineering group AECOM Technology Corporation.

The deal itself sees EIB provide a €100 million (US$125m) loan and Bank of Scotland arrange a €100 million (US$125m). Bank of Scotland also arranged a €40 million (US$55m) equity bridge and in addition there was an €18 million (US$23m) mezzanine loan provided half by Meridiam and half from Allied Irish Bank (AIB).

The DirectRoute consortium provided 50 per cent of the €40 million equity with Meridiam and AIB each contributing 25 per cent.

MBIA is acting as a wrapper for both the senior facilities. A €3m standby facility is also involved.

The monoline wrap is understood to have been priced at around 20bp over LIBOR, while the senior debt should be priced at around 40bp - giving an all-in price of debt of around 60bp.

The conduit facility is an interesting structure that blends the use of bond financing with traditional banking facilities and is widely credited to Peter Macfarlane at HBOS.

The long maturities and lower funding rates offered by the capital markets have long been attractive to infrastructure investers - but the biggest problems such funding sources enhanced by monolines face are inflexibility during drawdown and the effect of the Spens formula post drawdown in the event of restructuring or refinancing.

Instead of a long-term public market bond, the conduit facility is a private placement that effectively uses the commercial paper markets. Euro commercial paper can be borrowed at (or around) LIBOR - so long as you are a AAA rated entity. Commercial paper funding at Euribor allows a regular drawdown - you do not have go for full drawdown and reinvestment.

That AAA rated entity is created by a conduit company - of which HBOS has a couple in place that it has been using for other assets.

The means in which you achieve an AAA rated company, needless to say, is by bringing in a monoline to wrap the debt - and in this case it was MBIA.

From the SPV's point of view it is able to arrange a private placement out of HBOS, but it can fund itself in the same way that a bank funds itself on a regular drawdown.

The process in brief:

- funding up from the commercial paper
- processing this through a conduit vehicle
- the conduit vehicle is wrapped by a monoline
- money goes into project at (in this case) around 60bp all-in

As HBOS's Peter Macfarlane says: 'This combines the price competitiveness of the bond markets with the flexibility of the bank market. It is competitive with the bond markets, but offers something that bonds do not - which is being of a much more bank-like structure.'

Gershon Cohen, head of infrastructure at Bank of Scotland, said: 'This is a landmark transaction for Bank of Scotland Corporate and HBOSTS with the delivery of our first offering of a conduit financing solution and further enhances our investment in the Irish market.'

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A senior source close to the deal says: 'This is an excellent creation and all credit to Peter Macfarlane for it. It solves a lot of problems like inflexible drawdowns; the issues of refinancing; if you want to increase the facility, you issue more loan notes on the same basis; you can restructure the facility very easily.

'But at the same time it has the benefits of the long-term bond market and it is coming in at a lower cost than the banks.'

KMPG was financial adviser to

**Meridiam - a market entrant**

The European fund - headed up by chief executive Thierry Deau and senior investment directors Julia Prescot, Jens Genkel, Janet Nicolini and Stéphane Graells - plans to build the fund up to €400 million by early 2007.

Meridiam has had an early success in the close of the Limerick deal and is preferred bidder with the Alpine-led Bonaventura consortium on ASFINAG's 30-year, €800 million A5 Ostregion road PPP in Austria.

It is also currently - among other bids - competing on France's A63 motorway in a JV with Vinci and Axa; in the Cintra team for the US$525 million SH161 in Texas; and partnering Barclays Private Equity and NIB Capital on the €1 billion (US$1.2bn) Flemish schools programme in Belgium.

Meridiam is looking to institutional investors - like pension schemes and insurance companies - to bring in the other €210 million that it needs to reach its Q1 2007 target. It is seeking long-term investors to join the fund which, unlike many funds that have a 10-12 year tenor, has a maturity of 25 years.

The fund is targeting transport, public building and accommodation projects around Europe and North America - and of the European investments the majority of those will be in Western Europe.

Prescot says: 'We are looking for both user-paid and availability structures - essentially a balance between the two.'

'That is also reflected in the balance we are looking for in our portfolio with a mix of primary and secondary assets - probably with more primary than secondary,' adds Thierry Deau.

'In terms of instrument, we are flexible and would try to provide what is most flexible for the project at the time. We will do anything below senior debt, from mezzanine all the way to equity.

'The type of arrangements are like Limerick where we can be co-sponsors in the equity box with the industrial partners and be there at the very beginning - if we could. We have a take-and-hold policy, rather than buy-and-sell policy.'

Prescot adds: 'Research with potential investors leads us to think that what they want is a longer-term product. They would prefer not to be restructuring their investment at the end of 10 years .'

**Legal**

Linklaters advised the funders on the multi-source financing which includes combined EIB and HBOS arranged senior debt and an equity bridge arranged by HBOS - each of which were wrapped by MBIA, as well as mezzanine debt.

The law firm is no stranger to the Irish roads market having previously worked with this consortium when advising the lenders on the N8 Rathcormac to Fermoy bypass project in Ireland in 2005.

Linklaters advised each of MBIA, HBOS, the mezzanine lenders, Citicorp trustee - as trustee - and the funders generally (including EIB).

The other legal advisers were Ireland-based and were AL Goodbody for the sponsor and borrowers, while McCann

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Fitzgerald acted for the NRA.

Linklaters managing associate Matthew Job led the HBOS team and says: 'The most interesting bit of the transaction was the financing and it is a first in the market. It is very exciting that we have put together the conduit financing in the way that we have.

'It is particularly exciting that we have shown to the market that the conduit is a versatile project that can be harnessed in the context of PPP project because there were many people who said that it was too difficult.'

Job adds: 'It is great news that we and HBOS have been able to demonstrate the conduit as a versatile funding product that can be used on PPP products in general.

'The conduit is a very interesting structure, it is new to the market and represents what I think is a trend in some parts of the infrastructure finance market in that because there is increased competition on funding rates, the leading finance houses are constantly trying to look for increasingly efficient forms of financing to deliver their own internal rate of returns at the level they are expected to demonstrate.

'The conduit facility is an extremely efficient mechanism for financing.'

**Conclusion**

The Limerick Tunnel project sees the successful close of an innovative financing structure that stands as a pathfinder for a financing model that will surely be seeing the light of day.

It also puts the banks, financial advisers and lawyers who have acted on this transaction in a good position to pick up similar deals in the future.

Limerick provides an excellent case study for the first use of a conduit facility, it sees the close of the first rated transaction in the Irish PFI market and the first monoline-guaranteed PPP in Ireland.

**The project at a glance**

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|---|---|
| Project Name | Limerick Road Tunnel |
| Location | Tunnel linking all national routes converging on Limerick from Dublin, Tipperary, Cork, Kerry, Waterford, Ennis and Shannon Airport |
| Description | Twin tube tunnel at 900m in length |
| Sponsors | The National Road Authority of Ireland (NRA) |
| Operator | Roadbridge |
| EPC Contractor | Direct Route Consortium -<br>Strabag<br>John Sisk<br>Lagan Holdings<br>Roadbridge |
| Total Project Value | €430m (US$545m) |
| Irish government grant | €180 million (US$228m) |
| Total equity | €40m (US$50.7m) |
| Equity Breakdown | Direct Route - 50 per cent<br>Meridiam - 25 per cent<br>AIB - 25 per cent |
| Total senior debt | €240m (US$305m) |
| Senior debt breakdown | HBOS - €140m (US$178m)<br>EIB - €100m (US$127m) |
| Senior debt pricing | Around 40bp |
| Total Mezzanine | €18 million (US$22.8m)<br>Meridiam - €9 million (US$11.4m)<br>AIB - €9 million (US$11.4m) |
| Mezzanine pricing | North of 100bp |

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|---|---|
| Arranger | HBOS |
| Liquidity facility provider | Bank of Scotland |
| Mezz and 3rd party equity providers | Allied Irish Bank<br>Meridiam |
| Loan provider | EIB |
| Monoline | MBIA |
| Wrap pricing | Around 20bp |
| Overall pricing | Around 60bp over LIBOR |
| Legal Adviser to sponsor and borrower | AL Goodbody |
| Legal Adviser to NRA | McCann Fitzgerald |
| Legal adviser to banks | Linklaters |
| Financial adviser to DirectRoute | CIT |
| Financial adviser to NRA | KPMG |
| Loan note trustees | Citicorp |
| Security trustee | Citicorp |
| Date of financial close | 18 August 2006 |

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