

# INFRASTRUCTURE & PROJECT FINANCE

ANNUAL REVIEW 2015



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

[www.financierworldwide.com](http://www.financierworldwide.com)

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

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The background of the page is a grayscale image of architectural blueprints. The blueprints show various technical drawings, including floor plans with rooms and corridors, and cross-sections of buildings. The lines are thin and black on a light background. The text 'INTRODUCTION' is overlaid on the left side of the page, with a red horizontal bar above it.

## INTRODUCTION

Infrastructure investment and development is a vital tool for modern economies, creating jobs and helping to deliver growth.

Since the onset of the financial crisis of 2007-08, governments have been forced to get creative. In the US, for example, federal, state and local level governments have explored novel means of securing infrastructure investment from alternative sources. Private investment in particular has been adopted by virtually all types of infrastructure assets. This has not, however, been restricted just to the US market; public-private partnerships (PPP) and private finance initiatives (PFI) have become a core part of modern infrastructure development.

The importance of private investment is most vital in areas where core infrastructure assets are in a state of disrepair and local authorities are unable to provide the capital needed to maintain or improve their services. Though there tends to be some resistance to private investment in infrastructure development, public opinion, in certain jurisdictions, is shifting.

The alarming slowdown of the Chinese economy in the second half of 2015 has also had a bearing on infrastructure development and funding. In China, the government has launched a series of reforms to encourage local governments to structure PPP projects and issued government bonds. The PPP model has proven conducive to both growth and reform, with budget restraints likely to remain in place for most governments, we are entering the era of the PPP.



# PORTUGAL

**TERESA EMPIS FALCÃO**

VIEIRA DE ALMEIDA & ASSOCIADOS, SOCIEDADE DE ADVOGADOS, R.L.



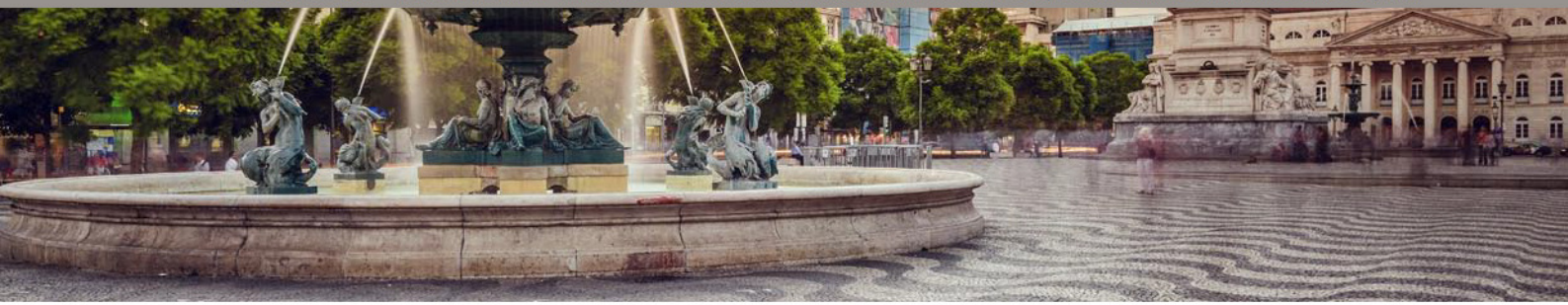
**Q HOW HAS THE INFRASTRUCTURE SECTOR FARED IN PORTUGAL OVER THE LAST 12-18 MONTHS? HOW ARE ECONOMIC CONDITIONS AND GOVERNMENT BUDGETS AFFECTING INFRASTRUCTURE INVESTMENT AND DEVELOPMENT?**

**FALCÃO:** In early 2014, the Portuguese government approved the Strategic Plan for Transport and Infrastructure, which has earmarked a range of infrastructure projects that could have a positive impact on Portugal from 2014 to 2020. The priority projects include the development and expansion of major Portuguese ports, the modernisation of the Portuguese rail freight sector, a few projects in the road sector deemed essential to complete the road network, and the increase of cargo capacity at the Lisbon airport. However, despite the approval of the Plan and the end of Portugal's EU/IMF bailout programme in June 2014 with the economy showing signs of a slow recovery, the project finance and PPP business in Portugal remains quiet. Most of the activity in the infrastructure sector, over the last 12-18 months, was focused on the renegotiation of existing PPP contracts, particularly in the road sector, aimed at reducing public expenditure, and also in the port sector with respect to the port concessions with a view to reducing operation costs and promoting exports. Indeed, PPPs are still the subject of strong public suspicion and, hence, only a few projects listed in the Plan have been formally launched. In addition, the legislative elections of 4 October 2015 have had the effect of postponing governmental decisions on major infrastructure.

**Q WHAT TYPES OF INFRASTRUCTURE PROJECTS ARE PROVING POPULAR AT PRESENT? WHAT OPPORTUNITIES EXIST IN AREAS SUCH AS ENERGY AND POWER, TRANSPORT, WATER SUPPLY,**

**FALCÃO:** For the past two years, most activity in the infrastructure sector has been focused on the renegotiation of the existing PPP contracts. The renegotiation of those projects has increased the potential for refinancing and secondary market sales in those sectors. In the energy sector, the market has seen a number of sales of large portfolio of renewables. There is also recognisable interest in Portuguese ports, although so far only the Lisbon cruise terminal and a small multi-purpose terminal – also in Lisbon – have come onto the market. Finally, the government has launched a privatisation programme which has





COMMUNICATIONS, WASTE  
MANAGEMENT, HEALTHCARE  
AND EDUCATION?

proven to be a success in terms of attracting foreign investors and which encompassed the privatisation of the state-owned airport operating company, the Portuguese airline carrier, the award of the concession for public transport networks in Lisbon and Porto and the privatisation of the state-owned waste management company.

**Q** TO WHAT EXTENT  
IS THE GOVERNMENT  
INTRODUCING POLICIES AND  
INCENTIVES TO ATTRACT  
PRIVATE INVESTMENT TO  
FUND INFRASTRUCTURE  
DEVELOPMENT? HAS  
THERE BEEN AN INCREASED  
APPETITE FOR PUBLIC-  
PRIVATE PARTNERSHIPS  
(PPPS) AND PRIVATE  
FINANCE INITIATIVES (PFI),  
FOR EXAMPLE?

**FALCÃO:** Portugal's negative investment grade rating has not deterred investor appetite for assets with long term predictable revenues and which are not overly reliant on the local economy for growth. The stability of regulation contributed enormously to maintaining investor confidence in Portuguese assets, hence ensuring the success of the privatisation programme launched by the government, driven by the terms of the EU/IMF bailout. In addition, the fact that the government elected to renegotiate the PPP contracts and extensions to the feed-in tariffs regarding renewables, rather than imposing unilateral modifications to the same, has proven to be extremely important to incentivising the demand for Portuguese assets and the Portuguese market. Moreover, by bringing PPP contracts to sustainable standards, the renegotiation process has increased the likelihood for secondary market sales of PPP assets and the refinancing of original financing contracts. Notwithstanding the above, the appetite for PPPs is still low.

**Q** WHAT TRENDS HAVE YOU  
SEEN IN PROJECT FINANCE,  
IN TERMS OF PRICING,  
TERMS, WILLINGNESS TO  
LEND, AND SO ON?

**FALCÃO:** There is currently no significant pipeline in Portugal for greenfield projects. Accordingly, the most recent project experiences relate to secondary market sales of PPP assets and the refinancing of existing project finance packages. We feel that there are funds available and a willingness to lend on the part of banks and other entities, such as private equity funds, pension funds or investment funds, but

a scarceness of projects to finance. In terms of pricing and funding conditions, the market has improved significantly from the borrower's perspective and no doubt the maturity of the projects at stake helps to strengthen the borrower's case.

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

**FALCÃO:** Although PPPs are expected to create synergetic dynamics by drawing on the strengths of each partner for efficiently delivering public services at a lower cost, evidence suggests that this is not necessarily the case and that PPPs have been beset with problems and limitations. The 'optimism bias' in project assessments by governments has led to ineffective risk transfers and implicit liabilities such as guarantees which may result in excessively large contingent liabilities and, consequently, in governments making large unexpected payments. In our experience, costs and delays are systematically underestimated, while the benefits are often overestimated in infrastructure PPPs. Due diligence is, therefore, absolutely crucial to ensure that limited resources are directed toward carefully selected projects, rather than projects that deliver benefits far lower than those estimated, with obvious counterproductive results, especially for resource-constrained economies such as Portugal.

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

**FALCÃO:** It is essential to put in place robust off-take arrangements or availability-based models or other similar arrangements, refinance existing projects by resorting to alternative and cheaper sources of funds, such as capital markets or funds provided by entities other than traditional commercial banks, and to promote competitive markets in order to reduce operational costs. It is also worth mentioning that for PPPs to be successful, governments must have a clear policy framework and effective procurement and management skills, which can help in prioritising sectors, designing bankable projects, distributing risks appropriately, and assessing technical and financial viability of projects. Appropriate legal and regulatory frameworks must also be put in place.

**“For PPPs to be successful, governments must have a clear policy framework and effective procurement and management skills.”**

**Q** LOOKING AHEAD, WHAT KEY TRENDS DO YOU EXPECT TO SEE IN INFRASTRUCTURE AND PROJECT FINANCE IN PORTUGAL OVER THE COMING MONTHS?

**FALCÃO:** We expect to see small-size projects compared to the mega-projects of the 1990s and 2000s. These include infrastructure projects focused on cities and social equipment infrastructure – hospitals, health centres, prisons, public buildings, and so on. We also expect to see continued secondary market sales of assets with renegotiated contracts and consequential refinancing, particularly in the road sector, which help to deleverage Portuguese construction companies and domestic banks.



**VIEIRA DE ALMEIDA**  
& Associados Sociedade de Advogados, R.L.

**Teresa Empis Falcão**

Partner

Vieira de Almeida & Associados, Sociedade de Advogados, R.L.

+351 21 311 3478

tef@vda.pt

Teresa Empis Falcão graduated in Law in 1995 from the College of Law of the Portuguese Catholic University. She took an LL.M in Banking and Finance Law at the London School of Economics and Political Science. She joined the London office of Allen & Overy LLP as a member of the Projects Group. Ms Falcão joined Vieira de Almeida & Associados, RL, in December 2008, where she was a managing associate in the Projects – Energy, Infrastructure and Natural Resources practice group.





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