BURROWING FOR SUCCESS

FINANCING THE SILVERTOWN TUNNEL AND INFRASTRUCTURE US-STYLE

GARETH BACON
GLA CONSERVATIVES
GREATER LONDON AUTHORITY

2015

CONTENTS

INTRODUCTION

London needs £1.3 trillion[1] of infrastructure investment in its transport network, housing stock, broadband and educational insti tutions.

Recent figures show that in the last financial year there was already a deficit of £130bn in infrastructure funding in the capital.[2] The upgrade of the Underground is well under way thanks to the efforts of the present Mayor, but the fate of the Silvertown Link, Crossrail extension to Ebbsfleet and the upgrading of broadband connectivity to name but a few, are very much up in the air.

The Mayor of Chicago recently said about his own city: "We have a critical need in this city, which is we have a 21st century economy sitting on a 20th century foundation."[3] The same could be said for London.

Government sources state that 66% of funding for infrastructure will need to come from the private sector[4] - but how? What mechanism can be used to ensure that vital improvements are delivered to maintain the capital's competi tive edge in a global economy?

Looking back to Chicago, they have approached the problem by setting up an infrastructure trust that aims to channel private sector investment into public works that show a clear return on investment for both investors and the city and its residents. This report will pick a case study, and apply the Chicago infrastructure model as a funding mechanism for the project. In an era of tight financial expenditure by government, a true partnership between the public and private spheres is the only solution to improving the economic lot of London.

THE CHICAGO MODEL

The Chicago Infrastructure Trust came into life via executive order of Mayor Rahm Emmanuel and City Council resolution in April 2012.[5] The Trust's basic mission is to help "the people of the City of Chicago, the City government and its sister agencies in providing alternative financing and project delivery options for transformative infrastructure projects."[6] The Trust structures innovative funding strategies to attract capital for a diverse group of investors.

The Board of Directors is made of a mixture of business experts and politicians which includes the former CFOs of the Boeing Company, Sara Lee Foods, a Trade Unionist and City Councilman.[7]

To date, one project has been identi fied and moved through to implementation. The project is a major $12.234million energy retrofit programme for 60 public buildings[8] with a share of the energy savings being split between the private sector and public sector over an 11 year period. The project would see an annual saving of £1,383,918[9]. The burden to deliver on those savings is with the energy companies involved with the project, Schneider, Noresco and Ameresco, not with the city government.

1. www.cityam.com/218761/private-investors-can-plug-london-s-infrastructure-gap-if-we-allow
2. ibid
3. www.shapechicago.com
4. www.cityam.com/218761/private-investors-can-plug-london-s-infrastructure-gap-if-we-allow
5. www.shapechicago.com/about/how-it-works/
6. ibid
7. http://shapechicago.org/about/who-we-are/
8. http://articles.chicagotribune.com/2013-11-12/news/ct-met-chicago-infrastructure-trust-1113-20131113_1_energy-efficiency-retrofit-chicago-city-council
9. http://shapechicago.org/wp-content/uploads/2014/11/FS_PBC_GNM_RetrofitOne_ProgramSummary_201404091.pdf

RETROFIT PROGRAMME SUMMARY

Building Group	Company	Project Cost	Guaranteed Annual Savings	Projected Annual Savings
Police Buildings	Schneider	$3,565,221	$407,922	$428,866
Fire/Shops/ City Hall	Noresco	$2,614,046	$273,818	$273,818
Library/Admin/ Cultural	Ameresco	$6,055,127	$702,178	$775,886

The first phase of this project will cover improvements for:

- 22 libraries
- 15 police stations and buildings used primarily by police
- 11 facilities that provide health care, community centres and facilities for the disabled
- Many unique city properties including City Hall, the Chicago Cultural Centre, 311 Centre, Office of Emergency Management and Communications/911 Centre, and the police and fire training academies.

The Trust has recently negotiated a $32million 4G upgrade of the Chicago transit system which will be paid for by the major wireless operators AT&T, Verizon, T-Mobile and Sprint.[10]

FUNDING THE SILVERTOWN LINK THE CHICAGO WAY

To demonstrate the suitability of using the Chicago Infrastructure Trust model, we have used, for the purposes of this report, the proposed Silvertown Link as a case study. The tunnel is a major piece of infrastructure that has a clear budget without a confirmed funding plan.

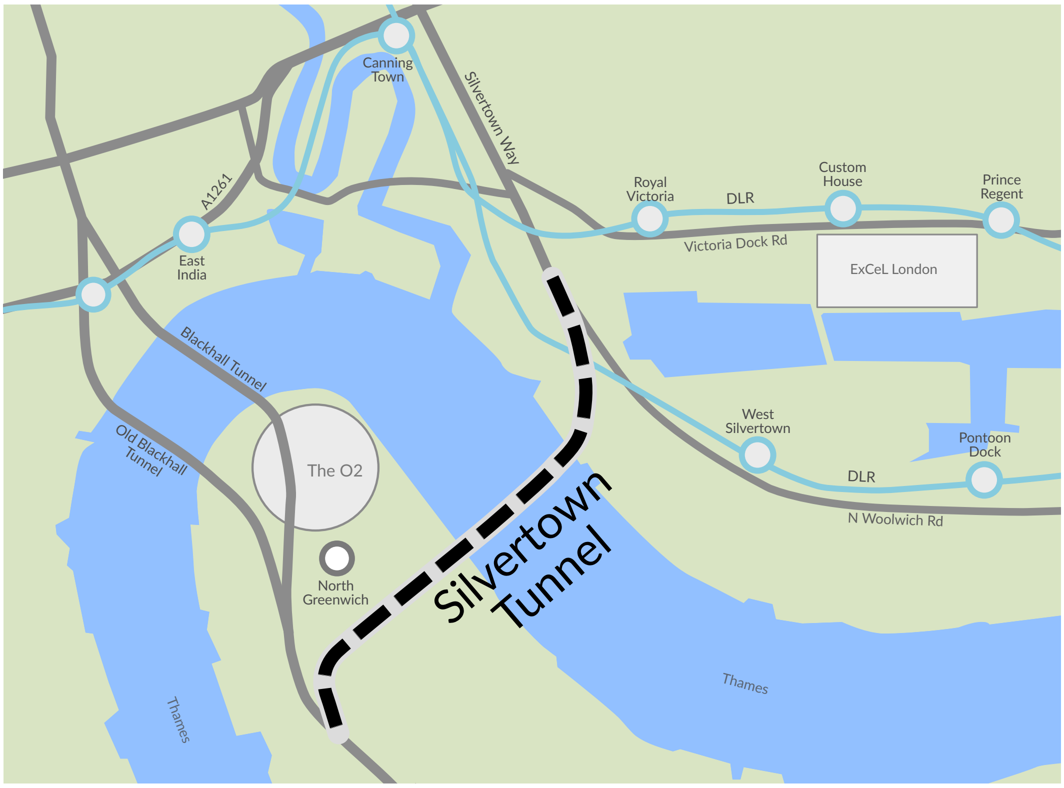
Major developments at the Greenwich Peninsula, Canary Wharf, Stratford and Royal Docks have contributed to an increased demand for travel in this part of South and East London.[11]

There has been a failure to invest in vehicle crossings in the same way that public transit has been invested in, whether it is through Crossrail, the DLR, Tube and Cable Car. The average distance between crossings in east London is 8km, compared to 1-2km in central and west London.[12]

The Silvertown Tunnel will be a twin-bore tunnel providing a road link that would go under the river to link the Tidal Basin roundabout in the Royal Docks to the Blackwell Tunnel South Approach on the Greenwich Peninsula.[13]

The current cost attached to the project is £750m. This report calculates that a joint funding approach between private investors and the public sector is achievable with a return on investment for private financers that would prove to be considerably more lucrative than the average government gilt. The average yield on a ten year government gilt is 2.06%[14] (as of publication of this report). Any finance deal that can match or improve on this return would be of interest to the market.

10. http://shapechicago.org/2015/01/30/trust-brokers-32-5m-4g-deal-on-ctas-behalf/
11. https://consultations.tfl.gov.uk/rivercrossings/silvertown-consultation/user_uploads/why-build-the-silvertown-tunnel_updated.pdf
12. ibid
13. https://consultations.tfl.gov.uk/rivercrossings/silvertown-consultation/user_uploads/what-is-the-silvertown-tunnel_updated.pdf
14. http://www.bloomberg.com/markets/rates-bonds/government-bonds/uk



TfL has previously stated that they will make use of the Dartford Crossing charging system for the Silvertown tunnel[15], and that they will simultaneously begin charging at the Blackwall Tunnel using the same system. The Dartford Tunnel generated £92,548,000 in fare revenues in 2014/15; if the same return was achieved by the Silvertown and Blackwall tunnels, then TfL would generate £185,096,000 in fare revenues per annum. We can make the presumption that Silvertown revenues would be similar as increasing congestion in that area of London ensures that these tunnels will be at least as busy as Dartford. They may, in fact, negatively affect the revenues obtained by the Dartford Tunnel, as these two tunnels are closer to the centre of London and may draw traffic westwards.

The initial private sector investment provided to the LIT for the Silvertown Tunnel would be repaid through fee revenues. If the private investor (or group of investors) received 10 per cent of yearly fee incomes for ten years, they would receive £185,096,000 over that period. If the investor was offered 10 per cent interest on the initial injection of finance, then the investor would have had to have contributed £168,269,091 to the project. This would represent roughly one-fifth of total funding for the project. TfL would instead invest £581,730,909 to the project, and still receive £1.7bn in fee revenues over ten years.

An investment of £168million is modest, considering Legal and General's recent declaration that they want to increase the amount they invest in public infrastructure from £3billion to £15billion over the next ten years.[16] L&G have already invested £500million in student accommodation.[17]

Utilising private sector investments to fund large infrastructure projects is advantageous when the costs of construction are meaningful. The current scheduled open date for the Silvertown Tunnel is 2020. Given a detailed project plan has yet to be submitted to HM Treasury, this is clearly ambitious, and 2022 is perhaps more reasonable. Making use of private sector finance to hasten the completion of the Silvertown Tunnel would benefit TfL and Londoners. By ensuring the project is not delayed to at least 2022, bringing project completion forward by two years would

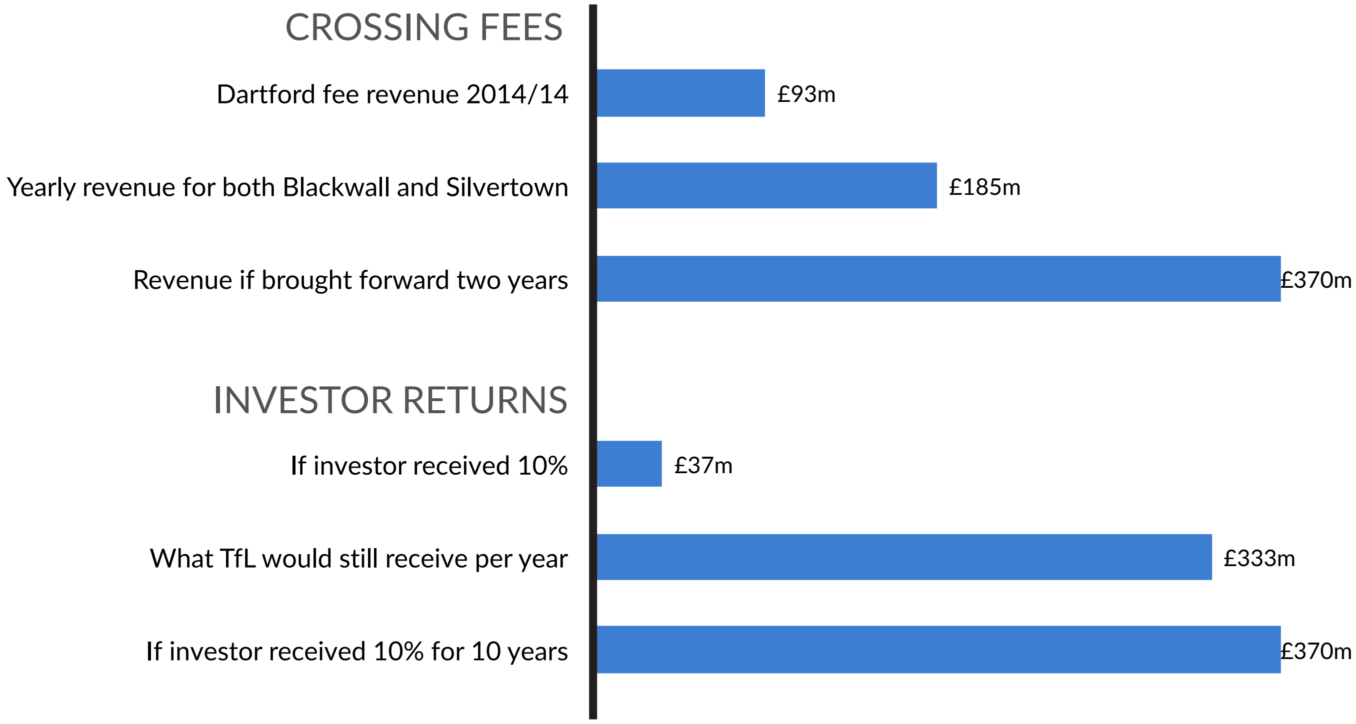
15. Based on GLA Conservative calculations, using data from the Dartford Crossing as a basis for calculations.

16. http://www.telegraph.co.uk/finance/newsbysector/constructionandproperty/10220975/Legal-and-General-in-15bn-infrastructure-pledge-for-UK-but-HS2-will-miss-out.html

17. ibid

reduce the economic costs of congestion by £43.3m; mostly accrued from reduced commuter fuel costs. It would also ensure that TfL started receiving receipts from the two tunnels a lot sooner: it would benefit from £333.2m in additional revenue if brought forward two years.

TfL does currently have a public market borrowing programme to fund its capital expenditure.[18] But with Crossrail 1 yet complete and Crossrail 2 priced at £27bn, the £7bn currently earmarked for bond issue is insufficient to fund these projects and the Silvertown Tunnel. Given HM Treasury will be asked to provide the remaining funding, having a fifth of project costs provided by the private sector would improve the business case. Crossrail 1 was part funded by a Business Rate Supplement by London's businesses: securing private finance through the LIT would also ensure London's businesses do not have to part-fund this project.



HOW WOULD THE TRUST BE CONSTITUTED?

It would be straightforward to set up the proposed London Infrastructure Trust (LIT). Just like the London Enterprise Panel (LEP), the London Infrastructure Trust would legally be a non-incorporated consultative and advisory body established under sections 30 and 34 of the Greater London Authority Act 1999. As a Mayoral appointed body with no separate independent or corporate legal status, the LIT would operate through the GLA, which would act as the LEP's accountable body and financial guarantor. As the legal provisions already exist to establish the London Infrastructure Trust, no amendments to primary legislation would be required. Further, as the LEP manages £294m on behalf of the GLA, there is precedent for the Mayor to act as a guarantor for the large sums of money the LIT would manage.

CONCLUSION/RECOMMENDATIONS

The LIT would offer a sensible solution to funding large infrastructure projects that doesn't make the compromises that some of the less successful PFI deals have done, most spectacularly demonstrated in the health sector. The LIT is not seeking to procure PFI type financial packages.

18. https://tfl.gov.uk/info-for/investors/borrowing-programme

The funding solution would be closer to government bonds. Ownership of the infrastructure and management of the project would remain in the hands of the public sector, with the financers acting as silent partners in most cases. A PFI involves asking a company to build and run an insti tution, such as a hospital, and the risk is shouldered entirely by the public sector. With the financial arrangements put together by the LIT, the risk is spread between the public and private investors.

It should be noted that not all infrastructure projects would be a good fit with this solution. To attract investment, there needs to be a clear way of offering a return that doesn't put an unacceptable burden on the public purse. Other projects that could be financed via this method are the extension of Crossrail to Ebbsfleet, where a share of ticket revenues could be used to pay back investment. It would not work with projects where the long term income generation is unclear.

In conclusion the Mayor should implement the following recommendations:

RECOMMENDATION #1 - Set up the London Infrastructure Trust which would include amongst its membership key business figures as well as public officials as a non-incorporated consultative body established under sections 30 and 34 of the Greater London Authority Act.

RECOMMENDATION #2 - The Silvertown Link should be the first project funded via the LIT.

RECOMMENDATION #3 - The Trust should investigate if other unfunded projects, namely the Crossrail Extension to Ebbsfleet and expansion of broadband in London could be funded via the LIT.

FEEDBACK

Connect with us online and tell us what you thought about this paper.

Twitter: @assembly_tories

Facebook: facebook.com/glaconservatives

Email: assembly.tories@gmail.com

GARETH BACON
LONDON ASSEMBLY
Greater **London** Authority
City Hall, The Queen's Walk
London SE1 2AA