Queen Alia Airport

Flying to new heights

The new Amman airport is one of the Middle East's largest private infrastructure projects to-date. It uses an innovative win-win formula that benefits all sides. By **Imane Akalay**, senior investment officer, infrastructure, and **Towfiqua Hoque**, investment officer, advisory services, at the **IFC**.

On November 15 2007, Jordanian officials transferred control of the country's largest airport to new private operators, concluding an intensive 20-month process in which the International Finance Corporation acted as the government's lead adviser and main financier of the project.

At US$700m, the Queen Alia International Airport upgrade is the largest private investment in Jordan's history – one bringing the country a new, state-of-the-art terminal designed by renowned architect Sir Norman Foster. The airport will do "a great deal to propel Jordan's economy into the future", in the words of the then Transport Minister Saoud Nsairat.

It was a landmark transaction, not just for transport in Jordan but for private infrastructure of all kinds in a part of the world that has had much less of it than most other regions. It was also done in record time: financial close was reached just six months after the bid award. Getting to the finish line was not easy, given this region's risk profile. How did it happen?

Background

To begin, consider Jordan itself: a stable country in an unstable region. Home to a sound and growing economy, it is an emerging market with much in its favour today.

It is a WTO member with ambitious, well-thought-out plans for the future and is doing its best to attract the considerable amounts of private capital needed to achieve them. But many private investors are wary of making long-term commitments to projects in some areas of the Middle East, due to the perceived threat of conflict.

This leaves an important role for multilateral development finance institutions, which are in the business of helping emerging market countries reach their goals by attracting productive, socially responsible investment to projects that address major economic and social needs. One of these is Jordan's plan for a comprehensive upgrade of the Queen Alia airport, its capital city's main aviation gateway.

The role of tourism

Built in 1983, Amman's current airport can no longer adequately serve the new economy that this otherwise resource-poor country has since developed, much of it centred on tourism and business travel.

The ancient desert ruins of Petra now rank as a major international destination, having been named one of the "New Seven Wonders of the World" in a July 2007 global internet and telephone poll that drew the participation of more than 100m voters. Jordan has attractive beach resorts at Aqaba as well, plus the wonders of the Dead Sea, biblical and Roman sites, and many other locations that are attracting increasing numbers of foreign travellers. It also draws increasing number of business travellers from the Gulf and other regions.

Tourism-related revenues are on the upswing as a result. Already accounting for 10% of GDP, this industry could bring even greater benefits to the country's 6m people in the future. Some time ago, realising that expanded tourism would require new airport infrastructure, government officials committed themselves to attaining this objective with private sponsorship and financing, thus freeing up government funds for other high-priority social needs such health and education.

However, large-scale airport upgrades are expensive undertakings. They carry high upfront capital costs and have long payback periods. They can also involve currency mismatches, with significant portions of their revenues earned in local currency but bills from international contractors and financiers due in dollars. Commercial

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banks are also not willing to provide long-term financing for some projects with perceived high political risk in the region.

So when the Jordanian authorities began work to implement King Abdullah II's vision for a new airport in 2005, they turned to the IFC. Part of the World Bank Group, the institution fosters sustainable economic growth in developing countries by financing private sector investment, mobilising private capital in local and international financial markets, and providing advisory and risk mitigation services to businesses and governments.

After advising the government on structuring the concession, the IFC put together a US$280m financing package for the winning bidder, a newly formed consortium called Airport International Group that now holds a 25-year rehabilitation, expansion, and operation agreement. It is committed to building a new terminal in 42 months that will more than double the airport's passenger capacity, an important testament to the country's progress.

The business case

The business case for expanding the Queen Alia airport begins with the source of about 60% of its traffic, Royal Jordanian Airlines (RJ). Already one of the few profitable state-owned carriers in the developing world, RJ is likely to increase its revenues thanks to its significant improvements in operating efficiency and its recent entry into the Oneworld Alliance alongside British Airways, American Airlines, and others.

Citi has been appointed to advise the government on the airline's forthcoming privatisation. RJ is also embarking on a new strategy, emphasising the airline's role as a high-frequency, small aircraft carrier that will use Amman as an air transport hub for the Middle East at a time when Jordan is becoming increasingly integrated into the regional and global economies.

The government saw the potential for a profitable airport from the outset. But new private operators were sure to face questions from potential lenders regarding the many risks in the region – and were unlikely to finance the airport's upgrade from purely private sources. Therefore, the government's project planners went to the IFC, an institution with a long record of advising governments on successful private infrastructure projects throughout the developing world, and one that could also offer anchor financing for whichever bidder eventually received the concession.

Concession structure

Building on its earlier experience with airport public-private partnerships in Saudi Arabia and other countries, an IFC advisory team helped the Jordanian government hold a fair and transparent competitive bidding process that attracted five respected industry groups with strong track records.

The bid was to be awarded on the basis of the highest concession fee offered, in percentage terms averaged on a net present value basis over the life of the concession. The World Bank provided significant funding to support the IFC's advisory services under a US Agency for International Development trust fund that it administers, funds used in part to retain law firm of White and Case as legal adviser during the structuring of the concession.

All bidders knew they would have to raise their own financing within six months of the bid award. The centrepiece of the project was to be construction of a new 900,000-square foot terminal based on preliminary designs by Foster + Partners – architect of Hong Kong's highly regarded Chek Lap Kok airport and the spectacular new airport in Beijing that will open in time for the 2008 Summer Olympics, to mention just two. The bidders were also asked to undertake certain predefined improvements to existing airport infrastructure, demolish the existing terminal once the new one is built, and manage all airport services.

When envelopes were opened in Amman in April 2007, the winner had offered a concession fee of more than 50% of revenues on average over the life of the concession. Operating as a special purpose corporation formed solely for this project, Airport International Group brings the financial strength of lead investor Abu Dhabi Investment Company, the industry expertise of Aéroports de Paris Management, a French firm that runs more than 30 airports worldwide, and J&P-AVAX and J&P Overseas as construction experts. The remaining members are two financial investors from the Arab world, Edgo Group of Jordan and Noor Financial Investment Company of Kuwait.

Financing

Upon sounding out the market, the sponsors and their financial adviser, Ernst & Young, realised that they could not get commercial term financing beyond five to 10 years, which was not adequate for an investment of this size. The IFC's offer of long-term financing thus proved critical, as the project budget was front-loaded with high capital expenditure requirements in the first four years but revenues that would take 25 years to flow back in full.

In the end, the IFC provided:

- A US$70m, 17-year senior loan
- A US$40m, 18-year subordinated loan with a 15-year grace period to match the cashflows generated during the concession
- A US$10m standby loan to be disbursed in the event that the cashflows generated by existing operations were insufficient to complete the financing of the new terminal during the construction phase

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In addition, the IFC mobilised US$160m in a 16-year syndication that attracted French banks Calyon and Natixis as well as Europe Arab Bank. It also provided a swap to Airport International Group to minimise the interest rate risk on the transaction. With a greater ability to accept long-term credit risk of clients in emerging markets, the IFC intermediates between derivatives market-makers and clients to provide clients with full market access to risk management products.

The Saudi-based Islamic Development Bank provided US$100m in parallel Islamic financing. Sponsor equity and internal cash generation will cover the remainder of the approximately US$700m in total project costs.

Why did the IFC finance the project at terms and volumes that commercial institutions would not? Based on more that 50 years of experience in emerging markets, it saw many strengths that made it a risk worth taking:

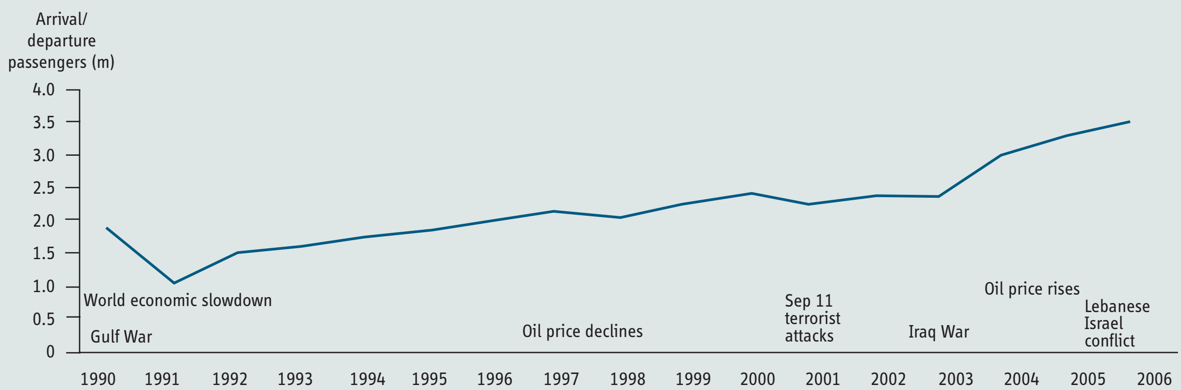
- Market risk – The IFC commissioned independent traffic consultants' reports that confirmed the sponsors' revenue forecasts.
- Foreign exchange risk – While local law requires that the largest portion of the project's revenues be denominated in Jordanian dinars, the IFC negotiated mechanisms to ensure a restoration of earlier economic conditions should the local currency be devalued by more than 10%. Should this happen, the government has agreed to accept a smaller share of revenues, thus protecting the viability of the concession and the lenders' interests.
- Sponsor risk – In upgrading the level of service the airport offers travellers, the experienced French management team seconded from AdPM will open new revenue streams that raise the financial viability of the project, from improved airport shops, parking, offices, and the like. The construction company involved, J&P Group, is among the 30 largest in the world, with significant experience in the Middle East, and specialises in building international airports.
- Political risk – Political risk insurance for acts of terrorism is frequently not available at affordable terms for such projects in the Middle East. In the event of war, terrorism, or other force majeure events that would adversely affect the concessionaire's revenues for more than six months, IFC-negotiated terms give the concession-holders the right to terminate the concession agreement; should this happen, the Jordanian government would repay the sponsors' equity and assume their debt obligations.

Conclusion

By demonstrating the feasibility of limited recourse financing for infrastructure projects in Jordan, the IFC played a significant role in bringing other investors on board. As a result, a new internationally certified terminal will be built that can serve 9m passengers annually. This is more than twice the current level, giving a new face to transportation in the country.

The largest IFC undertaking in Jordan to date, this project demonstrates the multi-faceted package of solutions that the World Bank Group can provide for private sector investments in infrastructure. Looking more broadly across the Middle East, the IFC now looks forward to helping bridge critical gaps of this kind in infrastructure and increasing the quality of service standards in the region by undertaking more projects in the transport sector.

EVOLUTION OF TRAFFIC AT QUEEN ALIA INTERNATIONAL AIRPORT BETWEEN 1990 & 2006



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