M25 road refinancing, UK

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London's orbital M25 motorway refinancing was the largest infrastructure refi seen in the UK since the Intercity Express deal of 2015.

The transaction may be somewhat of a rarity but it was very necessary. There was much room for improvement on the terms of the original financing, which featured cash sweeps and debt pricing which reflected the drying up of credit in the middle of the financial crisis.

The primary financing reached financial close in May 2009, less than a year after the collapse of Lehman Brothers, with £698.58 million ($896 million) of senior debt provided by a club of 16 commercial banks, in addition to around £390 million of European Investment Bank (EIB) debt.

The project entailed the widening of 63 miles (102km) of the M25 – converting the remaining three-lane sections to four – and was pushed through by a government keen to show that despite the banking chaos, the UK was still proceeding with (and securing credit for) its large infrastructure projects.

The pricing margin on the commercial term loan was:

- 250bp over Libor – years 1-7
- 300bp over Libor – years 8-10
- 350bp over Libor – years 11-27

Debt was due to mature in 2036, but there was a cash sweep of 50% from years seven to 19, and 100% from then onwards.

These cash sweeps were clearly an incentive to refinance, but huge swap breakage costs meant that replacing the existing debt package was challenging.

Private or public

At first the sponsors considered replacing existing debt through a private placement.

Ultimately it was determined that better pricing could be achieved (possibly as low as 90bp over Libor, although more likely around 100bp) on public bond markets, one source explained.

According to the source, this thinking proved somewhat mistaken. During negotiations prices crept upwards on public markets, and the borrower might have actually been able to get cheaper debt than the 115bp finally agreed if they had pursued a private placement.

The public bond financing did put the sponsors in a better negotiating position, however, enabling them to present investors with a take-it-or-leave it proposition, the source added.

The £889 million, A+ rated bond priced on 24 July (2018). Investors consisted of a group of UK pension funds and institutional investors, with the majority of the issue going to Legal & General Investment Management.

The new notes mature on 31 March 2039, and the refinancing left £383.3 million of outstanding EIB debt in place, dispelling market concerns that the EIB wanted to get out of the deal because of Brexit.

It was always considered preferable to keep the EIB debt in place because its pricing was low and break costs were significant, said one source. And the EIB was happy to do this as long as the risk allocation remained largely unchanged.

Sponsors have had to pay for their cut in margin. The difference between the £889 million bond and the original senior debt (£698.58 million) reveals the magnitude of swap breakage costs.

Interest-rate swaps were broken and inflation swaps were novated to three banks that were originally on the swaps, but had since partly sold down, and who also acted as lead managers on the bond issue:

- Barclays
- HSBC
- Lloyds

The issue was 1.7-1.8x oversubscribed the first time investors bid, and then they bid for a second time at a lower margin.

Shareholders

The shareholder structure is:

- 50% – Dalmore Capital, Equitix and GCM Grosvenor, through two Edge vehicles
- 15% – Balfour Beatty
- 12.5% – Dalmore Capital
- 12.5% – Equitix
- 10% – DIF (9%) and Egis Investment Partners (1%)

This reflects Balfour Beatty's recent equity sales to Equitix and Dalmore Capital.

Balfour Beatty sold a 12.5% stake in the concession company to Dalmore Capital-managed funds for £103 million in December 2017.

Not long after that, the construction company agreed to sell a further 7.5% of the M25 concession for £62 million to Dalmore Capital.

However Equitix-managed funds had the option to acquire this stake instead of Dalmore for an identical price, which they exercised in February (2018), along with an additional £42 million purchase of 5% of the M25 Connect Plus concessionaire.

The original widening project saw Skanska and Balfour Beatty add capacity to the M25 between Junction 16 (M40) and Junction 23 (A1 at South Mimms) and Junction 27 (M11 at Bell Common) and Junction 30 (A13 at Thurrock). It was delivered in phases from 2009-12.

Advisers on the refinancing were:

- HSBC – sponsors’ financial adviser
- Ashurst – sponsors’ legal counsel
- Ernst & Young – Highways England's financial adviser
- DLA Piper – Highways England's legal counsel