HICL Infrastructure Company Limited

Case Study

Queen Alexandra Hospital

September 2010
Queen Alexandra Hospital ("QAH") – a PFI project case study

- Queen Alexandra Hospital ("QAH") PFI project
- Acquired by HICL in June 2010
- Acquired from Carillion Private Finance Limited and Royal Bank Project Investments Limited (RBS)
Queen Alexandra Hospital ("QAH") – Discussion topics

- History
- Facilities
- Structure and contracts
- Revenues and cashflows
- Funding
- Asset management
Project timeline

- OJEC notice: 2001
- Preferred bidder: 2003
- Signed: 2005
- Construction completed: 2009 – 2010
- Fully operational: 2010
- HICL acquires interest: 2010
- Concession ends: 2040

1. Official Journal of the European Union
Client

- Portsmouth Hospitals NHS Trust

- One of the largest acute teaching trusts in UK

- The new QAH brought together 3 hospitals into one site: the pre-existing QAH, St. Mary’s Hospital in Portsmouth and the Royal Hospital Haslar in Gosport

- Employs around 7,800 staff

- Around 1,400 inpatient beds

- Turnover of around £432m p.a.

- Major provider of education and training of under and post-graduate nurses, doctors and pharmacists
Contractual structure

Client
NHS Trust

Financial Guarantor

Secretary of State for Health

Financing agreements

Project agreement

Project Company

Sub-contractors

Construction sub-contract

Carillion Construction Ltd

Carillion Services Ltd

Operating sub-contract

Carillion Services Ltd

Sub-contractors

HICL

Shareholders agreement

74.9%

25.1%

HICL

RBS

Client
NHS Trust

Operating sub-contract

Carillion Services Ltd

Carillion Services Ltd

SPC day to day management

Secrctary of State for Health

Financial Guarantor

Sub-contractors

Construction sub-contract

Carillion Construction Ltd

carillion services ltd
Project agreement

- Concession of 30.5 years post construction*

- Once built, contractual monthly payments for serviced facilities, subject to:
  - RPI annual indexation
  - Performance deductions
  - Un-availability deductions

- Agreement covers items such as:
  - Specification of services to be provided and relevant quality/quantity thresholds
  - Variation mechanics
  - Dispute resolution procedures
  - Termination events and compensation payments
  - Handback criteria

*Construction was completed in June 2010
Construction

- Fixed-price, turnkey contract of £248.7m
  - 55 monthly payments, subject to technical adviser’s sign-off

- Built by Carillion Construction Ltd
  - Parent company guarantee from Carillion plc
  - Cap on liability: 50% of contract sum
  - 12 months of delay liquidated damages
  - 3% retention amount
  - 12 year latent defect period

- Programme
  - Construction started: December 2005
  - Target completion date: over 3 phases between 15 June 2007 to 15 June 2010. Main works completed 15 June 2009.
  - Start of operations: 16 June 2009
Construction in progress
Services

- Estates Services
  - Building maintenance
  - Grounds maintenance

- Catering

- Portering

- Linen & laundry

- Housekeeping

- Help desk

- Car Parking

- Retail

- Coffee bars
Benchmarking and market testing

- Commences in 2014 and every 5 years thereafter
- All services other than Estates Services and Help desk
- Benchmarking initially, client option to market test
- Project Co responsible for managing and co-ordinating Market Testing
Performance monitoring

- Helpdesk logs all problems
- Rectification times
- Service Response times
- Service Failure points
- Unavailability deductions – areas weighted
- Service failures passed to Facilities Management ("FM") contractor
- Unavailability deductions passed down unless Project Co caused
- All payment deductions to date passed down to sub-contractors
Revenue basics

- Single monthly unitary fee from client
- NPV of base case revenue £468m
- Variable monthly payments for meals and utilities – passed down to FM contractor
- Base revenue of £32.9m (real) pa
Indexation

▲ Revenue and Operating Costs
   ▲ Annual indexation
   ▲ RPI index is RPI (all items)
   ▲ Base date of April 2002
   ▲ Contract year commences in December
   ▲ Indexation uses preceding February index
   ▲ Sub-contract indexation is similar

▲ Senior Debt
   ▲ Index-linked guaranteed loan from Secretary of State for Health
   ▲ RPI Index
   ▲ Base date April 2005
   ▲ Indexation semi-annually at Mar and Sep using previous Jan and July indices respectively
Revenue and costs - cashflows

Source: HSFML: Taken from the project’s financial model
Operational Cash cascade

Revenues, less operating costs, less tax

Pre-finance post tax operating cash flows

Cash flow available for reserve deposits

Cash flow available for shareholder debt service

Cash flows available for dividend distributions

Senior debt and working capital financing charges

Deposits to senior debt, and asset renewal reserves

Shareholder debt service

Payment of loanstock & interest to shareholders

Payment of dividends to shareholders
Funding the project

- Index-linked guaranteed loan from Secretary of State for Health
  - £262m guarantee loan
  - £3m stand-by facility
  - £24.3m equity bridge facility

- Shareholders
  - £24.3m loan stock
  - £50k equity

- Debt : shareholder funds – 91.5% : 8.5%
Sources & uses of funds, during construction

- Interim Revenue
- Shareholder equity & loan notes
- Senior Debt
- Pre-funding of Reserve Accounts
- Interest during Construction
- Overhead
- FM Start-Up Costs
- Development Costs
- Construction Costs

Source: HSFML: Taken from the project’s financial model
Key funding terms

▲ Guaranteed Loan (£262m facility)
  ▲ Provided by Secretary of State for Health
  ▲ Monoline wrapped by Financial Security Assurance
  ▲ Index-linked semi annually in line with RPI
  ▲ Base coupon 1.79% pa
  ▲ Tenor
    – 35 years
    – 15 month tail

▲ Loan stock (£24.3m)
  ▲ 12.5% fixed coupon
Non recourse to Equity

- Debt funding is to Project Co

- Secured on:
  - Concession with public sector
  - Payout on termination in certain cases
  - Security over:
    - Project Co assets and contracts
    - Project Co shares

- Hence, funding is non-recourse to shareholders
Debt ratios

Source: HSFML: Taken from the project's financial model
Key Equity risks

- Performance deductions
  - when not passed on to subcontractors

- Major Maintenance forecasts
  - Costs and timing – risk & opportunity

- SPV costs, insurance & overheads

- Accounting standards & tax changes

- Inflation/deposit rates

- Change in Law
Major maintenance

Source: HSFML: Taken from the project's financial model
Insurance

▲ Various policies cover:
   ▲ Project company
   ▲ Authority
   ▲ Sub-contractors (and their sub-contractors)
   ▲ Senior funders
   ▲ Third parties

▲ Risks insured:
   ▲ Contractor’s all risk
   ▲ Third-party liability
   ▲ Delay in start-up
   ▲ Property damage
   ▲ Business interruption

▲ Concession contract includes risk gain/pain-sharing with Authority
   ▲ Five year reviews

▲ Cost increase sharing:
   ▲ First 100% increase: 100% Project Company risk
   ▲ Thereafter: sharing 90% (Authority) / 10% (project company)

▲ Cost decrease sharing:
   ▲ First 25% decrease: 100% Project Company upside
   ▲ 25-50% decrease: 50% sharing
   ▲ 50%+ decrease: 90% Authority upside
Cash deposits

Source: HSFML: Taken from the project’s financial model
Forecast* shareholder cashflows

*Prospective investors should note that no assurance or guarantee can be given that these cashflows will be achieved.

Source: HSFML: Taken from the project's financial model
Rolling investment valuation*

*Assuming a constant discount rate. Prospective investors should note that no assurance or guarantee can be given that this valuation will be achieved.

Source: HSFML: Taken from the project’s financial model
Sensitivity analysis

- FM Costs +/- 10%
- Revenue Deduction 5% throughout
- Insurance +/- 50%
- Lifecycle +/-10%
- Corp. Tax Rates +/- 2%
- Deposit Rates +/- 2%
- Inflation +/- 1%

% Movement in Value

Sensitivities are applied to all remaining years of the concession (i.e., RPI +1% is an increase in the RPI assumption for each remaining year of an additional 1% pa).
Deductions of 5% pa assumes these deductions are not passed down to sub-contractors.
Lifecycle is major maintenance (asset renewal) forecast spend.

Source: HSFML: Taken from the project’s financial model
HICL Asset Management

- Dedicated team of three asset managers and portfolio director
  - Value preservation and enhancement

- HICL takes an active role:
  - Regular board meetings
  - Liaison meetings with clients, project team and key subcontractors
  - SPC management performance
  - Annual budgets and plans developed
  - Quarterly review of performance
  - Monitor sub-contractor credit worthiness
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