Hajj Terminal - a Saudi PPP innovation

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The renovation of Saudi Arabia's Hajj Terminal at Jeddah's King Abdulaziz International Airport to cater primarily for the pilgrims to the Holy City of Mecca has yet again pushed the boundaries for Islamic finance.

The project follows the lead set by last month's Queen Alia airport deal, which showed the way for Sharia-compliant private financing of sensitive infrastructure projects.

The Hajj terminal is named after the annual Muslim pilgrimage which this year brought two million believers to Mecca - around half of whom passed through the terminal on arrival in Saudi Arabia.

The terminal itself won architectural awards on its completion in 1980, but it is now due for upgrade and expansion to deal with the ever-increasing number of pilgrims who make the trip.

Given the object's religious significance, Sharia-compliant financing was a non-negotiable aspect of the deal.

The resulting arrangement is special because this is the first time that a build-transfer-operate deal has been arranged in compliance with Sharia law - which until now has been seen as problematic due to the immediate transfer of the physical asset back to the government agency.

The financing was secured on an 'Ijara' - or leasing - deal, whereby the assets being constructed are sold to the lenders and leased back to the SPV together with a right of use over the asset to generate project cashflows.

In this respect, it differs from the Queen Alia deal which used back-to-back leasing - with the MLA leasing the airport to then lease it on to the operating SPV.

Private finance in the Arab world

The contract and its 20-year concession was awarded by the General Authority for Civil Aviation (GACA) to the Saudi Binladin Group (SBG) through the SPV Hajj and Umrah Terminal Construction and Development Company (HTDC).

This is seen as a breakthrough in the field, as the increased willingness of the Kingdom of Saudi Arabia over the last few years to involve the private sector in core infrastructure assets has been limited by the rulers' reluctance to allow strategic assets - such as the airport terminal - to be held in private hands.

"Although the private sector in Saudi Arabia has been active in other sectors such as petrochemicals since 2000-2001, we are now witnessing their increasing involvement in core infrastructure transactions such as water and railways, and now the first BTO airports deal in Saudi Arabia - particularly in view of the Kingdom's objective to both introduce private sector financing and technical know-how, and utilize the PPP process as a 'spring-board' for addressing its infrastructure requirements," says Patrick Mgbenwelu, MD at Gulf One Investment Bank who advised on the transaction.

For all the enthusiasm for private capital in Saudi Arabia, however, there was never any question of the Hajj terminal in Jeddah being privatised.

'Because of the strategic nature of the asset', says Vishal Joshipura of Gulf One, 'the government would never have privatised it.'

It's not just any old airport terminal; it's being upgraded specifically to deal with Islamic pilgrims and as such its ownership is even more sensitive.

This is why BTO was the only viable PPP route. However, that raised the question of how to keep it Islamic, when the physical asset is transferred before the finances have been recouped, and paid back, by the SPV.

The precedent this deal sets 'provides an Islamic finance product platform from which subsequent infrastructure deals can be done, both in the Kingdom and the wider Middle East region', says Craig Nethercott, the White & Case partner advising on the deal.

Vishal Joshipura of Gulf One feels it will continue to be relevant to the Saudi aviation sector where investment is set to continue - including greenfield airport developments.

Patrick Mgbenwelu sees it as a major breakthrough in the Saudi project finance lending market given that it represents the first ever project financing in the Kingdom where lenders have assumed traffic risk. He adds that 'the unique financing structure will set a precedent for other traffic-volume based Islamic transactions in the infrastructure sector.'

Financing

The project, valued at US$315 million, was financed through a limited recourse combination of senior debt and equity.

This included senior debt of US$204 million with a tenor of 12.75 years provided by three MLAs working in a club:

- Bank Aljazira (agent and account bank)
- Credit Suisse
- Islamic Development Bank

Bank Aljazira and the Islamic Development Bank have their own Sharia boards, which approved the deal under Islamic law.

The MLAs were advised by White & Case, in association with the law office of Mohammed Al-Sheikh in Saudi Arabia.

The remainder of the total was financed as follows:

- Subordinated shareholder loan - US$37.3 million
- Shareholder equity - US$13.3 million
- Pre-completion revenues - US$60.4 million

The financial adviser to the sponsor was Bahrain-based Gulf One Investment Bank, with legal advice provided by UK-based Trowers & Hamlins and its Saudi-based partner Hassan Al-Mahassni.

White & Case provided legal advice to the banks. This US-based law firm was previously involved in the revolutionary Islamic finance deal for the Saudi telecoms operator Mobily.

Under that deal, airtime minutes were the asset transferred to the financers, with the operator then acting as the agent able to sell the minutes at a profit.

KPMG Al Fozan & Al Sadhan acted as HTDC's external auditor, while Deloitte & Touche Bakr Abulkhair & Co (Dammam office) undertook the review and independent assessment on the financial model. London-based SH&E acted as technical and traffic adviser to HTDC.

Conclusion

This deal pushes yet further the boundaries of what can be financed under Islamic law.

The opening up of the BTO frontier will surely have implications beyond Jeddah's international airport as strategic assets can now be built and operated under PPP arrangements without governmental agencies having to cede ownership of them.

With Saudi Arabia, and its Arab neighbours, becoming increasingly comfortable with the concept of project financing their infrastructure, this breakthrough provides grounds for optimism on all sides that such future deals will not be held back by Islam's ban on usury or the necessity in some cases to keep key assets in public hands.

The project at a glance

Project Name	King Abdulaziz International Airport Hajj Terminal
Location	Jeddah, Saudi Arabia
Description	Build, maintain and operate the Hajj Terminal Project in King Abdulaziz International Airport, Jeddah, Saudi Arabia
Sponsors	Hajj and Umrah Terminals Construction and Development Company (HTDC), SPV led by Saudi Binladin Group (SBG)
Project Duration (Including construction)	20 years
Total Project Value	US$315 million
Total equity	US$111.1 million
Equity Breakdown	Subordinated shareholder loan - US$37.3 million Shareholder equity - US$13.3 million Pre-completion revenues - US$60.5 million
Total senior debt	US$204 million
Senior debt breakdown	Club agreement between 3 MLAs
Debt:equity ratio	65:35
Mandated lead arrangers	Bank Aljazira Credit Suisse Islamic development bank
Legal Adviser to sponsor	Trowers & Hamlins Law Office of Hassan Mahassni
Financial Adviser to sponsor	Gulf One Investment Bank
External Auditor to sponsor	KPMG Al Fozan & Al Sadhan
Legal adviser to banks	White & Case The Law Office of Mohammed Al-Sheikh
Financial Model Auditor	Deloitte & Touche Bakr Abulkhair & Co.
Technical & Traffic Adviser to sponsor	SH&E (London)
Date of financial close	11 December 2007