# PPP stakes – buyer beware…

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The touch paper has this week been lit on a little-discussed financing wheeze that involves the sale of "economic interest stakes" on under-construction PPP projects – creating a bomb that (in worst case scenarios) will blow up in investors' faces.

The project that has alerted *IJGlobal* to this issue is Edinburgh's £185 million Royal Hospital for Sick Children that was scheduled to start operations on Tuesday (9 July).

It has hit a massive stumbling block with the ventilation system failing to meet standards, and sources warn that opening could be delayed by as much as four months… having already been severely delayed.

The Scottish Government last night (4 July) issued a statement saying: "This decision was taken following final safety checks which revealed that the ventilation system within the critical care department in the new hospital requires further work to meet national standards."

A disaster in and of itself, but that's a long way from being the end of this tawdry tale.

### Economic interest

The Sick Kids Hospital is a non-profit distributing (NPD) PPP that reached financial close in February 2015 with IHS Lothian Limited as the SPV with Brookfield Multiplex, Macquarie Capital and Bouygues.

The EIB took half the £150 million senior debt package (as it is wont to do) alongside two equal lenders – M&G Investment Management and SMBC – pricing at Libor +150bp. The same debt division was deployed on the £20 million mezz tranche. Both loans have a tenor of 23 years.

There was also a sponsor loan – provided by Macquarie – of £15 million which was clearly an equity bridge loan. Our database does not have a maturity on that loan, but one can assume it was to be retired by equity prior to, or at, completion.

Ah well now, that's not quite what happened and brings us nicely to the nub of this entire piece.

Perusal of Companies House will tell you that Mark Dooley of Macquarie fame – now global head of its Green Investment Group – was appointed director of IHS Lothian Limited in late December 2014, a couple of months before financial close.

A little more than a year ago (29 May 2018), Richard Osborne – senior VP at Macquaire – makes his appearance as a director in Companies House, and there's little to remark on that. He did, after all, work on the project in the first place.

All progresses pretty much as normal until almost exactly one year ago (6 July 2018) when John Gordon – managing director of PPP asset management at Dalmore Capital – appears on the scene.

According to sources, this is when the economic interest stake was evidently sold by Macquarie to Dalmore.

In essence, Dalmore has acquired all – or a percentage… though given the size it's more likely to be all – of the equity from Macquarie… but the Aussie giant remains the titular owner as far as the public sector is concerned.

Dalmore is clearly at the table, but it would be interesting to know how much understanding NHS Lothian and the Scottish Government has of this.

Now that's a rather important point of order as the equity owner is not supposed to sell out for an agreed period – usually up to three years – post construction.

All a bit under the radar, but it really shouldn't matter… just so long as everything goes to plan.

### Only a problem when the wheels fall off…

 

Let's take it back to where we started. I think it's fair to say that the wheels have fallen off a wee bit on this project.

It will miss the operational start date by a country mile and – let's be human about this – children were being readied to relocate from the Sick Kids hospital in Sciennes, to world-class facilities in Little France, on the Edinburgh Royal Infirmary campus.

Scottish politicians who have long despised the PPP model no matter how much they sanitise it to their taste with the NPD model, will view this in the same light as, say, a school wall falling down. This happened in early 2016 and resulted in the temporary closure of 17 schools delivered under the PFI programme.

In the case of Edinburgh's Sick Kids, one cannot help but feel a tad concerned for Dalmore as it is clearly the holder of the equity… but has no say on how they resolve this issue, sitting on the side lines and hoping for the best.

Doubtless, Macquarie will keep them well informed… but that's £15 million (likely a good deal more than that as it will not have changed hands at book value) up in the air for the foreseeable future and a big question mark hanging over the project.

PPP haters – and Scotland has more than its fair share of these – have another piece of ammunition in their war against private sector involvement in the financing, delivery and operation of infrastructure.

In a world where PPP contracts are increasingly being challenged by the public sector and put under onerous pressure to deliver – in many cases – above and beyond what they signed up to, this is not going to pass without notice.

It also rather leaves one wondering how many PPP projects under construction around the UK and beyond are impacted by this sale of economic interest stakes leaving equity investors – many of whom will be blithely unaware that they don't have "full ownership" of the asset – at severe risk should things "go wrong".

Of course, the SPV's primary priority comes around in September when it will have to service its first debt repayment…