

# AKE Special Report

## Public-Private Partnerships (PPPs) in Latin America



### Overview

Public – Private Partnerships (PPPs) are widely regarded as an effective and collaborative way for countries to address financial and development needs. Across Latin America, there has been significant growth in the number of PPP projects, attracting large amounts of investment. This AKE Special Report looks at the environment for PPP projects in Chile, Brazil, Colombia and Argentina, highlighting the progress that has been made but also outlining where improvement is still needed. Several countries in the region have made progress in developing their PPP legislative and regulatory frameworks, including new PPP legislation and the allocation of PPP-specific units. However, implementation challenges such as improving transparency in the PPP development process and the recurrent prominent role of corruption continue to threaten the full development of this tool. Effectively tackling these issues therefore remains key in order for PPPs to significantly contribute to sustainable economic growth in the region.

### Public - Private Partnerships

Since the 2008 global financial crisis, there has been renewed interest in Public – Private Partnerships (PPPs) in both developed and developing countries. Facing constraints on public resources and fiscal space, as well as recognizing that investment in infrastructure facilitates economic growth, governments have increasingly turned to the private sector as an alternative source of financing to overcome their funding gaps. According to the World Bank's Private Participation in Infrastructure Project Database (PPI), there have been a total of 3,517 PPP projects in low- and middle-income countries between 2008 and 2017. Thus far, collaborative efforts between the public, private and civil sectors have proven effective in addressing major social challenges, such as poverty, public health and education. Such partnerships therefore also respond to the ever-growing calls on the private sector to do more in support of the United Nations' (UN) Sustainable Development Goals. Alongside this, the private sector also has a direct interest in tackling these key challenges to improve the overall business climate in a given country.

Over the past decade, several international donor agencies, multilateral lenders and firms, including the World Bank and the Organization for Economic and Cooperative Development (OECD), have focused their efforts on developing specific guidelines for generating and implementing PPP projects. In addition, they have devised frameworks for evaluating countries' abilities to attract and sustain private investment in infrastructure via PPPs. Latin America and the Caribbean (LAC)

stands out because large investment flows into the region have remained relatively stable year-on-year since 2007. In 2016 PPP projects in LAC attracted US\$33.2bln in investment, representing 47 per cent of global investment in infrastructure with private participation. Most of the projects were in Brazil, Colombia and Mexico, and in the energy, transport and water sectors. Overall, there has been positive progress in the environment for PPP infrastructure in the region, particularly regarding legislative, regulatory, and financial frameworks. However, transparency and accountability in developing PPPs remain problematic. For instance, only a few Latin American countries fully disclose project information.



### About us

*AKE is a political and security risk consultancy firm with over 20 years of experience working with the insurance sector, providing clients with unrivaled political and economic risk consultancy. Our experienced team of regional experts provides tailored analysis and strategic forecasting, allowing our clients to better monitor, manage and mitigate risks. Our flagship Global Intake platform contains country political and security risk profiles, ratings and violent incident mapping, Daily Risk Updates and twice-weekly Analytical Briefings on key developments. We also provide bespoke consultancy services, including tailored reports on specific country risks. Contact us for further information or a free trial.*

## Frameworks, Institutions and Support

Legislative and regulatory frameworks for PPPs have recently been developed in several countries in the region, including Argentina, Costa Rica and Nicaragua. It will inevitably take time to properly implement the frameworks. Other countries with more experience in PPPs, such as Chile, Brazil and Mexico, have extended PPP legislation to new areas including sports arenas and recreational, educational and prison facilities.

Several countries in the region have established national infrastructure plans by allocating PPP-specific units to support the implementation of projects beyond a government's term in office. Relevant examples of this positive trend include Brazil, which in May 2016 created the new Investment Partnership Programme (PPI) Secretariat to coordinate PPP policy, providing technical support and oversight of PPP projects. In October 2016 Nicaragua's new PPP law created the General Directorate of Public Investments to promote technical support and supervise PPP contracts. In November 2016 new legislation in Argentina created a PPP unit, which will soon be in charge of collecting all contracts governed by the new PPP regulatory framework and will provide consultative, operational and technical support to project formulation, preparation of bidding documents and contract performance.

**“Political support for PPPs is strong across the region, favouring development of frameworks for implementation.”**

Political support for PPPs is strong across the region, favouring development of frameworks for implementation. According to the Infrascope 2017 results, 18 of 19 countries scored highly in PPP support from senior politicians, apart from Guatemala where there was a lack of data. However, the region shows a mixed picture overall regarding support across the political spectrum. While nine countries reported support for PPPs across the political landscape, 15 experienced public opposition to PPPs.

## Country overviews

### Chile

Chile has more than 25 years of experience in private-sector participation in public infrastructure projects, leading the region in this area. During 1990-2016, Chile awarded a total of 197 projects, worth approximately US\$69.4bln, including 16 airports, 12 ports, 35 major roads, 26 water and sanitation facilities and 87 electricity projects, to private enterprises. There is a high level of industry concentration, with only a few firms winning a major share of PPP contracts. Only three firms account for almost 80 per cent of all projects: Almendral SA from Chile (with investments of US\$2.8bln across 81 projects), Telefonica SA from Spain (with investments worth of US\$10.8bln across 75 projects) and SUEZ from France (with investments totalling of US\$7.9bln across 71 projects).

Chile has a strong regulatory and supporting institutional framework for PPPs, which is reinforced by a solid investment and business climate and well-developed financing instruments. Chile's current PPP regulatory framework was established by Law No. 20410 of Public Works Concessions of January 2010 (Ley de Concesiones de Obras Públicas), which made significant improvements to the existing legislation, including greater transparency and incorporating more objective criteria to compensate private actors in the case of license cancellation or expropriation of assets. However, Chile faces two key challenges in PPP infrastructure development: the high project costs and an ever-growing demand for greater transparency across the PPP process, including improved costs monitoring, service levels and economic performance.



The upcoming November 2017 general elections, in which centre-right former president Sebastian Pinera seems increasingly likely to win, are not expected to negatively affect the PPP framework.

### Colombia

Colombia is also amongst the countries with the largest number of PPP projects in the region. Between 1990 and 2016, it awarded a total of 180 PPP infrastructure projects worth around US\$62.6bln, including nine airports (US\$1.5bln), 29 electricity projects (US\$12.9bln), nine information and communication technology (ICT) projects (US\$18.8bln), 11 natural gas projects (US\$1.1bln), 13 ports (US\$2.5bln), two rail projects (US\$500m), 55 roads (US\$24.2bln), and 52 water and sanitation facilities (US\$1.1bln).

Colombia has a strong regulatory framework for PPPs, approved in Law No. 1508 of 2012, applied to any government entity at the national or subnational level. Later regulations were compiled in Law No. 1082, providing additional requirements for project planning and structuring, guidelines for co-ordination between government entities, conflict resolution mechanisms, elimination of obstacles for licensing, and stronger support of the transport sector. The development and maintenance of PPP projects has attracted a significant degree of private-sector participation in infrastructure projects.

## **“The main challenges for PPP development remain achieving financial closure ... and the execution of Fourth Generation (4G) infrastructure projects.”**

The main challenges for PPP development remain achieving financial closure, which continues to be hampered by the lack of transparency, and the execution of Fourth Generation (4G) infrastructure projects. However, costs have significantly decreased with the implementation of the PPP Law in 2012. Further necessary improvements include developing social projects under the PPP scheme, providing adequate incentives to attract new investors for all sectors, and enhancing sub-national level capacities to develop projects under the PPP law.



Private participation in infrastructure investment is likely to remain a priority for whichever administration manages to secure power following the May 2018 presidential elections.

## **Brazil**

Brazil's PPP environment is relatively well developed, with a total of 774 projects tendered in the past two decades. However, Latin America's largest economy continues to struggle to bridge its infrastructure gap. Brazil has relied heavily on PPP projects to address challenges of increasing investment. Two key trends are expected to shape the development of further PPP projects over the coming years according to the 2017 Infrascope report. First, the diversification of the type of assets and services delivered by PPP mechanisms, including public services such as healthcare, education, prisons and street lighting amongst other projects. Secondly, the leading role of subnational governments in infrastructure development outside the energy sector. Most of the projects in 2016 were led by local authorities, which remain likely to produce more subnational non-energy sector projects in the coming years.

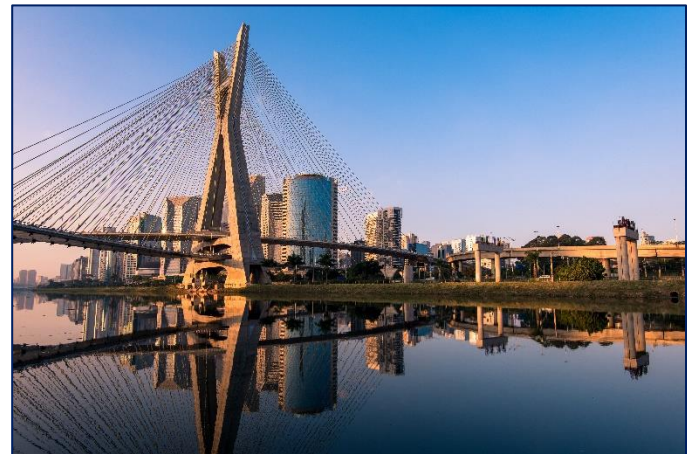
Brazil has had a strong regulatory environment for PPPs since the mid-1990s. The current PPP regulatory framework was established in two laws: Law 8987 of 1995 on the Concessions Regime and the Provision of Public Services and law 11074 of 2004 establishing the general rules for bidding and contracting

PPPs under public administration – enabling all levels of government to implement PPP projects.

Over recent years, Brazil's institutional environment has undergone two significant improvements. First, the creation of the Investment Partnership Programme (PPI) Secretariat, a central department for PPPs within the presidential office, which is responsible for several functions associated with central PPP units, such as the promotion of PPPs, support for procuring authorities and capacity-building. Secondly, the beginning of formal reduction of the role of the publicly-owned Brazilian Development Bank (BNDES) as the main lender for PPP capital requirements.

## **“The reduction of BNDES's subsidised lending ... should help ... create increased opportunities for commercial banks to provide long-term financing for Brazil's infrastructure.”**

In line with this repositioning of BNDES, on 5 September 2017 the Senate approved a lending reform according to which the bank's basic lending rate will be a market rate based on the five-year treasury rate instead of being freely determined by a government-run committee. The reduction of BNDES's subsidised lending will begin in 2018 and the transition is expected to take five years. The reform opens long-term lending to greater competition from the private sector and should help to diversify capital markets and create increased opportunities for commercial banks to provide long-term financing for Brazil's infrastructure.



Despite persistent uncertainty over who will secure Brazil's presidency following the October 2018 general elections – and even over who will be eligible to run – the current administration's privatisation drive is expected to gain traction and is unlikely to be completely reversed after 2018 given the pressing need to shore-up the persistently high fiscal deficit and consolidate Brazil's exit from its worst recession on record. Ongoing, evolving and emerging corruption scandals, however, could hamper efforts to consolidate private and foreign investor appetite, which nevertheless appears to be increasing.



## Argentina

Argentina's investment environment is one that is slowly emerging toward improving the attractiveness of PPPs. Following years of chronic infrastructure under-investment, the country has made important and substantive progress towards enticing private investors back into the economy. Building an environment that is conducive to PPP projects has been at the top of the economic agenda since President Mauricio Macri's administration took office in December 2015. Critically, the final approval in November 2016 of a dedicated PPP contracts law (No. 27328/2016) is expected to facilitate private and foreign investment in public projects, mainly in infrastructure, energy and housing. It is ultimately expected to become one of the main tools for channelling private investment toward not only infrastructure but also in other areas with investment deficits, including services, research and technological innovation. The law is aimed at lowering regulatory barriers to foreign investment while requiring that 33 per cent of goods and services contracted by the state come from local firms.

**“Macri's government has positioned infrastructure development through PPPs as one of the key drivers of economic growth.”**

Macri's government has positioned infrastructure development through PPPs as one of the key drivers of economic growth. Infrastructure initiatives such as the Plan Belgrano and the National Plan for Transport and Infrastructure are worth approximately US\$33.3bln in PPPs. Reflecting this improved economic potential, in March 2017 ratings agency Moody's upgraded Argentina's sovereign credit rating outlook from stable to positive, maintaining the issuer rating at B3 (speculative). S&P Global Ratings recently upgraded its sovereign rating for Argentina from B- to B.

Argentina has also made rapid progress toward developing the legal and institutional frameworks for PPPs. Since 2000 there have been two decrees establishing the framework for the promotion of private participation in infrastructure development (No. 1299/2000 and No. 967/2005), and an attempt at regulation under both the Public Works Law and the Concession of Public Works law (No. 17520/1967).

The new PPP regime was not designed from scratch. It builds on input from Latin America's main exponents of PPP experience, namely Brazil, Chile, Colombia, Peru, Uruguay and Mexico. The government also invited multilaterals and world-leading law firms to participate in the drafting process. Argentina's new PPPs legislation follows the resolution of the sovereign bond default in 2016 and several market-friendly measures introduced by Macri's administration.

However, the IMF noted that filling the infrastructure gap will take time and will require further improvements in the legal and institutional frameworks for private-sector participation. Argentina's main challenge lies in restoring confidence to raise the required financing at any government level. Relationships with multilateral institutions are improving and the government expects the private sector to contribute half of the 2018 investment in public works.

As such, infrastructure investment is forecast to increase from 2.6 per cent of GDP to 3.5 per cent in 2018, with overall capital spending expected to increase to 6 per cent in around eight years. To promote investment, the government plans to launch an ambitious infrastructure program, increasing capital spending from 2 per cent to 6 per cent of GDP in about eight years, with two-thirds coming from partnerships with the private sector. The energy sector is also likely to benefit greatly from the new PPP framework, with projects likely to accelerate following the upcoming 22 October mid-term legislative elections.



## Key challenges

### Corruption

A major challenge to the public perception of infrastructure PPP projects stems from a series of corruption scandals, involving some of the region's largest construction companies in the infrastructure sector. This includes the prominent Odebrecht scandal, which also highlights that corruption cases have extended to several countries in the region, including Brazil and Argentina. These have hindered public perceptions of private-sector involvement in major infrastructure initiatives, and forced governments to take strong measures against corrupt practices, such as voiding already signed PPP contracts. Despite short-term issues, a firmer stance against corruption and adequate deterrents could eventually bolster transparency and openness in public-private relationships, while also forcing governments to adopt new legislation to prevent similar cases in the future.

### Implementation

The efficient and transparent implementation of emerging and evolving PPP legal and institutional frameworks continues to offer room for improvement. Many countries in the region have made efforts to develop infrastructure project frameworks – including new PPP laws in Nicaragua (October 2016), Argentina (November 2016), and Costa Rica (December 2016). However, despite the establishment of PPP-specific units and increasing transparency of the PPP process, the gap between PPP legislation and its implementation in practice often persists. Addressing this gap will be crucial to the region's outlook for infrastructure development.

### Concentration

PPP projects tend to be oligopolistic in structure, with a few multinational corporations accounting for the largest proportion of projects, both in those countries with many established PPPs such as Chile, Colombia and Mexico, and those newer to these partnerships. In the case of Colombia, three firms (Mexico's América Móvil and Spain's Telefónica and Endesa) account for almost 80 per cent of the projects. The lack of industry competition could pose a risk for countries that have started to consider PPPs for infrastructure development by limiting the range of options and making the bidding process less competitive. While some markets are not large enough to attract sufficient competition from international companies, in others the current political environment deters or drives away foreign investment, such as the case of Venezuela.

### Financing

Financial facilities to support PPP projects remain a challenge in the region. Countries with weak or under-developed capital markets still rely on international institutions for funding and will need to expand alternative financing mechanisms to sustain their access to capital. In Chile, existing private pension funds have more than US\$180bln in assets under management but they are currently not allowed to directly finance infrastructure projects. The deepening of domestic capital markets could help ease the region's dependence on multilateral lenders for infrastructure funding.

## AKE's consultancy services

PPP projects will remain a key feature in the region, with marked differences between countries, some of which have a long way to go before they are able to consolidate reliable frameworks that mitigate against some of the key risks faced by private and foreign investors, and those that insure them. Indeed, the largest economies in Latin America are currently working on developing and enhancing these frameworks. AKE's consultancy team advises a wide range of clients on the political and economic risks linked to specific projects across the region and beyond, providing them with a clear understanding of the investment climate and the likelihood of such projects and the legislative and regulatory frameworks supporting them to offer viable opportunities for investment.

