Thameslink rolling stock project, UK

Sakshi Sharma & Sarah Tame

25/07/2013

Earlier this month saw the financial close of one of the UK's most anticipated transport deals - the Thameslink rolling stock project - confirming above all that long dated bank debt is available for key national infrastructure projects that are well-structured.

The £1.6 billion (US$2.5bn) Thameslink rolling stock project aims to provide better connectivity between north and south London through central London, while creating direct links to Crossrail and Eurostar trains. Stations outside London will benefit from better connectivity to the centre of the city whereas overcrowded tube lines within the city - especially the Northern Line - are expected to get a breather. Major refurbishment work will also take place at key stations like London Bridge.

Despite the lengthy wait, the eventual close of the project - backed by a solid group of 20 international and local banks - is testimony to the fact that long-term debt is available for the worthy. While the project was complex due to the number of parties involved - there were certainly nervous moments during the financial structuring process - the end result does bode well for future big ticket deals in the UK.

The Project

The project was brought to the market back in 2008 and the Cross London Trains consortium led by Siemens was nominated preferred bidder for the mega project in June 2011. Bombardier was the other bidder in the running for the project. The time period between preferred bidder and financial close stretched out to almost two years, owing to the financial crisis and the project's complex contractual structure involving negotiations between four different parties namely; the UK Department for Transport, the project vehicle and owner of the fleet 'XLT', Siemens Financial Services and the lenders.

The project experienced a series of delays between 2011-2012 for a variety of reasons including the authority, sponsors and lenders wrangling over who will own the asset. The government had initially intended to opt for a traditional lease model but due to the financial crisis, government spend was constrained and it needed to source a large amount of debt for the project. As a result the project was created as a lease deal but structured to fit into the PPP model.

In its final form; Thameslink is set up as a public-private partnership between the Department for Transport and the project consortium Cross London Trains (XLT). Siemens Financial Services (SFS) acts via Siemens Project Ventures GmbH as equal shareholder in XLT next to private equity investors 3i and Innisfree in the total £177 million equity.

The total 25-year concession comprises the design, construction, maintenance and leasing of around 1,140 electric multiple carriages – a net increase of 480 – in 115 units, to be leased to the train operator, providing passengers on the Thameslink line with over 15,000 extra seats.

Each train will carry up to 1,750 passengers. The Thameslink Rolling Stock Programme (TRSP) also includes a contract for the construction and lease of two depots – at Hornsey and Three Bridges – financed through an innovative receivables purchase agreement between SFS and Siemens UK.

The first trains are expected to be delivered two years from now and the final unit is to be completed four and a half years later.

Stuart Rowson, lead partner from Linklaters for the Cross London Train consortium said that along with being a complicated four-way negotiated deal, there were periods when the parties were nervous regarding contract structure and financing. However the parties were preparing for all scenarios, he added. Johannes Schmidt, chief executive of Siemens Financial Services Project Finance Infrastructure Cities & Industry business unit said, "The complexity is not so much about the plan A but rather the plan B; What if the trains come late, what if a bank falls away? The many what ifs made the deal more complex."

In-terms of financing, Rowson said that in the two-year period between preferred bidder and financial close, different financial structures were looked at. But in the end the government and sponsors found traditional bank debt led financing to be the most viable one for the deal.

Siemens agreed the main financing documentation with the core banks on the deal; SMBC, BTMU, Lloyds and KFW. The other banks in the bank club then agreed on these terms with all banks lending on the same terms for a tenor of 25 years to match the length of the concession.

Financing

Thameslink was brought to successful financial close by a combination of commercial lenders, the European Investment Bank and sponsor equity. The project re-opens the debate on whether or not banks are out of the long-term lending game. Now, even though there is enough discussion around pension funds and insurance companies and alternative solutions, the reality is that Thameslink has been financed using the traditional bank club model. Twenty banks were involved in the financing of Thameslink and in terms of liquidity and appetite for the deal those who worked on the deal said it was in "abundance."

Charlie Johnson-Ferguson, who works in PwC's transport practice which acted as financial advisor to the DfT said that there was significant appetite from the banking community for this deal. "As there are less deals in the market the demand for well-structured deals such as Thameslink is strong." Coupled with that is Siemens' strong credit rating and balance sheet, which gave lenders confidence in the sponsor's ability to manage the construction risk.

That is not to say that an institutional or capital markets solution was not explored for the project. Johnson-Ferguson ehcoes Rowson's thoughts above, that when the funding process for Thameslink was designed all financing options were looked at. However a year, to nine months ago, when funding conversations began there was no real precedent for a transaction of this size to be funded in the capital markets. Johnson-Ferguson expects that where the capital markets and institutional investors will play a role is in the smaller transactions that are out there in the market.

The debt/equity ratio on the deal stood at 93:7 and the commercial bank group involved in the financing is:

- Credit Agricole Group
- Bank of China (lead bank)
- Barclays
- BayernLB
- Commonwealth Bank of Australia
- CIC Bank
- Development Bank of Japan
- Deutsche Bank
- DZ Bank
- HSH Nordbank

- ING Bank
- KfW (lead bank)
- Mizuho Financial Group
- LBBW
- Lloyds Banking Group (lead bank)
- Sumitomo Mitsui Banking Corporation (lead bank)
- Bank of Tokyo-Mitsubishi UFJ (lead bank)
- Skandinaviska Enskilda Banken

Banks raised about £1.1 billion in senior debt in addition to £500 million of EIB facilities, comprising of £175 million of project risk debt, sponsor equity and subordinated debt. The swap rate is 3.84 per cent.

The debt pricing will change over the years of the contract and is as follows:

- Years 1-7: 265 bps
- Years 8-9: 315 bps
- Years 10-15: 355 bps
- Years 16+: 370 bps

Pricing of course remains key for project financed deals and according to Johnson-Ferguson the banks were the right answer for this deal. He said, “Pricing is still fine from banks. We can’t say at the moment that institutional debt is better value.”

Johnson-Ferguson added, “There is a big difference between pricing from banks and the capital markets. The cost of carry in the bond market offsets many of the benefits of having a lot of institutional money in the deal and that is something that has to be considered.”

It’s arguable that bank financing also provides the sponsor with greater flexibility, as it offers refinancing opportunities. The Thameslink deal was rated A-, which would support a refinancing after seven years, Johnson-Ferguson said.

Schmidt added, “This project has a long life and there are a number of instances where refinancing is possible and will most likely be done. From the DfT's perspective – we assume - it was important to lock in base rate for the deal and offer flexibility to refinance when the market is favourable.

“This flexibility is hard to offer in a bond financing. Banks offer a more flexible approach to getting projects started. They can better deal with construction risk and they are better equipped to deal with necessary changes during the construction phase of the project. It is hard to debate with an anonymous group of bond holders.”

Siemens did not rule out the possibility of bond financing in the future. Schmidt said, “Once track record is established and construction is complete, then that is the time to consider the bond financing route - at a point where the risk profile is a lot clearer and the trains are operating, then that is an obvious situation when we can think about the capital market.”

Looking to the future Rowson said that Thameslink confirms the fact that for big deals, there is appetite. "It tells people that deals do get done, where there is a good deal of know-how," he said. The ultimate expectation from the industry of course is to have a future project pipeline to work on.

Advisory Roles

Barclays acted as financial adviser to the consortium, Linklaters was legal adviser and JLT was insurance adviser. Quasar Associates was commercial adviser to Siemens.

For the lenders, Clifford Chance was legal adviser, Atkins was technical adviser, Aon was insurance adviser and PKF (now BDO after the merger) was model auditor.

PwC was financial adviser to the UK Department for Transport, Freshfields was legal adviser, Interfleet Technology provided technical advice, while Willis was insurance adviser. Siemens also acted as an adviser on the deal.