Levelling the playing field

By Mauricio Endo, KPMG in Brazil

In a bid to encourage greater international competition for projects, Brazil's new US$64 billion infrastructure program reduces subsidized credit, eases restrictions on profits, and gives contractors more time to prepare bids.

The announcement of a new set of infrastructure concessions has raised hopes that Brazil can finally start to attract a significant amount of foreign investment into the sector. The latest package, worth 64 billion US dollars (US$), covers roads, railways, ports, and airports, and is designed to open up a market traditionally thought to favor domestic contractors.

A previous set of concessions in 2012 enjoyed mixed fortunes. Although contracts for two-thirds of road projects and both airport projects were completed, none of the port or rail tenders managed to close. This time around, the government is determined to create the right conditions to avoid a repeat, with a number of important changes to its approach.

In recognition of the complexity of infrastructure projects, the deadlines have been substantially lengthened, to give potential bidders sufficient time to carry out detailed studies into construction, demand and capital expenditure, to more accurately size the costs and risks. Foreign investors have, understandably, less knowledge of the Brazilian market, so this extension should increase their chances of preparing a competitive bid. In addition, the judging criteria will now acknowledge contractors' overall international track record, and not just their experience within Brazil.

The financing environment has changed considerably. Whereas previous programs imposed a maximum internal return on investment, the latest concessions have no fixed ceiling, and will instead be assessed on a case-by-case basis, to ensure that contractors can achieve margins in line with the sector average.

An abundance of cheap debt from the Brazilian Development Bank (BNDES) has meant that taxpayers have effectively subsidized contractors, which has tilted the odds towards domestic players with local contacts. To address this imbalance, debt-to-equity ratios have been adjusted for each of the four sectors of roads, railways, ports, and airports. The maximum proportion of a project that can be financed by the BNDES, at subsidized rates of interest, has been reduced to 45 percent for roads, 35 percent for ports and airports, and 70 percent for rail[1]. In a bid to make financing more internationally competitive, BNDES will offer more subsidized funding to companies that raise debt on capital markets via infrastructure debentures – which also carry tax incentives until 2020.

“In a bid to make financing more internationally competitive, BNDES will offer more subsidized funding to companies that raise debt on capital markets via infrastructure debentures – which also carry tax incentives until 2020”

1. http://www.bnamericas.com/news/infrastructure/brazils-bndes-cuts-infra-project-financing-limit-in-half

Restoring confidence

With many Brazilian construction companies embroiled in the corruption scandal involving state-run oil company Petrobras, the government is keen to create an environment of transparency. The country's 2014 Anti-Corruption Law has sent a strong signal that unethical business practices will be outlawed and prosecuted, and should reassure foreign businesses that they will encounter a more level playing field when bidding for projects within Brazil.

A series of international roadshows are taking place in 2015 in selected countries, to broadcast the opportunities to interested investors. The tenders are expected to be carried out by 2017, with the rights to 29 ports, along with four highways totaling 2600 kilometers (km), up for auction by the end of 2015, further 11 road projects scheduled for 2016, and four international airport and six rail concessions (covering 7500 km of track) scheduled from 2016 to 2017.

The single biggest initiative, worth an estimated US$13 billion, is an ambitious railway linking the Atlantic and Pacific oceans via Peru, while airport developments include the cities of Salvador, Florianópolis, Fortaleza and Porto Alegre.

After a troubled few years, Brazil's economic revival is dependent upon strong infrastructure. President Dilma Rousseff, currently in her second term in office, has pledged commitment to private finance to bridge the funding gap, stating that "This initiative reflects the partnership and the confidence that must be established and which must be unflagging between the government and the private sector."[2] If these efforts can encourage a critical mass of foreign investment into infrastructure, they could help re-establish Brazil as a key destination for international capital.

A snapshot of Brazil's US$64 billion infrastructure program

Sector	Sector Program Value	Minimum equity per project	Maximum TJLP subsidized funding from BNDES	Minimum infrastructure debenture required to qualify for maximum TJLP subsidized funding from BNDES
Roads	US$21 billion	30%	45%	25%
Railways	US$28 billion	10%	70%	20%
Ports	US$12 billion	30%	35%	35%
Airports	US$3 billion	30%	35%	35%

Discover more about investing in infrastructure in Brazil

Mauricio Endo, Head of Government & Infrastructure for KPMG in Latin America, has worked extensively with many foreign investors, helping them navigate a complex regulatory and financial environment. Over the last 15 years, he has advised private investors by structuring infrastructure projects private initiatives, competing in bids and project financing. He has worked with governments to structure concession programs in several sectors, such as airports, ports, power, roads, railways, water and social infrastructure – with total investments adding up to more than US$15 billion.

2. *Brazil outlines $65bn infrastructure package*, Financial Times, 10 June 2015.

Contact us

Dane Wolfe
Marketing Manager
Global Infrastructure
KPMG International
T: +1 416 777 3740
E: dmwolfe@kpmg.ca

kpmg.com
kpmg.com/socialmedia

kpmg.com/app

Download on the App Store

Designed by Evalueserve.
Publication name: Foresight.
Publication number: 132581-G
Publication date: July 2015