

INFRASTRUCTURE & PROJECT FINANCE

ANNUAL REVIEW 2016



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Telephone: +44 (0)845 345 0456
Fax: +44 (0)121 600 5911
Email: info@financierworldwide.com

www.financierworldwide.com

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INFRASTRUCTURE & PROJECT FINANCE

OCTOBER 2016 • ANNUAL REVIEW

Financier Worldwide canvasses the opinions of leading professionals around the world on the latest trends in infrastructure & project finance.

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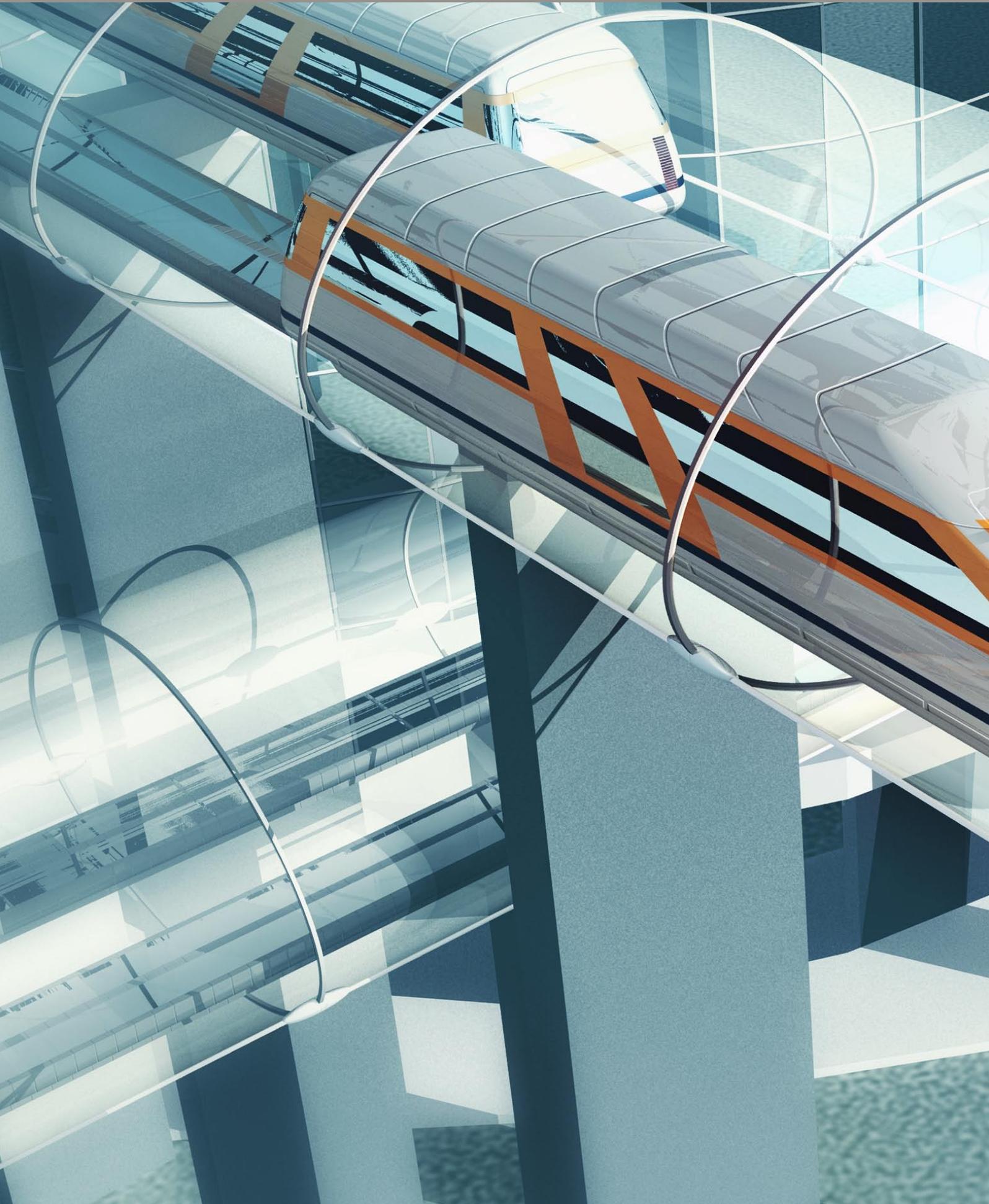


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INTRODUCTION

Infrastructure projects play a vital role in a country's economic development. Developing and delivering infrastructure schemes can improve a country's productivity and bolster economic growth. This can be particularly useful in times such as these, where economic, financial and geopolitical conditions worldwide have created significant uncertainties and instability in the commodities markets, and the oil & gas sector in particular.

Not only do infrastructure schemes enhance the efficiency of production, transportation and communication, they can also provide economic incentives. Public-private partnerships (PPPs) and private finance initiatives (PFIs) are attractive propositions for local and national governments as they look for sources to fund, operate and maintain hugely expensive projects which are, more often than not, a net benefit both locally and nationally.

In Canada and the US, for example, where there are significant infrastructure deficits, the attractiveness of private sector involvement in the infrastructure space cannot be understated. Provided investors have done their homework, including detailed due diligence, significant gains can be made. In developing markets such as India and Brazil, the challenges are often greater; labour, tax, and corruption risks, among others, must be taken into consideration.

Away from the more traditional road and rail networks, an area of considerable PPP and PFI growth in recent years has been the renewable energy space. In Japan, for example, there has been growth in solar power investment. Renewables are an attractive proposition for many investors, although more conventional infrastructure markets such as transportation and telecommunications will remain a focal point of PPP and PFI structures in the foreseeable future.



UNITED STATES

MICHAEL E. PIKEL, JR.
NORTON ROSE FULBRIGHT US LLP



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN THE US OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

PIKEL: There was a time when the US was the global leader in infrastructure. Since that time, despite having the world's largest economy, the US has failed to invest in new infrastructure and failed to adequately maintain and rehabilitate existing infrastructure. This underinvestment has led to decaying public infrastructure and created a tremendous funding gap, all of which, according to a 2013 report by the American Society of Civil Engineers, could cause the US to lose approximately \$3.1 trillion in gross domestic product through 2020. The good news is that the biggest trends to emerge over the last 12 months are a rapidly growing recognition of the need to invest in infrastructure and growing demand for infrastructure investment. Further good news for investors is that the opportunities for investment in the US are increasingly diversified. With a few notable exceptions, nearly all of the greenfield public-private partnership (PPP) projects that closed between 2010 and 2015 have been in the transport sector. Over the last 12 months or so and over the next 12 to 18 months, the opportunities for investment have been and will be diversified. In addition to opportunities in transport, there are opportunities in social infrastructure, energy, water and wastewater, storm water management and telecommunications.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

PIKEL: Budgetary pressures, partisan political bickering, lack of funding and gridlock in Washington, DC have caused state and local governments to take a leadership role in delivering public infrastructure and has forced them to be innovative. As a result, state and local governments across the US are increasingly turning to alternative projects delivery methods from design-build to PPPs to privatisation. Today, 35 states and Washington, DC have adopted some form of P3 enabling legislation. Several jurisdictions have also established P3 offices in order to implement P3 programmes.



Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

PIKIEL: Following the retrenchment of traditional project finance lenders – meaning, European banks – during the global financial crisis, there is no shortage of capital for credit-worthy projects and there is appetite to lend. Over the last few years, we have seen the full return of European commercial banks, Japanese, Canadian and regional US banks entering and participating in the market, the emergence of infrastructure debt funds and the Term Loan B and project bond markets become very important sources of debt capital. In addition, foreign development banks and export credit agencies have been increasingly active in the US. In addition, the tax equity market has also been very strong in recent years. So long as the fundamental principles of project finance are met, the current project finance market in the US is not limited by sector as there are examples over the last 12 months or so of projects being financed in a wide variety of sectors.

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Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

PIKIEL: The identification and allocation of risk are fundamental to the project financing of any project. As a result, due diligence plays a very important role in identifying risks, one of which is regulatory uncertainty. Project sponsors need to identify and understand the risks in a project so that they can decide how to effectively manage the risk – by assuming the risk, allocating it to another party, insuring the risk or restructuring the project. Project lenders have similar goals and concerns. Once all of the risks in a project have been identified, the parties will be able to allocate the risk to the party in the best position to bear or manage it.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

PIKIEL: A deep understanding of commercial theory, public policy and federal, state and local law are often necessary for the delivery of a successful infrastructure project in the US. Infrastructure projects in the US are extremely complex and frequently require governmental entities and investors alike to successfully navigate numerous layers of bureaucracy or governmental oversight, understand a complex contractual regime and avoid legal and regulatory issues. So, in order to create long-term value and generate a return on equity, the knowledge and expertise of all parties involved are critical. An understanding of the local marketplace and political landscape is very helpful as well because political will and commitment are particularly important to the success of an infrastructure project in the US.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

PIKIEL: Mergers and acquisitions involving infrastructure assets are becoming increasingly common as a progressively broader group of investors chase yield in a low-interest rate environment. There are a number of examples where interests in infrastructure projects, primarily demand risk concessions, have changed hands over the last year. In addition, there are a number of M&A transactions involving infrastructure projects currently in the market and the trend is likely to continue, particularly as more and more greenfield projects transition from construction to operations. We are also seeing the definition of infrastructure stretched by investors to include businesses that offer infrastructure-like returns. In addition, there is a good deal of capital looking to invest in infrastructure creating considerable demand for secondary market and privatisation opportunities.

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“The dream of the US as the largest infrastructure market in the world continues.”

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN THE US OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

PIKIEL: We expect to see more state and local governments turning to PPPs to help them deliver much needed improvements to critical public infrastructure across the US. We expect to see the diversification of the sectors in which PPP projects are procured to continue as procurements are launched for a flood diversion project, an automated people mover and a consolidated rent-a-car centre and as decisions are made on whether data centres, street lighting, courthouses, detention centres and projects in other segments of the market will be procured as PPPs. In addition, we see the demand for privatised assets and secondary market M&A transactions to continue to be strong. We also expect to see the definition of infrastructure continue to be expanded. The dream of the US as the largest infrastructure market in the world continues.

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www.nortonrosefulbright.com

Michael E. Pikiel, Jr.

Partner & Head of Infrastructure, Mining and Commodities, US

Norton Rose Fulbright US LLP

+1 (212) 318 3134

michael.pikiel@nortonrosefulbright.com

Mike Pikiel is a New York-based partner at Norton Rose Fulbright and the Head of Infrastructure, Mining and Commodities, United States. He represents sponsors, developers, investors, lenders and underwriters in a wide range of projects and complex finance transactions, including project financings and acquisition financings. Mr Pikiel focuses his practice on the infrastructure, transportation, energy and mining industries.



CANADA

MAXIME TURCOTTE
STIKEMAN ELLIOTT LLP



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN CANADA OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

TURCOTTE: Public-private partnerships (PPPs) continue to be attractive for federal and provincial governments. We have seen both levels of government use private markets to build, operate and finance transportation and social infrastructure. The Canadian market also has a number of developers that seek to monetise their projects post-construction, creating attractive opportunities for investors seeking moderate risks over the long term, such as pensions funds and insurance companies. Renewable energy activity has historically been strong in Ontario, Quebec and British Columbia. Investment opportunities in renewables have been supported by favourable governmental programmes whereby Canadian projects usually involve long term fixed price contracts with government backed public utilities. These favourable terms have recently been the subject of public criticism in certain regions that have seen increases in electricity prices or energy surpluses. Now, with the province of Alberta moving away from coal toward renewable energy, we expect to see a lot of the growth coming from that province.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

TURCOTTE: Various levels of government have expressed a commitment to infrastructure investment and development. There is a large infrastructure deficit across Canada and infrastructure spending continues to be used to stimulate economic growth. The federal government's 2016 budget announced a plan to invest more than \$120bn in infrastructure across the country over the next 10 years. In addition, many provinces have announced plans to invest billions of dollars in infrastructure. For example, Ontario announced that it will be making the largest infrastructure investment in its history with about \$160bn over a period of 12 years while Quebec announced investments of approximately \$88bn over the next 10 years. Federally



and provincially, governments continue to use PPPs as an effective means of transferring many of the risks associated with these projects to the private sector. Also, many projects include post-construction operation and the P3 construct insulates sustained spending on maintenance from the political election cycle.

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Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

TURCOTTE: Like everywhere else, projects that are properly structured and economically viable are the ones most likely to be funded. Canada is often seen as a straightforward jurisdiction for project finance. A majority of the projects are based on low risk revenue streams post-construction. For example, road projects often derive a great majority of their revenues from availability payments and renewable projects benefit from long term contracts that protect them from market fluctuations. Canadian banks are very present and competitive in the project finance area but very few of them will offer long term financing solutions, which forces project sponsors to tap other sources such as life insurance companies, pension funds, foreign banks and the bond market.

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Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED

TURCOTTE: The diligence exercise is key to any successful infrastructure transaction. The focus will be on how the various risks associated with the project have been allocated to third parties who are in the best position to assume and deal with them. In a greenfield project, the appropriate allocation of risks will determine whether or not the project is bankable and will be able to obtain project financing on customary market terms. On the secondary market, the purchaser of an equity stake will want to make sure the moderate returns to be obtained from



TO BE MADE WHEN
NEGOTIATING AND
PREPARING TRANSACTION
DOCUMENTS?

its investment are supported by an appropriate risk allocation. In these cases, the purchase agreement will focus on the investor’s ability to benefit from agreements assigning risks to third parties and, in all other respects, will usually be light on representations and indemnities.

Q IN YOUR EXPERIENCE,
WHAT ELEMENTS ARE
ESSENTIAL TO OPTIMISING
EXISTING PROJECTS,
GENERATING RETURNS
AND CREATING LONG-
TERM VALUE FROM
INFRASTRUCTURE
INVESTMENTS?

TURCOTTE: There are three essential elements in terms of optimising existing projects. The first is tax planning to make sure the most efficient tax structure is used throughout the life of the project. The second element is financing structure, which means adjusting the leverage to be financially optimal. In a number of scenarios, the governmental authority that procured the project will want to share some of the gains obtained from a refinancing since an increase of the debt level will usually entail a greater financial exposure for the government under certain termination events. The third element is optimising performance by third parties involved in the project. There may be cost saving opportunities when agreements with particular sub-contractors allow for termination and there is an alternative lower cost provider.

Q TO WHAT EXTENT ARE
YOU SEEING MERGERS AND
ACQUISITIONS INVOLVING
INFRASTRUCTURE ASSETS?
WHAT PARTICULAR
CHALLENGES TEND TO ARISE
WHEN EXECUTING DEALS IN
THIS SENSITIVE SECTOR?

TURCOTTE: We are seeing many M&A transactions involving infrastructure in Canada. There is an established deal ecosystem that generally functions well. We have many project developers that are willing to take on the higher risks of the development stage, sell projects once they are stabilised post-construction, and reallocate the capital earned toward new development opportunities. At the same time, many institutional and other long term investors are willing to purchase operational projects that give them stable and long-term returns that are difficult to find elsewhere in the market. In the context of generally favourable macroeconomic conditions, we have seen a good flow of deals and expect this trend to continue in the foreseeable future.



“We have seen a good flow of deals and expect this trend to continue in the foreseeable future.”

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN CANADA OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

TURCOTTE: A number of large projects have been announced across the country – for example, the Site C Hydro Project, the Gordie Howe Bridge and the Montreal Light Rail Project. These and other similar projects will continue to attract significant interest from the private sector. Otherwise, two key developments are to be closely monitored. First, the large infrastructure programmes announced by various levels of governments may represent significant opportunities to project sponsors, developers, constructors and lenders. It remains to be seen how and where such funds will be spent and whether the PPP structure will continue to be systematically considered. The other development to be monitored will take place in Alberta where a significant renewable energy plan is expected to be announced this year. Renewable developers are looking at Alberta as the key growth market for Canada.

STIKEMAN ELLIOTT



www.stikeman.com

Maxime Turcotte

Partner
Stikeman Elliott LLP
+1 (514) 397 2421
mturcotte@stikeman.com

Maxime Turcotte is a partner and member of the Corporate Group. His practice focuses on providing corporate advice (often with a cross-border or international component) in the context of public and private M&A, corporate finance transactions, and project mandates related to development, M&A and financing. He is included in The Best Lawyers in Canada 2016; A Guide to the Leading 500 Lawyers in Canada (2016); and the 2014 Rising Stars edition of Lexpert as one of the Leading Lawyers Under 40 in Canada.



MEXICO

MARCO A. SOTOMAYOR MELO
RDA – RODRÍGUEZ DÁVALOS ABOGADOS



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN MEXICO OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

SOTOMAYOR: Adverse economic and financial conditions worldwide continue to cause uncertainties in commodities and oil prices as well as currency instability. There is a crisis in Mexico in terms of governmental leadership which is causing uneasiness throughout the business community. In spite of these factors, which have been affecting investment decisions, there is still some activity in infrastructure projects, specifically in the areas of transportation, energy, oil & gas and healthcare. In general, the Mexican government has reduced its budget for infrastructure projects but it is looking to compensate through a major participation of private capital in such projects, through public-private partnerships. There is still a commitment to incentivise private investment through all Mexico's key sectors, which include transportation and telecommunications, energy, hydraulics, healthcare, urban development and tourism. There certainly is an appetite to invest in infrastructure in these sectors, especially in transportation and energy.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

SOTOMAYOR: In general, the government is still committed to continue with infrastructure investment, but due to adverse economic conditions, and specifically low oil prices, the government has reduced its budget to accomplish the goals set in the National Infrastructure Program 2014-2018 (NIP). Nevertheless, we are seeing in some sectors the use of PPPs and PFIs to renovate and construct new infrastructure and public works. We are seeing even more participation at local government level to incentivise the use of PPPs and PFIs due to a lack of funds being received by the federal government.



Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

SOTOMAYOR: Financing structures still come from commercial and national development banks. It is important to point out that we continue to see foreign commercial banks dominate transactions, since it is crucial to have a good balance on pricing and terms. There is still a considerable appetite for banks to finance any project that has government backing, either through a direct payment commitment by the federal government entity or indirectly through federal participations of state or municipal governments. Also, we have seen more inquiries by banks as to the possibility of financing energy production plants in Mexico, although they are being cautious as the electric market is still in its early stages.

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Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

SOTOMAYOR: Infrastructure deals in Mexico need to have a solid legal foundation. It is extremely important to understand current events in Mexico in order to cope with all regulatory changes that the federal government has proposed to promote investment. When talking about PPPs and PFIs, we do need to take into consideration all regulatory provisions to make sure all necessary approvals, either local or federal, are obtained in a correct and timely manner. Failure to do so can be disastrous for a project.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

SOTOMAYOR: A proper, consistent, clear and fair legal framework in all aspects is essential. It is important to have a comprehensive view of the lifecycle of a project, from idea stage to full operation, and take into account environmental, tax, financial, antitrust and anticorruption frameworks, among many other aspects. In the current socioeconomic climate in Mexico, good project planning should include projects that have social profitability in order to be truly successful. We expect many PPPs projects will be developed going forward. Adequate income distribution in accordance with the risk of each participant should be applied. However, a clear explanation of such projects should be made to the general public where the projects will be developed, so that the local community is able to see the benefits.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

SOTOMAYOR: During 2016 there have been some acquisitions in the energy sector and we will continue to see more acquisitions through the rest of the year, and beyond. Equally, we will continue to see funds come into Mexico to analyse opportunities and buy into big infrastructure projects. One particular challenge that we are seeing today, and which will continue to be a challenge, will be in connection with authorisations by the Mexican Antitrust Commission, as they are time consuming and the Commission is being very strict on its interpretation of all applicable legislation relevant to each transaction.

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“Adequate income distribution in accordance with the risk of each participant should be applied.”

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN MEXICO OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

SOTOMAYOR: In my opinion, foreign investors will continue to come into Mexico looking for opportunities in the infrastructure sector. The lack of funds to reach all the goals under the NIP opens up lots of opportunities for investors, both private and institutional. I still see a trend in connection to the energy sector, which will become stronger as energy reform continues to be implemented.

RDA RODRÍGUEZ DÁVALOS
ABOGADOS



www.rdabogados.com.mx

Marco A. Sotomayor Melo

Partner

RDA – Rodríguez Dávalos Abogados

+52 (81) 8336 5353

msotomayor@rdabogados.com.mx

Marco A. Sotomayor Melo is a partner at RDA. He heads the Monterrey office and the Project Financing Group. He obtained his law degree from the Universidad de Monterrey. His practice is strongly focused on project finance, financial and corporate mechanisms, foreign investment and strategic restructuring. He has solid experience with M&A, joint ventures and secured transactions. Mr Sotomayor led the 'Los Ramones' financing for all its phases, representing the owners in a more than US\$2bn transaction. He also participated in the bidding process for multiple services contracts in the Burgos Basin, leading to the financing of four MSC blocks.



BRAZIL

DANIEL ENGEL
FELSBERG ADVOGADOS



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN BRAZIL OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

ENGEL: Infrastructure investments in Brazil can be divided between greenfield, brownfield and distressed. Over the last few months, as a result of the prevalent Brazilian economic and political circumstances, greenfield investments have been on a downward trend. Brownfield investments have taken place under strategic and specific market opportunities, and not necessarily as a consequence of a well developed secondary market itself. Also, investments in distressed infrastructure assets have increased significantly. Investors have shown a particular interest in greenfield investments, most notably in power generation from renewable sources – mostly wind and solar power – as well as transmission lines and urban mobility projects. In terms of brownfield investments, airports concessions, water and sewage, waste management, healthcare and education have been attracting the most attention. With regard to distressed infrastructure M&A, power distribution, toll roads, water and sewage, and telecommunications have attracted the most interest.

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Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

ENGEL: The current Brazilian government is committed to infrastructure investment and development. A very recent law – signed on 13 September 2016 – created the Investment Partnerships Program (PPI) which intends to increase and strengthen the interaction of the public and private sectors in Brazil, attracting more domestic and overseas investors to the infrastructure sector through the execution of PPP, and similar, agreements. PPPs have been widely used in Brazil, particularly at the state and municipal levels. The federal government expects to increase the number of PPPs by launching several projects under the PPI.

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Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

ENGEL: Historically, long-term funding sources for infrastructure projects have been provided by multilateral and local development banks, especially by the Brazilian Development Bank, BNDES. Infrastructure financing in Brazil is challenging compared with other countries, in light of local market peculiarities. High interest rates inhibit funding from commercial banks. There is not a strong appetite to lend. However, there is a trend in Brazil to reduce the dependence of infrastructure projects on public financing, to bring multilateral banks back to the market and to foster tax incentivised project bonds. Governmental or quasi governmental entities are set to provide around US\$10bn under the PPI to purchase such bonds. Projects are most likely to be funded through project bonds after completion, once the construction risks no longer exist. Scarce funding sources from BNDES are expected to be directed with priority to certain projects, such as water and sewage concessions.

Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

ENGEL: Due diligence is key to managing risks in infrastructure deals in Brazil. There are recurrent material issues regarding labour, tax, real estate, environmental, regulatory, compliance and anticorruption matters. As common practice in the international market, risks are allocated under representations and warranties and in the indemnification clause provided in the transaction documents. However, there are Brazilian peculiarities that should be taken into consideration. Non-recourse project financing is not available. Liability spill-over means certain project company liabilities may affect its economic group and the other way around, especially in environmental, competition, labour and compliance or anticorruption matters. In the allocation of construction risks, the financial and insurance markets offer low coverage for performance bonds, regularly 10 percent of the expected capital expenditures and EPC contractors regularly do not accept a liability cap above 20 percent of the contract price. In terms of permits, regulatory instability may affect environmental licensing and



“We expect that, within the next year, new infrastructure projects will be launched and state-owned companies will be privatised.”

require a thorough review of permits' validity and the rights arising from them. Finally, land rights issues, especially for projects in isolated regions and on the coast, must be considered.

Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

ENGEL: First, it is important to maintain an efficient commercial operation, taking the measures for preventive maintenance in a timely manner, as well as equipment replacement, and so on. Secondly, companies should be aware of refinancing opportunities. Thirdly, good governance policies and efficient contract management should also be implemented. Efforts should be made to guarantee a full overview of the rights, obligations and liabilities provided in the contract, as well as to provide the contract manager with the capacity to enforce the relevant rights at the proper time and form. Finally, efficient claims management should be observed, before both the government – for example, under a PPP agreement or due to rights arising from the relevant permits – and contractors.

Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

ENGEL: We have seen a significant number of distressed M&A deals, related to both distressed project companies or distressed shareholders interested in selling assets. Distressed shareholders are selling project assets to raise funds and service their debt, including in the context of an out-of-court debt restructuring or of a court supervised reorganisation. In the latter case, assets may be sold 'liability free' under a public auction, so that the enterprise value is maximised to the benefit of the creditor. The main challenges are regularly related to poor management of project agreements and of governmental relations, regulatory instability or high indebtedness in view of the project's failure to meet the base case. Liability-free deals require, in addition, attention to certain risks, such as potential conflict between regulatory entities and court concerns; regulatory entities may want to step in or take over a concession, or even block a certain reorganisation structure, and there may be a lack of clarity as to whether courts will in the future recognise that certain non-material contingencies are free of succession, especially in the case of compliance and anticorruption matters.

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN BRAZIL OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

ENGEL: In view of the PPI and the government's need to strengthen private investment in infrastructure, we expect that, within the next year, new infrastructure projects will be launched and state-owned companies will be privatised. According to the preliminary schedule of PPI, it is expected that, during the first half of 2017, bidding procedures will be held to grant concessions in the airport sector and in water and sewage. Further, new rounds will be held for the exploration of oil & gas. In the second half of 2017, the publication of invitations to bid may be expected to grant concessions for private investments in ports, toll roads and railways, as well as for the privatisation of power distribution companies. We would also highlight, as new trends to emerge in the coming months, projects related to public lighting and smart cities, solid waste and distributed solar power microgeneration. Finally, new initiatives to foster cross-border financing may be discussed, such as a dollar component in project revenues to address foreign exchange risks and direct agreements between the government and project lenders.

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www.felsberg.com.br

Daniel Engel

Partner
Felsberg Advogados
+55 11 3141 9107
danielengel@felsberg.com.br

A partner in Felsberg Advogados' Infrastructure Department, Daniel Engel has extensive experience in this area, including administrative contracts, concessions and PPPs, the specific regulation of different sectors (such as energy, mining, transport and finance), project finance, infrastructure contracts, and mergers and acquisitions. He has also assisted his clients on a number of different matters including corporate finance, commercial agreements, anticorruption and compliance, and the third sector. In 2013, Mr Engel worked as a foreign associate at Hengeler Mueller in Frankfurt, Germany.



SPAIN

JOAQUÍN SALES
KING & WOOD MALLESONS



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN SPAIN OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

SALES: The infrastructure sector in Spain has been stagnant over the last 12 months. Very little new money has been invested and a number of existing road and transport projects have been refinanced. The public sector has put most investment initiatives on hold, due both to budget constraints and the negative circumstances affecting the Spanish government, with repeat elections resulting in a much divided congress. At the time of writing, no government has been formally appointed. However, we are seeing renewed interest in the energy sector and investors trying to find reasonably priced portfolios, if not standalone projects. And, of course, going forward, Spanish infrastructure companies will continue to invest heavily abroad, in North America, Latin America, Europe and Australia in particular.

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Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

SALES: Infrastructure has significant social impact and pushes social and economic development. All governments want to improve resource supply since these key elements boost economic growth. Unfortunately, we have no government now, and when we finally do have one, it will have very little or no money to invest. For this reason, PPPs and PFI within the traditional concession model, or the new negotiated procurement processes, will play a key part in the development of the sector. It should be pointed out that the Spanish concession model has proved to be very flexible, and capable of accommodating different procurement strategies.

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Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

SALES: Pension funds from the Asia-Pacific region have shown an active interest in the Spanish market in the last few months. Projects with stable cash flows backed by strong sponsors and in sectors with low regulatory risk are the ones attracting the most interest. Unfortunately, Spain has seen very few of these in recent years. Spanish and European banks will also compete for those assets, with significant liquidity at their disposal. This competition can benefit sponsors, but only if the economics of their projects are sound. Lenders are willing, some are even eager, to lend, but today they are much more cautious. Credit committee requirements have also been increased, as a general rule.

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Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

SALES: Due diligence is important to ensure that project risks are properly allocated and managed. In particular, where sponsors include the contractors that will be involved in the construction and operation of the project, a thorough understanding of project agreements is necessary. After recent experiences in the infrastructure and renewables sector, it would be prudent for investors and lenders to familiarise themselves with regulatory risks. Transaction documents should provide for a robust financing structure while leaving borrowers sufficient room to adapt to changing circumstances. In practice, we have been faced with the paradox that borrowers find it easier to obtain waivers and consents from their lenders under finance documents with more controls over project cash flows. In projects where finance documents are more lax, lenders often refuse to give borrowers any additional leeway.

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“Proper cash flow control is essential, with adequate reserves and financial covenants that accurately track the evolution of the business.”

Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

SALES: Post global financial crisis, a more conservative approach may be wise. High liquidity may tempt sponsors and lenders to repeat the mistakes of the past, with overleveraged projects and loose covenants. Alluring as this may be, it may prove not to be sustainable in the long term. Proper cash flow control is essential, with adequate reserves and financial covenants that accurately track the evolution of the business. In many cases, simply extending the maturity of the debt will not be sufficient to make projects attractive to investors, or even viable.

Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

SALES: M&A transactions may be a good solution for troubled projects, in particular to build portfolios of a substantial size, which can be refinanced in capital markets. However, change of control clauses are common both in project and finance documents so that consent from lenders and, if applicable, procuring authorities, must be sought. In some cases, there is a risk of shifting value from ownership to the contractors building and/or operating the asset, which must be properly accounted for in acquisition documents. And the risk allocation between owners and contractors must be adequately reflected in the financing documents as well.

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN SPAIN OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

SALES: The lack of political stability, together with budgetary restrictions, means that it is unlikely that significant new infrastructure projects will come to the market over the next few months. But it is also true that new investments across a number of sectors are required. Projects with good sponsors and a solid capital structure may still be attractive. There is a clear appetite among domestic and international lenders and providers of alternative financing sources, but only for high-quality assets. In particular, we expect developments in the water and waste management sectors, as well as in connections between sea ports and land transport infrastructure. These can benefit from increased liquidity and innovative financing structures, such as project bonds or direct lending from institutional investors.

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www.kwm.com

Joaquín Sales

Partner
King & Wood Mallesons
+34 91 426 0050
joaquin.sales@eu.kwm.com

Joaquín Sales is partner and head of the banking & finance team of King & Wood Mallesons in Spain. He advises banks, financial institutions and funds, as well as corporations, on all kinds of financing transactions – project finance, acquisition finance, corporate and asset finance – as well as on structured finance transactions and securitisation deals, both domestic and international. Some of his clients are BBVA, Banco Santander, EIB, ICO, La Caixa, Kutxabank, Banco Popular, Barclays, Hispasat, Endesa, Iberdrola and Unión Fenosa. Mr Sales is recommended by the main legal directories including Chambers & Partners, Best Lawyer and Legal 500.



ITALY

ANDREA SCIALPI
EY ITALY



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN ITALY OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

SCIALPI: The Italian economy is rebounding from a period of decline and has recently seen moderate growth. With the onset of recovery there has been renewed interest in infrastructure, with the government providing stimulus for the private sector, along with European funding, to invest into the sector. In particular, we are seeing a renewed focus by the government on the disposal of strategic infrastructure assets. Investors increasingly consider Italy a place to invest their money, and the transport sector appears to be particularly high on the list. The recent attempt to dispose of a stake in Aeroporti di Roma, the upcoming minority disposal of ASPI, the recently completed acquisition of the A4 motorway by Abertis and potential transactions involving other Italian airports are clear examples of this trend.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

SCIALPI: The Italian government is committed to developing infrastructure assets with a focus on ensuring that its spending occurs both at the central and regional levels. However, in line with austerity measures, expenditure has not substantially increased. Government expenditure in 2014 was around €40bn. To provide additional stimulus, the government has committed investment through a number of major plans. Firstly, the Juncker Plan comprises an investment of €315bn across the European region, primarily to boost infrastructure projects. It envisages the €300m acquisition of new rolling stock, €40bn to modernise and upgrade major airports and €40bn for 80 roads and highways projects. Secondly, the 'Unlock Italy' law was primarily enacted in 2014 to stimulate Italy's stagnant economy after its third recession in five years. It is also aimed to cut red tape and boost the construction industry. The law committed €2.1bn for the new terminal at Fiumicino airport, €1.5bn for the construction of a tramway at Florence



airport and €40m for the construction of Aeroporto di Salerno - Costa d'Amalfi airport. Thirdly, the EU launched the 2014-2020 Operational Programme for infrastructure and networks, which targets investments in railways, port infrastructure and intelligent transport systems. It is primarily aimed at developing the multi-modal Single European Transport Area by investing in the Trans-European Transport Network (TEN-T). Along with EU investment and private and public partnership (PPPs), this suggests that there is scope for future growth in the infrastructure sector in Italy. Several projects in the gas and utilities sector are planned or under way, including a new gas pipeline from Azerbaijan to Italy, which seeks to diversify Europe's gas supply, foreseeing the longer-term growth in utilities infrastructure value. However, the focus appears to remain on brownfield projects, with the greenfield component, for the most part, relating to the completion of existing and unfinished larger projects. An aspect, the effects of which still need to be further evaluated, relates to the recently enacted procurement code for use in the public sector.

Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

SCIALPI: Overall, bank loans still remain by far the most relevant funding source for infrastructure projects, along with EU financing provided by the EIB. Certain type of assets, such as hospitals and subways, are typically funded through project finance initiatives. There are also other sources of financing which are timidly starting to emerge, such as project bonds. Project bonds and similar financing structures are expected to play an important role in Italian infrastructure in the medium term, a market that has been reliant on the relationship between banks and public financing. In April 2016, the Italian public sector entity *Concessioni Autostradali Venete* (CAV) issued an €800m project bond to refinance the upgrading of Passante di Mestre, a toll road bypassing Venice. This deal, one of Italy's largest project bond transactions, is the first to benefit from the EIB's project bond credit enhancement (PBCE) scheme.



Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

SCIALPI: Due diligence, from financial to technical to regulatory, continues to have great strategic importance when assessing infrastructure opportunities. Several infrastructure asset classes popular in the Italian M&A arena are subject to a strict regulatory environment. As such, while this provides reassurance over an investment and constitutes a risk mitigation factor, it is key to ensure that typical financial and tax analyses are in tune with the work performed by the technical and regulatory specialists, in order to maximise understanding and benefit from the quality of advice provided to investors. This includes making sure that potential changes in the regulatory environment are well reflected in modelling assumptions and sensitivity analysis. This may lead to benefits also in terms of both financing availability and deal pricing. Similarly, thorough legal due diligence on the contracts underlying the main revenue streams is a fundamental piece of pre-acquisition diligence, along with analyses of the key aspects concerning the approval and status of projects such as capex plans, costs, approval timing, schedules, and so on.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

SCIALPI: It is certainly important to have direct access to the key regulatory bodies and gain a clear understanding of potential threats and hold-ups. While this is only partially addressable through due diligence on the asset, it is becoming ever clearer that further reduction of bureaucracy and regulatory uncertainty is required. Furthermore, it is crucial that the deal team is not only experienced but has knowledge of the asset, the market and the regulator, and that it can easily connect the dots in order to improve the attractiveness of the project holistically.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE

SCIALPI: Recent polls conducted among infrastructure operators have confirmed that the outlook is positive for the country's infrastructure and renewables M&A market, notwithstanding the scepticism around greenfield infrastructure driven by the new procurement code. Recent transactions by Equitix and Meridiam, and the acquisitions of SGI and Grandi Stazioni, reveal a growing appetite for Italian assets. Also, while the interest of international investors is on the up, more and more developers are looking

“Overall, the market appears to be in a transition phase toward operational and financial efficiency, given the huge potential for aggregation.”

WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

to divest their assets, creating a range of opportunities for buyers. Overall, the market appears to be in a transition phase toward operational and financial efficiency, given the huge potential for aggregation.

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN ITALY OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

SCIALPI: Interest in concessions has increased substantially of late. The recent acquisition by Infracapital of an 80 percent stake in a Condotte's PPP portfolio is a clear example of this. District heating and street lighting appear to be major potential drivers of deals, pushed by the recent EU regulation on pollution reduction. More 'exotic' infrastructure funds are also expanding their interest into areas such as smart cities. In addition, an additional wave public sector infrastructure asset disposals is expected in the coming months.



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Andrea Scialpi

Partner
Ernst & Young Transaction Advisory Services
+39 334 695 2475
andrea.scialpi@it.ey.com

Andrea Scialpi joined the transaction support team of Ernst & Young in Rome in April 2004 after an Ibank experience. Since then, he has been involved in over 100 transactions, covering pre-acquisitions, sell-side assistance and JV setup on both domestic and cross-border deals. He spent two years in the EY Transaction Support office of San Francisco, California, where he gained significant middle market PE expertise. Mr Scialpi has worked for clients in numerous sectors, including aerospace and defence, airlines, utilities, fashion & luxury, publishing, real estate and industrial products, and is currently the Italian leader of the Infrastructure and transportation segment.





LUXEMBOURG

ALEXANDRINE ARMSTRONG-CERFONTAINE
KING & WOOD MALLESONS



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN LUXEMBOURG OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

ARMSTRONG-CERFONTAINE: Much is being done to attract investors in new and alternative technologies and the Luxembourg government has made economic diversification a priority. We see activity developing with a big push from the government into 'new' sectors. One such area is sustainable development, with close to 200 eco-enterprises, mainly active in the renewable energy sector, waste management, water treatment and eco-construction, supported by 28 public agencies and six research institutes. Furthermore, the University of Luxembourg and various public research centres have joined together with a number of world-renowned American research institutes for various projects. Data management and storage centres have also been active areas. The government is not only supporting such projects financially, but also promoting them intensively.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

ARMSTRONG-CERFONTAINE: The government has been dedicating a great deal of its budget to investing in infrastructure development in recent years, especially in emerging and innovative fields; it has also focused on high-end information and communication technologies, e-commerce, media, logistics and environment. Thanks to the installation of a fibre-optic network for its internet service and to its generally advanced IT infrastructure, Luxembourg has become an ideal place for installing data management centres and IT businesses. In 2014, the government launched '*Digital Lëtzebuerg*' to develop the digital economy sector and to promote electronic administration. The Luxembourg government has given a big push to the research, development and innovation sector. Since 2000, Luxembourg has multiplied its public



expenses for public research by 10, and in 2013 it reached its objective of spending more than 1 percent of national GDP on public research in addition to the almost 1.4 percent of national GDP invested in research and development by private enterprises and significant state funding. It has not been in vain, as some of the big players have brought their research and development centres to Luxembourg – Goodyear, ArcelorMittal, Avery Dennison, Euro-Composites, Guardian Glass and DuPont de Nemours, to name just a few. An estimated €200m will be spent by the government on the promotion of research, development and innovation between 2016 and 2020. It is now developing the capital's infrastructure by connecting Kirchberg and other developing areas by tramway, allowing the rapid expansion of business centres.

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Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

ARMSTRONG-CERFONTAINE: Project financing has been impacted by Basel III given the costs of such financings on the banks' balance sheet. While syndicated loans remain one of the main sources of financings, alternative finance providers are now seen to provide long term financings through financing platforms, and bonds are used for certain projects – in particular in the US for the financing of power projects or for refinancings generally. In addition, export credit agencies and multilateral agencies are an important source of finance.

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“Given the challenging economic outlook, a proper valuation of the targeted investment with a forecast on potential pitfalls against its growth is essential.”

Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

ARMSTRONG-CERFONTAINE: Due diligence of the regulatory situation is of the highest importance for infrastructure deals, as the investor must have a clear understanding of the legal, regulatory and political landscape in the country in which they are going to invest. Infrastructure investments are illiquid investments and regulatory changes or political instability are two of the most important risk factors, as any change therein could lead to a loss of the investment or a situation where a forced sale would need to take place. These risks, as well as those that may occur between the construction phase of the project and the operation, are addressed during the negotiation process with mitigation techniques and milestones in the execution timetable.

Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

ARMSTRONG-CERFONTAINE: The success of any project depends on the sourcing and costs of the materials – energy, for example – and sales, risk hedging, fiscal optimisation, process efficiency but most importantly on the stability of the regulatory environment and the financial stability of the region of the investment.

Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

ARMSTRONG-CERFONTAINE: Appetite varies depending on the location of the asset and the sector. The current macroeconomic environment and legal and tax uncertainties have impacted on acquisitions in the UK and Europe as a whole, and this has an impact on the level of activity in Luxembourg. Due diligence conducted early – and including the litigation team – is essential. The current regulatory, tax and legal uncertainties in Europe need to be considered thoughtfully to identify potential risks for assets located in the UK. Given the challenging economic outlook, a proper valuation of the targeted investment with a forecast on potential pitfalls against its growth is essential.

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN LUXEMBOURG OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

ARMSTRONG-CERFONTAINE: EU member states are facing large infrastructure investment needs over the coming decade. As a significant part of the existing assets come up for renewal in the established member states, new member states still have scope for raising their infrastructure capital stock. Developing countries are still facing a large infrastructure deficit compared with the Millennium Development Goals, and needs continue to rise with population and economic growth. Moreover, global changes in socioeconomic factors, such as climate change and an ageing population are driving the demand for greater infrastructure investment. As such we expect to see brownfield infrastructure deals come on the market. With regard to the Luxembourg market, the European long-term investment fund (ELTIF) is a pan-European regime for alternative investment funds making long-term investments linked to the activities of the 'real economy', including the development and operation of infrastructure. Such opportunities will further increase the Luxembourg toolbox that is available to initiators.



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Alexandrine Armstrong-Cerfontaine

**Managing Partner
King & Wood Mallesons
+352 27 47 56 3401**

alexandrine.armstrong-cerfontaine@eu.kwm.com

Alexandrine Armstrong-Cerfontaine is the managing partner of King & Wood Mallesons' Luxembourg office. She is listed among the best women in private equity worldwide (Euromoney). Her practice focuses on private equity transactions, banking and finance and M&A, specifically in LBO and private equity transactions, advising private equity sponsors on their investments, corporate finance, funds finance, syndicated financings (including leveraged financing and restructurings) and fund formation.



INDIA

MUNISH SHARMA
DUA ASSOCIATES



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN INDIA OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

SHARMA: Infrastructure investment in India has seen substantial activity over the last 12 months, particularly in roads and bridges, renewable energy such as solar power, ports and healthcare. There have been some improvements in terms of infrastructure creation and service delivery in water supply and sewage treatment, largely due to increased interest from the government. This has been the welcome signal that the infrastructure sector had been looking for, having been at a standstill for more than five years. Investors and developers have also shown considerable interest in the water supply, waste management and education sectors.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

SHARMA: The government is committed to infrastructure development through PPPs, PFIs and other initiatives. The newly passed Goods and Service Tax law comes into effect on 1 April 2017 and is expected to make India's tax regime transparent. The government is keen to develop regional airports under the PPP model, even though PPPs have seen mixed success in India. There are a large number of stalled PPP projects in power and roads, some due to unforeseen events, but mostly due to improper risk allocation, poor dispute resolution and inadequate financing sources largely from commercial banks. Recently, the government modified the PPP model in the case of road projects with a view to attracting investors and developers. One of the key reasons that the road sector has seen some activity is that a new financing model for highways has been introduced called 'Hybrid Annuity', which would replace the classic PPP model. In this model, the private partner takes on the construction and maintenance risk, while the concession grantor, the National Highway Authority of India (NHA), takes the traffic risk. It is expected that going forward, to address the



fiscal deficit position of the government, PPP models will play a more crucial role, given the expected investment requirement of over US\$1 trillion in the next five years.

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Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

SHARMA: In the past, the main funding source for project finance has been government owned financial institutions and Indian commercial banks. Projects with clear land allocated and assured revenues that are backed by guarantee or other mechanism are most likely to be funded. Indian banks are currently very cautious about investing in the infrastructure sector on account of their existing non-performing assets. The government has set up the Indian Infrastructure Finance Company Limited (IIFCL) to provide direct long term lending to commercially viable infrastructure projects by way of direct lending, take-out-finance and credit enhancement guarantees for instruments issued by infrastructure companies. The Reserve Bank of India (RBI), the country's central bank, has recently allowed non-banking financial companies (NBFCs) to provide take out financing to infrastructure projects, an option so far available only with banks. This flexibility will most likely see more NBFC involvement in project financing. Recently, the government also set up a fund of funds – the National Investment & Infrastructure Fund (NIIF) – with a view to providing alternate financing options for stressed assets and for greenfield and brownfield projects.

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Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY

SHARMA: Detailed financial, legal and regulatory due diligence is necessary in any infrastructure deal in order to understand and manage risks and regulatory challenges. In share purchase deals, if the diligence process brings up land or regulatory issues, it would be more prudent to pay the consideration in tranches. Indemnity backed representations are effective in deriving some comfort in case



CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

of breach of representations. Arbitration in an efficient common law inclined jurisdiction which has reciprocity with India, helps in seeking effective and expeditious remedy. Another aspect that needs some consideration is access to secured project financing. It is difficult to accurately determine demand risk, and a take or pay arrangement is a good mitigating factor.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

SHARMA: There is no magic remedy for optimising existing projects or for stalled projects in the Indian context. The most elementary requirement seems to be to make available stable and efficient alternate sources of financing in order to attract increased private sector participation, and to facilitate the refinancing of existing projects. Even the proposed emphasis given by the government to revive the PPP model will require the availability of innovative ways of raising capital and a well balanced concession agreement. The NIIF is a step in that direction. However, its effectiveness will be known only when money starts to be channelled into the NIIF. The government needs to focus on reducing the overall risk scenario for infrastructure projects. Environmental and social risks also need to be evaluated and mitigated to the extent possible, before awarding new projects, or before existing projects are revived. For existing projects that face operational or maintenance difficulties, the government needs to either replace the developer or take over these projects with the consent of the developer so that their overall financial distress can be reduced and their attention can shift to new projects.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

SHARMA: There has been a significant increase in M&A in the infrastructure sector. There have been two types of M&A transactions – one set driven by banks and lenders putting pressure on highly leveraged project companies to sell assets to reduce their debt, and the other driven by developers opting for operating or running projects, instead of greenfield projects, thereby avoiding the usual risks associated with greenfield projects. Those promoters who held onto their assets are more than willing to pass them on to a more able developer or operator. Land acquisition issues and the inability of the project company to access the required clear and unencumbered land is a major issue. During the development stage, promoters usually ignore regulatory compliance, which sometimes has serious consequences.

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“In order to stimulate growth, the government is going to continue encouraging investments in infrastructure and inviting the private sector to participate.”

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN INDIA OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

SHARMA: Overall, the near future should be an exciting time for infrastructure development. In order to stimulate growth, the government is going to continue encouraging investments in infrastructure and inviting the private sector to participate. Several positive steps have been taken to make projects more bankable. Recently, the roads sector has seen innovative risk sharing models from the NHAI. PPPs will continue to be the preferred method of procurement. Budget allocation has also been made by the government toward initial allocation of capital to set up a fund-of-funds that would finance commercially viable greenfield projects and help restructure stalled projects. It is expected that most of the existing projects will see a change in ownership through M&A. Some asset sales, especially in the power sector, have already begun, driven by a need to deleverage existing balance sheets. Many developers are likely to opt for brownfield projects to expand their capacities rather than investing in greenfield projects that carry risks such as land acquisition, or fuel linkage or environmental clearances. Apart from stressed thermal assets, consolidation through M&A in the telecoms and road sectors is also expected.

DUA ASSOCIATES



www.duaassociates.com

Munish Sharma

Partner
Dua Associates
+91 11 2371 4408
munish@duaassociates.com

Munish Sharma is a partner at Dua Associates. His legal practice focuses on mergers and acquisitions, private equity, inbound and outbound investments, public-private partnership concessions, infrastructure projects, project finance, capital markets, corporate finance, cross-border transactions, joint ventures, business restructuring and corporate and commercial transactions. Mr Sharma has been involved in infrastructure projects in energy, oil, gas, power, airports and roads and in other sectors such as insurance, telecommunications, consumer goods, public relations, advertising and business process outsourcing.



JAPAN

IZUMI YAMADA

DELOITTE TOHMATSU FINANCIAL ADVISORY LLC



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN JAPAN OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

YAMADA: The government advocates the expansion of private participation in public services and assets through PPP and PFI schemes in its national master plan, the Japan Revitalisation Strategy 2016. The Cabinet Office (CAO), the supervisory agency of PPP/PFI, set numerical targets for 2013-2022, comprising ¥7 trillion for concessions, ¥5 trillion for public facilities with income-generating facilities, ¥4 trillion for public real estate utilisation projects, and ¥5 trillion for other projects. The government also targeted six airports, six water facilities, six sewerage facilities and one toll road between 2014 and 2016, and three educational facilities and six public housing projects between 2016 and 2018. The targets set by the CAO are more ambitious than the PPP/PFIs projects seen in recent years. A number of private entities have just begun operation of airport concessions including the Sendai Airport, the Kansai International Airport and the Osaka International Airport, as well as the toll road concession in Aichi prefecture. Various companies were keen to seek investment opportunities in these projects, and jointly participated in the bidding processes under a consortia. The bidding processes for airport concessions in Fukuoka, Takamatsu and Shizuoka airports is expected to begin soon, and this process is likely to attract many Japanese companies.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

YAMADA: The government is accelerating PPP/PFI initiatives for infrastructure investment and development. In December 2015, the CAO and the Ministry of Internal Affairs and Communications jointly announced The Guideline for Preferential Consideration of Various PPP/PFI Methods and also introduced Universal Testing, which compels local municipalities with a population of more than 200,000 to consider private capital utilisation when implementing public services. In addition, the CAO announced the PPP/PFI Promotion Action Plan in May 2016, designed to accelerate the formulation of a regional



platform for improving the capacities of PPP/PFI projects with local public authorities. The regional platform, which focuses on government-designated cities, is expected to improve the current situation where information and the know-how of local public authorities and private entities are not sufficiently shared and discussed through dialogue and proposals between them.

Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

YAMADA: In the past, project financing was usually oriented with PFI projects with the stable availability payments, mainly procuring huge finance volumes from lenders like megabanks. However, recent concession projects have tended to be more sponsor-oriented PPP/PFI projects, designing the project structure to meet more sponsors' interests. A further trend is increasing rural infrastructure projects as national targets, and local entities and local financiers seeking bigger roles, rather than participating as minority shareholders as they did previously.

Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

YAMADA: In Japan, infrastructure projects tend to be concession or brownfield types and the historical data and track records of these past projects are accessible. Thus, the common practice during due diligence is to analyse future business plans and cash flows based on this historical data when negotiating and preparing transaction documents, including the bidding price. The controversy in recent concession projects is about the allocation of risk between public and private, especially with the defection risk of the existing facilities during due diligence. In other words, upon transferring the ownership of the facilities from public to private under the concession agreements, if there are any defects identified in the facilities when operated by the public, the private entities believe the expenses should be borne by the public. The main issue here is the uncertainty over how many defects



“There is a huge necessity for asset renewal among public facilities.”

exist, how expenses should be included in the business plan and who will carry the cost. From private entities' perspectives, in addition to carrying out proper technical due diligence, the potential expenses attached to defects identified by technical due diligence should be reflected in the concession price after revising the financial model. A public entity undertaking the bidding process needs to consider how to allocate the defection risk and the extent of information to disclose to meet the concerns of private entities.

Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

YAMADA: Infrastructure in Japan has already matured in some respects, and there are only a few requirements to develop new, large-scale infrastructure assets. However, there is a huge necessity for asset renewal among public facilities. In such circumstances, where upward revenue trends cannot be easily expected, from the perspectives of private entities the key is to reduce project costs, especially in the water sector, to create long-term value and ensure profitability. In addition, private entities need to draw up a master plan for creating income-generating assets, such as real estate developments and shopping facilities, when considering value-up strategies in the airport and road sectors.

Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

YAMADA: M&A in Japan has been on an upward trend since the latter half of 1990s. However, M&A involving domestic infrastructure companies has not been active at all. In the energy sector, deregulation of electric power began in April 2016 upon revision of the Electricity Business Act, but existing power companies have a virtual monopoly on each supply area, resulting in a dearth of M&A activity to date. On the other hand, gas supply is scheduled to be deregulated from 2017 and then there is a possibility of M&A because this market is not monopolised – there will be 200 gas companies compared to 10 power companies. It has been reported that Idemitsu Kosan intends to purchase stocks of Showa Shell Sekiyu next spring, and in this context, realignments and alliances among operators will expand and synergise the energy business across the electricity, gas and oil space.

Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN JAPAN OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

YAMADA: Project finance in the domestic infrastructure market has been driven by solar power generation. However, it is expected that project finance for solar power generation will decrease to reflect lower feed-in tariffs. Regarding PPP/PFI, there appears to be a need for payment projects, mainly for social infrastructure assets. However, these projects are rather small scale, requiring less financial arrangements with project finance. Regarding concession projects, currently local governments prefer amortisation payments to upfront payments with concession fees that require less project finance. However, the Japanese government is considering setting a policy for payment exemption on guarantees of future interests, aiming to pursue early debt liquidation in the public sector. If this policy is introduced, there is a possibility that local governments will shift finance procurement to private rather than public finance, mainly in the water and sewerage sectors, creating huge investment opportunities for private entities.

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Izumi Yamada

Head of Infrastructure & PPP Advisory Group

Deloitte Tohmatsu Financial Advisory LLC

+81 3 6213 3710

izumi.yamada@tohmatsum.co.jp

Izumi Yamada heads the Infrastructure & PPP Advisory Group in Japan. Mr Yamada has extensive experience in various fields, including audit, reorganisation & restructuring services, infrastructure-related advisory services. In infrastructure business, he has considerable experience and knowledge of PPP/PFI through a good record of advisory services both for public and private entities in multiple sectors. He has also written on financial due diligence. Mr Yamada is a Certified Public Accountant in Japan.



ANGOLA

IRINA NEVES FERREIRA
ANGOLA LEGAL CIRCLE



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN ANGOLA OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

FERREIRA: It is a widely accepted fact that recent notable economic growth in Angola was mostly, if not entirely, supported by oil profits. The sharp drop in oil prices thus had a major impact on the country. Budgetary adjustments were required and the state budget for 2015 was amended only three months after its publication. Public investment policies – including in infrastructure – were consequently heavily reduced. The Ministry of Finance publicly stated that certain infrastructure projects would be suspended in order to guarantee the implementation of infrastructure projects deemed a priority. There are, however, a significant number of projects still reported to be ongoing – for example, the construction of a deep water port in Cabinda, the rehabilitation of a 1344 km section of the Benguela railway between the port of Lobito and the DR Congo, and the construction a new international airport in Luanda, together with a highway project connecting Luanda to the new airport.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

FERREIRA: Investment in infrastructure, in a more favourable economy, was a governmental priority due also to the need to rebuild the country in the post-war years. Much has been done in terms of roads and logistics but there is still huge potential for infrastructure development which, unfortunately, is now limited by diminishing oil revenues. Now, despite the steep drop in tax revenues arising from the oil sector, the government is reportedly committed to renewing Angola's infrastructure networks. The state budget still includes, for instance, the construction of an integrated communications and transport network and the Angolan state has recently provided a US\$210m sovereign guarantee to the loan made by banks to fund a biofuel project. A new code governing public contracts was recently enacted, aimed at modernising and simplifying public tender procedures. Not incidentally, over the course of the year many ministries created technical units to support



investment projects, as mandated by the new private investment law approved in August 2015. These units approved several new investment projects including a \$65m project for the construction of a plant for electric energy transportation lines towers.

Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

FERREIRA: Until the recent downturn in oil prices, Angola was one of the four sub-Saharan African countries with the highest deal volume of project finance, according to the World Bank. However, it is worth highlighting that if one disregards extractive deals, Angola would be in ninth position instead. Alongside traditional financing sources, the Angolan government is analysing the feasibility of alternative sources of funding for infrastructure projects – for example, turning to investment funds, capital market and partnerships with private entities. Angola sold its first Eurobond in 2015, raising \$1.5bn in the market. It should also be noted that new statutes introducing a legal framework applicable to collective investment undertakings and venture capital were recently enacted. Regarding the implementation of a capital market system in Angola, the IMF has recently praised the efforts made by the Capital Markets Commission regarding diversification of the economy.

Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN

FERREIRA: The risks of implementing an infrastructure project in Angola must be identified from the outset. The Angolan legal system and administrative organisation are still at an early stage of development. Angola is ranked 181 out of 189 in terms of ease of doing business, where the top countries have a regulatory environment more conducive to starting and operating a local firm. Appropriate planning and due diligence is required. The negotiation and preparation of transaction documents should also take into consideration potential time slippages and related consequences – namely, consequential slippages in the



NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

project's budget. Any potential investor must carefully assess the risks associated with environment construction licensing procedures, ownership of land, local content requirements, foreign-exchange constraints, customs, the private investment system and the public-private partnership framework.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

FERREIRA: It may be deemed as a common ground for all infrastructure projects that in order to optimise existing projects, generate returns and create long-term value, it is essential to enhance the economic or social benefit arising from the infrastructure maximising the use of the assets and the benefits for users. Secondly, it is important to decrease the cost of infrastructure by avoiding the potential impact of external factors, and to mitigate operation and maintenance costs. Finally, it is essential that efforts are made to improve the lifetime value of the infrastructure by boosting the durability of the assets and reinvesting.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

FERREIRA: Although it cannot be considered a typical M&A operation, Sonangol, the country's larger corporation, is currently undergoing a profound restructuring process. The restructuring in Sonangol's group – whose activities include oil & gas exploration, airline services, distribution and logistics, medical clinics and financial services – may create M&A opportunities since some of the group's subsidiaries can be merged in order to cut costs. Angola Telecom, the state own telecom company, is currently facing a similar restructuring process and the sale of some assets is under review.

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Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN ANGOLA OVER THE COMING MONTHS? DO YOU EXPECT

FERREIRA: The current economic crisis poses a threat to, and has effectively curbed, the Angolan government's efforts regarding infrastructure rehabilitation. However, notwithstanding the significant efforts to recover the country's infrastructure networks, the deficits are still manifest and the demographic pressure has been increasing. Also, the current economic situation has rekindled the debate on oil

“It is essential to enhance the economic or social benefit arising from the infrastructure maximising the use of the assets and the benefits for users.”

PARTICULAR TRENDS TO EMERGE OR CONTINUE?

dependency and the diversification of the economy, which is obviously still required. As a result, some structural infrastructure projects are likely to be developed in spite of the negative macroeconomic scenario. According to Angola's national development plan for 2013-2017, the structural infrastructure projects are mainly directed at the energy sector including transportation and distribution of energy, rural electrification and mini-hydro, the transport sector including construction of new roads, secondary and tertiary roads, and the water and sanitation sector including water supply in the most populated municipalities and in rural areas. Due to cuts in public spending, the diversification of funding sources for infrastructure projects will play a pivotal role. In light of this, project finance has the potential to become an attractive and viable alternative to public funding.



www.angolalegalcircle.com

Irina Neves Ferreira

Partner

Angola Legal Circle

+244 926 877 476

irinaferreira@angolalegalcircle.com

Irina Neves Ferreira is partner at Angola Legal Circle Advogados. She is a lawyer with considerable international experience, especially in the Angolan jurisdiction. In this market she has been involved in operations concerning private investment, insurance law, real estate (including providing support in the negotiation of lease contracts for petrol companies), tax law, foreign exchange law and customs. She also has a high degree of experience in corporate compliance, attained through her role as counsel for the EMEA (Europe, Middle East and Africa) region in the international compliance team of multinational company Hewlett Packard.



MOZAMBIQUE

PAULA DUARTE ROCHA
HENRIQUES, ROCHA & ASSOCIADOS



Q HOW WOULD YOU CHARACTERISE THE KEY TRENDS IN INFRASTRUCTURE INVESTMENT IN MOZAMBIQUE OVER THE LAST 12 MONTHS OR SO? DO INVESTORS SEEM TO BE ATTRACTED TO OPPORTUNITIES IN PARTICULAR SEGMENTS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY, COMMUNICATIONS, WASTE MANAGEMENT, HEALTHCARE OR EDUCATION?

ROCHA: Mozambique remains one of the most attractive markets in Sub-Saharan Africa with abundant natural resources being key for infrastructure development and rehabilitation. Low commodity prices, political instability and a debt crisis that has led to suspension of international aid, along with the metical depreciation – GDP growth slowed to 3.7 percent – have, however, been stalling the economy for the last 12 months or so, posing challenges to any investment opportunities. Investment opportunities in the energy, power and transport segments have not lost momentum, but the pace of negotiation slowed down and promising projects are yet to be implemented. The Catembe Bridge in Maputo, and the new port of Beira, both funded by China, have been the most significant infrastructure investments in the country since 2014.

Q WOULD YOU SAY THE GOVERNMENT IN YOUR REGION IS COMMITTED TO INFRASTRUCTURE INVESTMENT AND DEVELOPMENT? ARE PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AND PRIVATE FINANCE INITIATIVES (PFI) BEING USED TO ACHIEVE OBJECTIVES?

ROCHA: Opportunities around the natural resources space remain unlimited, with large investment flows from the gas and coal sectors expected from 2017. Furthermore, the government is still committed to infrastructure investment and development, the main challenge now being restoring international credibility so as to regain the confidence of investors and to attract foreign direct investment. Faced with this new challenge, the government is also considering structural measures to diversify the economy so as to channel the gains derived from natural resources and reduce the country's dependence on such resources. Agriculture and manufacturing are now also among the government's top priorities.



Q WHAT FUNDING SOURCES ARE ACTIVE IN THE PROJECT FINANCE MARKET? IS THERE A STRONG APPETITE TO LEND? WHAT KINDS OF PROJECTS ARE MOST LIKELY TO BE FUNDED?

ROCHA: In the aftermath of the devaluation of the metical and in an attempt to control inflation, the Bank of Mozambique, which is the country's central bank, has tightened monetary policy. This has considerably reduced access to local funding. Reserves of foreign currency continue to drop and high interest rates are a disincentive to borrow. The central bank's recurrent increases to the standing lending facility and changes to the compulsory reserves coefficient rules are directly affecting commercial banks, which in turn are being forced to implement measures that make the cost of borrowing in Mozambique considerably high. Foreign lending thus is increasingly 'the option' for investment projects in general, guaranteeing low and fixed exchange rates on loans with longer tenors.

Q WHEN EXECUTING INFRASTRUCTURE DEALS, HOW IMPORTANT IS DUE DILIGENCE TO MANAGE THE RISKS AND REGULATORY CHALLENGES? WHAT CONSIDERATIONS NEED TO BE MADE WHEN NEGOTIATING AND PREPARING TRANSACTION DOCUMENTS?

ROCHA: Due diligence is crucial, if not to keep pace with and ensure compliance with constant legislative developments, to mitigate common risks associated with the gap between legal principles and common practice, including the potential for corruption risks. Additionally, adjusting transaction documents drafted in accordance with current international practices to conform with local, civil law principles and Mozambique rules of general application, is often not easy and requires knowledge of transversal legislation applicable to the scope of each transaction. In general, one should bear in mind that in Mozambique, as in most sub-Saharan jurisdictions, what often happens in practice does not conform to one's expectations, even those that are founded on one's extensive knowledge of the applicable law in force at any given time and of one's familiarity with such practice. Therefore, when negotiating and preparing transaction documents, consideration must be given to the all-embracing possibility that in some respects accounts might be at odds with a certain practice. Flagrant examples exist where a certain sectoral legal diploma establishes public tender as the standard procedure for negotiating and awarding a concession contract, while directly applicable transversal



legislation may open exceptions to such a regime, and allow for a direct award.

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Q IN YOUR EXPERIENCE, WHAT ELEMENTS ARE ESSENTIAL TO OPTIMISING EXISTING PROJECTS, GENERATING RETURNS AND CREATING LONG-TERM VALUE FROM INFRASTRUCTURE INVESTMENTS?

ROCHA: The majority of economic sectors in Mozambique still require a significant amount of private investment. Besides Mozambique's urgent need to restore international credibility so as to regain the confidence of investors and attract foreign direct investment, reducing barriers to private infrastructure finance – that often impacts on projects' bankability – and diversifying the economy, including developing and reducing the rules imposed on the financial sector, as a desperate and inefficient measure to control the inflation rate, are essential to optimising existing projects and projects in the pipeline and creating long term value from infrastructure investments.

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Q TO WHAT EXTENT ARE YOU SEEING MERGERS AND ACQUISITIONS INVOLVING INFRASTRUCTURE ASSETS? WHAT PARTICULAR CHALLENGES TEND TO ARISE WHEN EXECUTING DEALS IN THIS SENSITIVE SECTOR?

ROCHA: The country's vulnerable economy, along with the considerable increase in security risks due to political instability seems to be promoting the 'appetite' for current players involved in infrastructure assets in Mozambique to partner with and bring in new investors to share the risk. The country's international credibility now more than ever requires the government's support and commitment to ensure the bankability of projects in the pipeline.

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Q WHAT ARE YOUR PREDICTIONS FOR INFRASTRUCTURE AND PROJECT FINANCE IN MOZAMBIQUE OVER THE COMING MONTHS? DO YOU EXPECT PARTICULAR TRENDS TO EMERGE OR CONTINUE?

ROCHA: Natural resources will continue to set the pace for the development of infrastructure and project finance in Mozambique, with the development of LNG projects playing a major role in restoring the country's welfare, creating investment opportunities and encouraging growth momentum. News circulated on 28 September 2016 indicates that ENI has begun to make contact with banks to secure the billions of dollars it needs to explore the natural gas deposits in Mozambique Area four, a project entailing the financing and operation of a FLNG unit, with capacity to produce 3.3 million tonnes of LNG a year. In early October there were indications that Mozambique and ENI had signed a 20-year

“Natural resources will continue to set the pace for the development of infrastructure and project finance in Mozambique.”

deal to sell LNG to BP. It is only fair to assume that the financial investment decision on ENI's project, initially expected for the end of this year, will be taken sooner than expected and will certainly help Mozambique to regain growth momentum. One must not ignore the fact that Anadarko's final investment decision regarding its project in Mozambique's Offshore Area one, entailing an onshore LNG terminal, is yet to be delivered. Non-official sources indicate that Exxon Mobil – recently awarded three exploration licences for offshore blocks to the south of the Anadarko and ENI discoveries – is considering acquiring participating interests in both the ENI and the Anadarko projects. The outcome of those deals will provide the government with much needed foreign currency in the form of capital gains tax, worth approximately \$1.3bn according to non-official sources. These facts and expectations indicate that Mozambique infrastructure investment will soon regain momentum and that the country will continue progressing as one of the most attractive markets in Sub-Saharan Africa.

HENRIQUES, ROCHA
& ASSOCIADOS
Sociedade de Advogados, Lda.



www.hrlegalcircle.com

Paula Duarte Rocha

Partner
Henriques, Rocha & Associados
+258 2134 4000
pdrocha@hrlegalcircle.com

Paula Duarte Rocha is a founding partner of Henriques, Rocha & Associados, a firm member of MLGTS Legal Circle as Mozambique Legal Circle (MLC). She is highly experienced in the Mozambican market having intervened in all areas of practice advising both national and foreign investors, with notable experience and track record in banking and project finance transactions, and in energy and infrastructure transactions.



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