EIB… something for the weekend?

Angus Leslie Melville

05/10/2018

Back in the PPP pipeline days, you could set timing on the project finance of any old piece of European infrastructure by the tired mantra of lenders intoning: “And… yes… you can count on the EIB taking half the debt.”

In those days, the EIB took an enthusiastic approach to its mandate of adding value to deals where it was most needed, “crowding in” commercial lenders where they were otherwise (presumably) too timid to play.

Well, they got it right this time with its loans to two crippled Carillion deals and right about now it’s waiting to see just how dramatic the haircut is going to be.

The two projects in the spotlight are:

- Royal Liverpool University Hospital – PPP contract terminated last month after the Carillion collapse
- Midland Metropolitan Hospital – another Carillion casualty with the government agreeing to fund remaining construction work in August, the banks having pulled out two months earlier

The EIB took a half share of the debt on both projects. On Royal Liverpool (FC Dec 2013) it lent £90.4 million which was matched by LGIM; while on Midland Metropolitan (FC Dec 2015) it was in for £108 million alongside Credit Agricole, DZ Bank, KfW IPEX and SMBC.

That’s the best part of £200 million lent to a couple of seriously messed-up projects.

Needless to say, the EIB is pari passu to the commercial lenders and they’re all in for an equally-bad haircut. Sources close to the deal warn that haircut’s gonna be nasty – especially on Midland Met which closed later and hence is far less advanced in its construction.

Sources close to the deal hint that the lenders – EIB, CA CIB, DZ, KfW IPEX and SMBC – are about to be “massacred” on Midland Met, with many suggesting they will be lucky to see 50p in the pound. Meanwhile, on Royal Liverpool sources say 90p in the pound sounds is more likely.

While on the subject of risk, it warrants mention that the Pensions Infrastructure Platform in November (2017) acquired 30-50% equity stakes in 10 UK PPP assets from Aberdeen Standard Investments for £400 million.

Nestled in that group is the ticking time bomb that is Royal Liverpool, shrouded in clouds of asbestos as cracks criss-cross the walls… that are encased in highly-flammable cladding. What could go wrong?

Aberdeen must still be high-fiving itself having punted on 30-50% in that turkey to PIP.

EIB – they’re a funny bunch…

It has always been the way that the EIB has carves a niche – usually 50% – across the European infra debt scene… which is curious given that that their bonuses are not materially impacted by the amount of cash they shovel out the door.

Taking a quick look at the IJ database, it warms the heart to see any number of difficult projects helped to financial close. Take, for example (chosen entirely randomly), those in the wastelands of Schleswig-Holstein, the ruination of Milan, the mean streets of Glasgow (actually that's fair), the hell-hole that is Sweden, and decidedly-dodgy Northern France.

For all that lenders grudge EIB involvement, their loans are gladly received by European governments that see the money they ploughed into the multilateral returned in kind; while on a local level, the procurer and SPV welcome significant cost savings.

On the other side of the table, the EIB team toast its success at hitting a massive target from a miniscule distance, perking up at the memory of good old days like a rheumy gundog cocking an ear at the distant report of a shotgun.

As for the commercial lenders who did the lion's share of the work, they slouch off, hands firmly thrust in pockets, muttering darkly about how they "was robbed".

You don't hear that so often these days.

Brave new world for timid lenders

In recent times, there has been a seismic shift for the EIB – which turns 60 this year with no sign of retirement in the offing (happy birthday, by the way) – and it is not seen quite so often.

Around three years ago, the EIB hired in a bunch of experienced bankers on four-year contracts (they never give permanent contracts, but will renew if your face fits) and this may be one of the key reasons that it no longer dominates lending activity across European infrastructure… not just PPP, but across the vista. They brought with them a banker's perspective, rather than a mandarin's motivation.

But a lot of it comes down to the bottom line. The differential in pricing between commercial debt and EIB loans has shrunk over last couple of years to the point where there's only 5-10bp (sometimes as much as 20bp) of clear air between the two.

Well, that's still a saving and there are few financial advisers on the street who will not see the advantage of shaving a few bips off the cost of a deal… so long as there aren't too many strings attached.

And that leads on nicely to the downside of working with the EIB – its "structural requirements remain as tough as ever" says one source closely linked to the multilateral, adding that this is a key incentive for sponsors opting not to select them.

"Once the EIB is selected," says another leading source from the infra finance community, "it remains constantly tough on covenants, additional conditions and technical due diligence. The EIB is maintaining its 2012 standards, not changing with the rest of the world."

Unlike commercial lenders – who, by implication, stand accused of the opposite – the EIB has not shifted its requirements in order to be selected more often.

Hmmm. Curious dilemma. Should the EIB then be lauded for refusing to erode covenants, adhering to strict and sensible banking guidelines… or should we be congratulating commercial lenders for stripping away covenants that make their loans less secure, but everyone gets a bonus?

One leading infra banker suggests that lack of EIB activity may result in downsizing and, with Brexit just around the corner, Brits in Luxembourg had better brush up their CVs. Which brings to mind an anecdote of a British EIB staffer being told by his boss: "Don't worry about Brexit, you still have a job… you just have a career any more."

One curious element that did crop up in discussions this week was the notion that sponsors want to maintain relationships with the EIB so they can rely on it when the economic cycle shifts again.

The most curious element of this thinking is that while the EIB is often accused of behaving like a commercial entity, it is not one… and it knows that. To seek to maintain a relationship with it on this level is baffling – no insult intended.

All you need is to tick a couple of boxes and the EIB are there – with bells on.

Now, sir, how would we like this? A Midland cut, you say. That'll be removal of half your hair with a centre parting.