INFRASTRUCTURE & PROJECT FINANCE

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

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INTRODUCTION

There have been some interesting developments in the global infrastructure market in the first half of 2018, with further new opportunities anticipated for the second half of the year.

The UK market remains disappointing, however. The private finance initiative (PFI) concept introduced in 1992 has dramatically fallen out of favour over the past year. Political support for the concept has collapsed among the previously enthusiastic Labour party, which has announced that it will move projects back under public sector control if or when it returns to office. At the same time, the collapse of Carillion, a major PFI construction player, has increased public opposition to private sector investment in infrastructure.

In addition, the UK National Audit Office (NAO) published a report in January which threw doubt on the methods used to calculate 'value for money' when comparing public and private sector investment for a project. The NAO maintains it cannot assess the actual efficiency of PFI or carry out an evaluation of the actual performance of PFI at the project or programme level.

We need more independent research globally on the value of private investment in infrastructure to counter these ambiguous and often incorrect assertions made against the PFI concept.

Globally, the PFI and public-private partnership (PPP) models have been shown to be better value for money and more efficient, in both the construction and operational phases, than infrastructure projects built and operated in the public sector. Fortunately, in other countries we are seeing further expansion of private sector investment and operation of infrastructure.

After a slow start, the Indonesian government's Infrastructure Plan now includes a requirement of 33 percent investment from the private sector. The Indonesian National Procurement Agency has been developing a new PPP procurement regulation and model bid documents which are presently out for consultation.

Following the 2016 elections in Argentina, the Ministry of Finance has now developed a PPP plan which requires a total of $26bn international investment in energy, mining, transport, communications, technology and social infrastructure. Some 60 projects have been identified with six road projects already out for tender.

The Japanese government has demonstrated its support for improving infrastructure through private investment and operation by announcing it intends to create a wealth fund to invest in American infrastructure projects. The state-backed fund will support infrastructure construction, along with resource development and storage, as well as investing in joint US/Japanese projects in other countries.

In the US M&A market, we are seeing a trend of developers selling down their project equity to passive institutional investors, like pension funds and sovereign wealth funds. They are also welcoming less expensive capital being brought into the market, as it allows developers' capital to be recycled into new projects.

Globally, we are seeing an enthusiastic interest in smart cities. The vision entails a city using renewable energy, energy efficiency, non-polluting transportation and the creation of local and regional electricity grids with services tied together by interconnected digital technology. The aim is a clean environment with adequate and clean power supplies at the lowest price. Likewise, interest in the green bond market continues to grow globally and offers corporate entities the ideal funding for smart cities. The UK is presently looking at a private finance 2 (PF2) or PPP model that could be used to procure district heating networks across the UK, offering a potential link to the new garden cities proposed.

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Irina Neves Ferreira joined Angola Legal Circle Advogados in September 2013. 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. Furthermore, she is highly experienced in corporate compliance – expertise attained from her role as counsel for the Europe, Middle East and Africa (EMEA) region in the international compliance team of the multinational company Hewlett-Packard.

Q. How would you characterise infrastructure investment in Angola over the last 12 months or so? Do investors seem to be attracted to opportunities in particular segments?

FERREIRA: Angola elected a new president in 2017 and he has stated on various occasions, including through the Governmental Programme for 2017-2022, that the Angolan executive is committed to making public investments in infrastructure, in particular in key sectors such as energy, water, roads, railways, ports and airports, in order to boost private investment in the country's provinces. For example, in the last 12 months, Laúca Dam in the province of Malanje and a 10 km railway in Luanda – the so-called 'nova marginal' – have been completed. From a private investment standpoint, the newly-approved private investment law – Law no. 10/18, 26 June 2018 – identifies infrastructure as one of the key strategic areas for development. This was foreseen in the National Development Plan 2018-2022. Recently, there has been a growing interest in infrastructure investment, both by domestic and foreign investors, with particular emphasis on electricity generation facilities. In its 'Long Term Strategy for the Electricity Sector', the Angolan government has determined that the electricity sector will require $23bn in investment from public and private funds.

Q. To what extent is the government in Angola using public-private partnerships (PPPs) and private finance initiatives (PFI) to achieve infrastructure objectives?

FERREIRA: Public-private partnerships (PPPs) are not a traditionally used method of contracting in Angola. The government may resort to private finance initiatives (PFI) to leverage public projects. These PFIs must be authorised by the president and subsequently published in the Official Gazette.

Q. What funding sources are active in the project finance market? Is there a strong appetite to lend?

FERREIRA: The Angolan project finance market is neither very active nor mature. Generally, the main sources for funding are still local commercial banks, which may enter into short-term financing agreements with private investors. From our experience, most of the country's infrastructure projects are financed either by local commercial banks, international commercial banks or export credit agencies. However, with the recent depreciation of the kwanza and the shortage of foreign currency in Angola, as a result of the last fall in the price of a barrel of oil, the transfer of funds from international financial and governmental entities to Angola has significantly decreased. In Angola we have a close foreign exchange system, meaning that the repayment of the principal and payment of the relevant interest, within the context of a financing agreement entered into with an international financial institution, for instance, must be preceded by approval from the Angolan Central Bank. Moreover, the capital market is still in an early stage and has not yet become the key driver for project finance initiatives through the issuance of shares or bonds, and there is no known investment fund currently active.

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?

FERREIRA: Appropriate planning and due diligence are important steps within the execution process, specifically when the sources of funds are derived from other countries or jurisdictions. Finance due diligence will seek to ascertain that a project is 'bankable', in the sense that the project actually generates a positive cash flow, that the owner of the infrastructure has guaranteed that the payment conditions are met, such as exchange rate variation control, and whether refunds and profits are expatriated with no constraints of a financial, legal or regulatory nature. The negotiation and preparation of transaction documents should also take into consideration potential time slippages and related consequences, such as exceeding the project's budget.

Q. In your experience, what elements are essential to optimising projects, generating returns and creating long-term value from infrastructure investments?

FERREIRA: One important element that must be dealt with, in a thorough manner, is the insufficient experience and exposure of local, mid-level decision makers on the international infrastructure and project finance scene. An immersion in this scene would significantly allow mid-level decision makers to experience international infrastructure and project finance realities that could bring more agility and flexibility to their decision-making processes, and which could expedite negotiations with public entities and enable quicker project implementation, for example by raising awareness of what usually constitutes a bankable deal. Furthermore, 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 infrastructure, maximising the use of the assets and the benefits for users.

Q. To what extent are you seeing M&A involving infrastructure assets? What particular challenges tend to arise when executing deals in this sensitive sector?

FERREIRA: Infrastructure and project finance has been primarily funded by PFIs, which may combine short-term loans, intended to be used for initial local payments, with funding sources from other jurisdictions, used to design, develop and construct the project. This, combined with

> *“With particular focus on electricity generating facilities, infrastructure has been piquing the interest of domestic and international investors of late.”*

the fact that the status quo of the Angolan financial market is not as favourable as it was between 2009 and 2014, has seen investors seek to assure that their projects are able to generate a positive cash flow and that it can be used with no constraints arising from the actual economy for the payment of international debts.

Q. What are your predictions for infrastructure and project finance in Angola over the coming months? Do you expect particular trends to emerge or continue?

FERREIRA: With particular focus on electricity generating facilities, infrastructure has been piquing the interest of domestic and international investors of late.

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