



SECURITISATION: BBC

Broadcasting central

THE BRITISH BROADCASTING CORPORATION (BBC), in existence for almost 80 years, experienced a first this year. The group, governed by successive Royal Charters since its inception in 1926, launched its first-ever capital markets transaction in 2003 with a groundbreaking bond issue and securitisation for Broadcasting House, the flagship property and London headquarters of the BBC, which will become the world's largest live broadcast centre.

Corporate profile

The BBC has been in existence for almost 80 years, governed by successive Royal Charters in the UK. The group has businesses along three main strands: public service broadcasting in the UK is funded by the annual UK licence fees and includes delivery of free-to-air

television services, network and local radio and online services. The World Service is its international radio and online service (funded by direct grant from the Foreign & Commonwealth Office). And BBC Commercial Holdings coordinates activity across the BBC's commercial businesses.



Principal terms of the £813m securitisation

Amount £813m

Type Fixed

Margin 52bp

Maturity July 2033

Bookrunners Morgan Stanley

The BBC first began looking at ways to develop its portfolio of over 500 properties back in 1999. Says Stephen Wheatcroft, Group Treasurer of the BBC: "We were really looking forward to the next 10 or 20 years. We wanted to open the BBC up to new technologies, create great workspaces for the staff and provide better public access." After getting endorsement from the government, the group began its first project redeveloping BBC White City at its Wood Lane site in London, which completed in the autumn of 2003.

With its first deal done and dusted, the BBC began looking at what to do about its flagship property, Broadcasting House (BH), in central London. Wheatcroft says: "But Broadcasting House is a landmark and hallmark of the BBC, so we had to take care to do it securely and as cost efficiently as possible."

The project faced almost insurmountable barriers. "First, as a public service entity, the BBC's public service activities are constrained to a £200m borrowing limit," says Wheatcroft. Estimates for the capital cost of the BH redevelopment came in at around £500m with a project period of five years. "Second, the BBC is a chartered organisation, where the charter is renewed every 10 years. But we wanted funding that would be accounted for and paid over the life of the asset, so we were taking a 30-year view on this," says Wheatcroft. This meant any funding would have to straddle three/four charter periods, thus effectively closing the bank market as an option. "The scale of the project was also a challenge for us, as it was obviously very different than that of the White City property," says Wheatcroft.

With all that in mind, the company looked at its objectives. "We had to have certainty first of all. We were looking to finance the whole project and had to be sure that it would reach completion. It was clear that it would have to be off-balance sheet financing, given the BBC's borrowing limit," says Wheatcroft.

Andy Jameson, BBC Broadcasting House Project Director, adds: "In addition, Broadcasting House is an iconic building. This is something that must stay in the BBC portfolio, so we could not just do a straightforward sale-and-leaseback.

"We also wanted stable financing costs and funding that would match with our existing finance streams," he says. "And of course we were looking to raise cash in the short term and pay it back over the long term."

In addition, it was very important that the deal go well, as it was the debut issue from the BBC and would set the tone for future issues. It was key that investors get to know the credit through a successful benchmark transaction.

The BBC, advised by NM Rothschild, requested banks to tender for the deal, and in April 2003 announced that they had mandated Morgan Stanley to put

together the transaction with Ernst & Young appointed as additional advisor. The bank acted as sole bookrunner on the transaction, which was to be a bond issue backed by a commercial mortgage backed securities (CMBS) securitisation for Broadcasting House. The Royal Bank of Scotland acted with Morgan Stanley as joint lead managers on the deal.

Jameson says Morgan Stanley was chosen for the story they presented, as well as their reputation and place in the market: "They are big in sterling and long-dated issues. We liked what they were offering and they worked hard to understand us as an organisation and as first time issuers.

"We are not typical issuers. We have a very strong brand but have never entered the market before, so we had very specific requirements," he says. "They led us through the debut process quite well, and also offered competitive margins." He says both The Royal Bank of Scotland and Morgan Stanley performed very well in getting the deal out there, managing the process, keeping control of price developments and leading the group through their first transaction process.

First-time issuers

After the mandate was awarded, the next step was to discuss the transaction with the market itself and with the rating agencies. Jameson says: "This was an interesting process, as it was difficult to know how they would view us as a corporate entity launching corporate debt, rather than the BBC as a public entity funded by licence fees."

With a number of discussions, it became clear that there was interest in the market for such a deal. In addition, the rating agencies had come up with a rating guidance that meshed with the group's view of where they should stand. But there was still some concern over investor appetite given the desired pricing guidance.

"We had been in discussion with the monolines since the beginning, but kept them on the back burner until we were further along with the deal," says Wheatcroft. "We were coming in as a strong AA- credit, but in the end decided to use the monoline for our own sense of security, and to guarantee investor interest at the prices we wanted. We went to MBIA, who offered us very aggressive prices for the wrap, giving the deal an AAA rating."

The result was a £813m 30-year fixed-rate deal – the largest single property-backed bond ever in Europe. It was almost two times oversubscribed and priced at the tight end of the range, at 52bp over Gilts.

Simultaneous execution

The deal was launched through Morgan Stanley's European Loan Conduit (ELOC). Through it a special purpose vehicle, Juturna, was granted a 150-year leasehold interest in Broadcasting House, and a 30-year sublease was then granted back to the BBC. Lease payments are linked to the retail price index, and the freehold reverts back to the BBC after the 150-year lease period.

Says Albert Ting, a Vice President at Morgan Stanley: "What is special about this transaction is that everything is highly structured and well integrated. In a normal conduit loan a transaction is executed in sequence, a borrower would already have a lease in place and we would then advance a loan based on the mortgage. As the loan pool accumulates we eventually securitise it." But in the case of the BBC it all happened simultaneously – with work on the loan happening alongside the lease being drafted, the inflation swap being sorted and the deal being securitised.



ANDY JAMESON
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"Everything was executed in parallel. The leases were signed, the inflation-linked loan made and the deal was securitised within a 48 hour window. It needed to be a very well-orchestrated process to make sure everything tied together."

Another advantage of Morgan Stanley's ELOC program, according to Ting, is its flexibility. "In the Broadcasting House transaction we were able to tailor the financing to meet the BBC's needs," he says. "As the largest issuer of commercial mortgage backed securities in Europe, we have an efficient and highly creative team thus a large amount of financing can be organised in a very short period of time." This speed and the ability to deliver were key to the BBC, as they were looking to go forward with the deal as soon as possible. The deal was mandated in April and closed just three months later, in July.

In addition to managing the three-pronged nature of the deal, the group also had hedges to contend with as the deal went forward. An index-linked bond would have best matched with the cashflows coming from the lease. In addition the BBC's main source of income – licence fees – are RPI-linked.

But the UK index-linked market is as yet young and could not in all likelihood absorb the transaction. So it was decided that a fixed-rate bond would give the best return and would best support the desired size and tenor of the transaction. The group thus wanted LPI-linked pre-hedges in place before the deal went ahead to ensure the pricing.

"This was tough," says Wheatcroft. "We were already in negotiations for all the other elements but had no concrete idea of when the agreements would be finalised. So it was difficult to know when to press the button and go ahead with the hedges without affecting the deal as it was launched and became generally known of in the markets."

In the end it all worked out, and the deal went ahead at record low pricing for a CMBS launch. Concludes Wheatcroft: "It was an incredible learning experience for us all. We would definitely consider it again, and we would certainly be much more prepared were we to go ahead with a further transaction. We are very pleased with how it turned out."

RUNNER-UP. METRONET



March 2003
£1.03bn multi-tranche financing, including index-linked and fixed-rate tranches
Mature 2032
Fixed-rate: 73bp over Gilts, Index-linked: 80bp over Gilts
Deutsche Bank, The Royal Bank of Scotland, UBS Warburg

Europe's largest-ever PFI/PPP transaction was impressively done. Bringing in a total of £1.03bn, the securitisation element of the Metronet deal was well-received in rather tough market conditions. For the company, it provides long-term funding to renovate and handle long-term maintenance of the London Underground.

The deal structure used elements of both PFI and corporate financing, plus characteristics of a whole-business securitisation. It was wrapped by monolines Ambac and

FSA, and conservative structuring overcame negative market sentiment towards transportation deals. Strong demand allowed spreads to tighten from initial talk. All tranches – including both fixed rate and index-linked pieces – were oversubscribed by as much as three times.

Part of the eagerness of investors was a result of a letter of comfort provided by the UK government saying it would support, although not guarantee, the obligations. It was the first PPP transaction in which two monolines participated, giving

investors extra assurance. As a result, the deal priced much tighter than any recent PFI deals, and the bonds tightened in aftermarket trading on launch.

A key goal of the transaction was to ensure that the London Underground had long-term funding that would be secure and be available when needed. This was clearly met with the deal. The deal was a long time coming, but when it did come it met the needs of the company very well, priced decently and provided a sound investment for the market.