

easyBrasil

FACILITATING INVESTMENT IN CONCESSIONS

Incentives to Competition,
Facilitation for Finance
and Greater Transparency

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A series of reports covering the Brazilian business environment, **easyBrasil** provides official, transparent, reliable information for those oriented toward investment and trade, and for those simply looking to learn more about the country and its economy. Each report addresses specific topics and opportunities in Brazil's diverse economic spheres, providing macro- and micro-economic information, information on regulation and policy, and forecasts, all affirmed and acknowledged by the Brazilian federal government. The series' individual reports are published as booklets in both digital and print editions.

FACILITATING INVESTMENT IN CONCESSIONS **Incentives to Competition, Facilitation** **for Finance and Greater Transparency**

A high priority of the Brazilian government at present is to attract external investment targeted to infrastructure development and services for the public. Toward this objective, the federal government has initiated legislative and regulatory measures, created new programs, reinforced incentives for competition, improved financing mechanisms, and established a standardized and permanent agenda for concessions.

Bids for infrastructure projects are now programmed via integrated network, and the federal government has consistently removed restrictions limiting the number of competitors in the infrastructure market. These measures promise, along with greater competition in concessions tenders and auctions, reduced costs and greater quality of services delivered.

Such efforts have rapidly shown positive results. In the logistics' sector, standouts in 2017 included auctions of airport and port concessions. Even more notable success came in the energy sector, with auctions for concessions in electric-power generation and transmission and oil and gas prospecting surpassing expectations.

8. Summary and Closing Considerations

The Brazilian government has significantly modified the present scenario through the adoption of measures to consolidate its active role in attracting private investment for development of infrastructure. Central to this effort are the creation of the Program for Investment Partnerships (PIP), increased incentives to competition in the infrastructure sector, improvement of the sector's financing mechanisms, and implementation of a regular schedule for granting concessions.

The launch of the PIP has shown notable results, supporting the country's return to sustainable development. Since the PIP's creation, 57 privatizations — of 145 anticipated, for 40% of the total — have been concluded, contributing substantively to the Brazilian economy with job creation linked to new investment.

Moreover, measures to increase competition in the infrastructure sector aim for delivery of improved services to the public. Foremost among these measures, is the most extensive opening of concessions to international participation (with increased transparency in the process, documentation made available in English, and

Enabling long-term planning and projections, the maintenance of a regular schedule for awarding concessions — put forward on a multi-year basis — encourages the entrance of new competitors into Brazil's domestic market

the establishment of a 100-day minimum interval between a tender for bids and the auction at which grants are awarded). Other provisions include reduction in the requirements for local content in the oil and gas sectors, and a new legal framework for the natural-gas sector under the Gas to Grow initiative.

Improvement to financing mechanisms for the infrastructure sector is another important step, with measures designed to encourage reduced participation by the National Bank for Economic and Social Development (BNDES), in favor of private financing, with the adoption of tax incentives for bond issues to fund priority infrastructure projects in all logistics and energy sectors.■

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Highway BR 153/GO-TO – from Aliança do Tocantins to Anápolis	Highway	Common Concession
Highway BR 364/RO - Porto Velho to Comodoro	Highway	Common Concession
Highway BR-040/MG/RJ – Juiz de Fora to Rio de Janeiro	Highway	Common Concession
Highway BR-101/SC – Paulo Lopes to São João do Sul	Highway	Common Concession
Highway BR-116/RJ – Além Paraíba to BR-040	Highway	Common Concession
Highway BR-116/RJ/SP (Dutra) – Rio de Janeiro to São Paulo	Highway	Common Concession
Highway BR-364/365/MG/GO – Uberlândia to Jataí	Highway	Common Concession
South Integration Highway – (BR-101/290/386/448/RS)	Highway	Common Concession
LPG terminals in Porto Miramar/PA – (BEL 05, BEL 06 and MIR 01)	Ports	Cession with Onus
Liquid Bulk Terminals in the Port of Belém/PA – (BEL 02A, BEL 02B, BEL 04, BEL 08 and BEL 09)	Ports	For Rent/Lease
Grain Terminals in Port of Paranaguá/PR – (PAR 07, PAR 08 and PAR XX)	Ports	For Rent/Lease
General Cargo Terminal at the Port of Itaquí/MA – (IQI 18)	Ports	For Rent/Lease
Wood Chip Terminal in the Port of Santana/AP – (MCP1)	Ports	For Rent/Lease
Cellulose Terminal at the Port of Paranaguá/PR – (PAR01)	Ports	For Rent/Lease
Vehicle Terminal in the Port of Paranaguá/PR –(PAR12)	Ports	For Rent/Lease
Liquid Bulk Terminals in the Port of Vitória/ES	Ports	For Rent/Lease
Liquid Bulk Terminals in the Port of Vila do Conde/PA – (VDC 12)	Ports	For Rent/Lease
Sale of Infraero share holdings	Miscellaneous	Privatization

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1. Creation of the Program for Investment Partnerships

The federal government created the Program for Investment Partnerships (PIP)¹ to encourage long-term collaborations between the public sector and private enterprise, targeting development of projects dedicated to services and implantation of and upgrades to infrastructure.

To further these aims, Law 13.334, enacted 13 September 2016, established two new administrative bodies: the PIP Council and Secretariat. The Council, an inter-ministerial body, evaluates and recommends to the presidency projects for implementation and integration of PIP; the Secretariat, operating under the executive branch, supports departments and agencies charged with the execution and regulation of the Program’s activities.

These bodies extend to sector-specific oversight agencies, which structure and coordinate their efforts to ensure effective investment policies with stability, legal protection, and reliable forecasting. By viewing and analyzing infrastructure projects in the context of a network, not solely on an individual basis, the PIP is aligning Brazil with international best-practices models for integrating infrastructure investment.

1 - “PPI” in Portuguese (Programa de Parcerias de Investimento)

2. Measures to Promote Competition in the Infrastructure Sector

With the combined aims of reduced costs, enhanced quality of services, and expanded competition in concession bidding, Brazil has been cutting back restrictions that tend to limit the number of competitors for contracts in the infrastructure market.

To this end, the federal government has prioritized the following actions:

- greater openness to international participation in the concessions market;
- reduced local-content requirements in the oil and gas sector;
- proposed new legal framework for the natural gas and power sectors;
- a regulatory framework for privatization in the electric-power sector.

GREATER OPENNESS TO INTERNATIONAL PARTICIPATION IN CONCESSIONS

Resolution 1/2016 of the PIP Board established overall directives and policies for the process of private-sector PIP contracting, for adoption and implementation by federal administrative entities.

Among these directives, most salient is the establishment of a minimum period of 100 days from a tender for bids to the close of bidding or auction date. Regulating this variable guarantees prospective participants the time necessary to take evaluative and preparatory actions requisite to presentation of a proposal, and has particular relevance for the international investor. Provision of minimum interval and deadline for documentation analysis and preparation of proposals serves domestic and foreign investors alike.

The new directives also established a minimum interval between bids on projects in the same sector. This provision encourages investors to pursue projects that best match their profiles and interests, while discouraging possible saturation of the market, overtaxing mechanisms for analysis or funding capacity of financial institutions.

To ensure comprehensive transparency in PIP contracting, documents, procedures and rules for competitions, proposals and auctions are disseminated, in English and Portuguese, via the official press and on the internet. The PIP Secretariat website centralizes this information, providing a single clearinghouse for information on the federal government’s infrastructure concessions².

REDUCED LOCAL-CONTENT REQUIREMENTS IN THE OIL AND GAS SECTOR

In 2017 the federal government simplified local-content (LC)³ policy applying to the oil and gas sector and reduced the minimum percentages required in concession and production-sharing contracting rounds to be conducted in biennium 2017-2018. The new rules aim at increasing efficiency and promoting competition.

Mainstays of the new policy make future auctions more attractive by allowing flexibility of demands and enabling adjustment of requirements in

7. Prospective: Future Infrastructure Investments

The following table presents an overview of anticipated infrastructure investment, updated as of 28 March 2018⁷.

PROJECT	SECTOR	MODEL
Airports in the Northeast, Midwest and Southeast (13 Airports)	Airports	Common Concession
Privatization – Brazilian National Mint	Miscellaneous	Privatization
Privatization – CASEMG	Miscellaneous	Privatization
Privatization – CEASAMINAS	Miscellaneous	Privatization
Privatization – Centrais Elétricas Brasileiras S/A – Eletrobrás	Miscellaneous	Privatization
Privatization – Companhia Docas do Espírito Santo – CODESA	Ports	Privatization
Mineral Rights of CPRM	Mining	Exploratory Concession Right
Power Distributors (CEAL, CEPISA, CERON, Eletroacre, Amazonas and Boa Vista)	Power Distribution	Privatization & Concession
EF-151 – SP/MG/GO/TO (North-South Railroad)	Railroad	Subconcession
EF-170 – MT/PA – Ferrogrão Railroad	Railroad	Common Concession
EF-334/BA – FIOL Railroad	Railroad	Subconcession
Loteria Instantânea – LOTEX (Lottery)	Miscellaneous	Common Concession
Oil & Gas – Marginal Accumulations (permanent offer)	Oil & Gas	Sharing Regime
Oil & Gas – Pre-Salt (4th Round)	Oil & Gas	Sharing Regime
PPP for Communications Network Management – Aeronautics Command - COMAER	Miscellaneous	Public-Private Partnership

⁷ - For further updates:
<http://www.avancarparcerias.gov.br/projetos1#/>
 English: <http://www.avancarparcerias.gov.br/projects#/>

THE OIL AND GAS SECTOR

In 2017, 43 offshore blocks were offered at auction, 37 in September and 6 in October.

ROUNDS CONDUCTED

ROUND	REGIME	AUCTION DATE	BLOCKS OFFERED	BLOCKS SOLD	AUCTION REVENUE BRL BN
14	Concession	09/27/2017	287	37	3.8
2	Production Sharing	10/27/2017	4	3	3.3
3	Production Sharing	10/27/2017	4	3	2.85
2017 TOTALS				43	9.95

In coming years, four additional rounds are anticipated, comprising two rounds under the concession regime (Rounds 15 and 16) and two under production-sharing (Production Sharing Rounds 4 and 5).

ROUNDS IN 2018

ROUND	REGIME	AUCTION DATE	BLOCKS OFFERED	AUCTION REVENUE BRL BN
15	Concession	29 March	68	8.01
4	Production Sharing	1st half 2018 (TBD)	5	4.65

The 15th Round of Exploratory Blocks was held on 29 March 2018, offering 68 blocks in the sedimentary basins of Ceará, Potiguar, Sergipe-Alagoas, Campos and Santos and in the basins of Parnaíba and Paraná. Out of this total, 22 blocks had proposals, generating a result of BRL 8 billion signature bonuses and more than BRL 1 billion in future investments. The auction recorded a premium payment of 621%. The objective of the Round was to expand basin reserves and decentralize exploration investments in the country, increasing the participation of small and medium-sized companies.

ROUNDS EXPECTED IN 2019

ROUND	REGIME	AUCTION DATE	BLOCKS OFFERED	AUCTION REVENUE BRL BN
16	Concession	2nd half 2019	TBD	TBD
5	Production Sharing	2nd half 2019	3	TBD

keeping with realities of the internal supply chain. With minimum percentages halved, and thus more feasible by domestic industry at competitive prices, forthcoming auctions can be expected to offer better opportunities in Brazil for companies engaged in oil and gas prospecting and production.

The new policy eliminates LC requirements for items and sub-items under a schedule specifying percentages for up to 96 items. Moreover, the LC requirement is no longer a scoring criterion in auctions, and fines imposed for failure to meet LC minimums were reduced.

The shift to a system enlisting global commitments also included the elimination of the existing waiver mechanism. This regulatory device, allowing for LC non-compliance in the case of: i) absence of a domestic supplier of specific goods or services,

and ii) excessive prices or deadlines relative to foreign equivalent, entailed an application process under the National Agency for Petroleum, Natural Gas and Biofuels (ANP)⁴, that tended to be overly protracted. Under the new system there is no need for these waivers; companies awarded concessions have leeway to meet local-content obligations via goods and services with which domestic providers are competitive.

Brazil's 14th pre-salt bidding round, conducted in September 2017 and offering 287 offshore blocks, yielded BRL 3.8 billion in signing bonuses with a premium of 1,556%.

The 2nd and 3rd pre-salt production-sharing bidding rounds, conducted in October 2017, offered 8 high-potential offshore blocks and yielded signing bonuses totaling BRL 6.15 billion.

AUCTION	PERCENTAGE OF RESERVES			SIGNING BONUS (BRL M)
	MINIMUM	OFFERED	PERCENTAGE (VARIATION)	
14^A BIDDING ROUND				
-	-	-	-	3,800
2nd PRODUCTION-SHARING BIDDING ROUND				
Sapinhoá Region	10.34%	80%	673.69%	200
North Carcará	22.08%	67.12%	203.99%	3,000
Soth Gato do Mato	11.53%	11.53%	0.00%	100
Southeast Tartaruga Verde	12.98%	-	-	-

2 - <<http://www.avancarparcerias.gov.br/>> / 3 - CL (conteúdo local) in Portuguese

6. Evolution of Investment in Energy Infrastructure

THE ELECTRIC-POWER SECTOR

In the area of power generation, the federal government awarded in 2017 four concessions for hydroelectric plants whose contracts had expired. The auctions denominated A-4 and A-6, conducted in December, showed good results in terms of discount. In the area of transmission, April 2017 saw the auction of 35 lots, of which 31 were sold,

and the granting of concessions covering some 7 thousand kilometers of transmission lines. On December 17, a further auction — in which all lots sold — granted concession covering 4.9 thousand kilometers of transmission lines. In the area of distribution, Resolution 20/2017 of the PIP Council approved privatization of six distributors controlled by Eletrobras, with auctions anticipated for the first half of 2018.

AUCTION ANEEL ⁶	TYPE	AUCTION DATE	RESULTS
Nº 05/2016	Transmission	04/2017	7,068 km of lines; average discount 36.47%; contracted investment BRL 12,7 bn
Nº 01/2017	Generation	11/2017	grant fee BRL 12.1 bn
A-4	Generation	12/2017	avg contract: 220 MW; avg price per MW: BRL 144.51; discount 54.65%
A-6	Generation	12/2017	avg contract 2,736.6 MW; avg price per MW: BRL 189.45; discount 38.7%
Nº 02/2017	Transmission	12/2017	4,919 km of lines, average discount 40.46%; contracted investment: BRL 8.7 bn
A-2	Generation	12/2017	avg contract 423 MW; avg price per MW: BRL 174.52; discount 9.6%
A-1	Generation	12/2017	avg contract 288 MW; avg price per MW: BRL 177.46 discount 18.2%

6 - National Agency for Electric Energy (Agência Nacional de Energia Elétrica)

AUCTION	PERCENTAGE OF RESERVES			SIGNING BONUS (BRL M)
	MINIMUM	OFFERED	PERCENTAGE (VARIATION)	
3rd PRODUCTION-SHARING BIDDING ROUND				
Peroba	13.89%	76.95%	454.00%	2,000
Upper West Cabo Frio	22.87%	22.87%	0.00%	350
Upper Central Cabo Frio	21.38%	75.86%	254.82%	500
Pau Brasil	14%	-	-	-

Source: Brasil Rounds (ANP)

The results of leasing and production-sharing auctions in 2017 demonstrate how reforms to the sector’s rules and tender protocols made these rounds more attractive to investors.

PROPOSALS FOR A LEGAL FRAMEWORK IN THE GAS AND ENERGY SECTORS

Historically, Brazil’s natural gas sector developed in a model of vertical integration, under mandatory control by the state oil company, Petrobras. In 2016, the government launched Gas to Grow, an initiative aiming to stimulate competition in the market and foster a favorable environment for multiple agents. The measure greatly benefitted from proposals put up for discussion throughout 2017 between the government and various entities operating in the sector.

Along with the initiative, this discussion yielded proposed legislation to define a new legal framework for the natural gas sector, Bill Proposal 6.407/2013, currently under consideration by Brazil’s congress. The proposal involves key points to promote investment and competition in the gas production chain, an effort made urgent by Petrobras’s strategic decision to

move toward divestment in this sector. Salient measures proposed include: a requirement for non-discriminatory access to essential facilities and infrastructure; a mechanism to enable the regulatory body to compel the sale of gas to the downstream market; new rules and governance structure for gas logistics and delivery, via authorization grants rather than concessions; restrictions on vertical integration.

REGULATORY FRAMEWORK FOR PRIVATIZATION IN THE ELECTRIC POWER SECTOR

Decree 9.192, issued 6 November 2017, regulates privatization conditions for companies distributing and transmitting electric power, under a newly promulgated concession contract. The regulation guarantees better legal security, and promotes such measures as appropriate association between transference of control and new concession contracts. The decree facilitates in particular the privatization of six Eletrobras distributors: Amazonas AS, Boa Vista, Eletroacre, CEPISA, CEAL and CERON. Most of these distributors, burdened by heavy debt and posting regular losses, have hovered at the lower end of supply-quality rankings by the sector’s regulator, the National

4 - Agência Nacional do Petróleo, Gás Natural e Biocombustíveis

Anticipated investments in the four airports, totaling approximately BRL 6.6 billion through the terms of concession, include capital for construction and expansion of passenger terminals, gate space, taxiways and runways.

In the port sector, concession renewals were signed in November 2016 for two facilities, the container terminal at Salvador (Tecon, Bahia) and the fertilizer terminal at Paranaguá (Fospar, Paraná), with anticipated investment, respectively, through the term of concession, of BRL 715 million and BRL 135.5 million. A new auction in 2017 awarded concessions for two terminals at Santarém (Pará), at a value of BRL

The latest auction conducted awarded a concession for the cereals port at Rio de Janeiro, at a value of BRL 1.8 million and anticipated investment through the term of concession of BRL 93.1 million

68.2 million and anticipated investment through the term of concession of BRL 29.8 million. All these port concessions have a term of 25 years. Also in the port sector it's worth noting the expectation of grant revenues via the leasing of new areas in the ports at Santana (Amapá), Itaqui (Maranhão) and Paranaguá (Paraná).

The rail-transport sector anticipates revenue of BRL 1.63 billion from the concession of the Ferrovia Norte-Sul (North-South Railroad). The Ferrogrão and Ferrovia de Integração Oeste-Leste (Integrated West-East Railroad) are also anticipated for concession, with minimum values yet to be determined.

Electric Energy Agency (ANEEL). A central aim of privatization is to allow for increased investment in concessions for distribution of electric power and attendant improvements in service.

Following the sale of these distributors, a further objective is to transfer Eletrobras (holding) to control by the private sector. Toward this purpose, on 19 January 2018, a bill was forwarded to the congress defining a privatization model of this transfer. Decree 9.351, issued 19 April 2018, includes Eletrobras in the National Programme of Privatization.

The proposed model seeks to promote equitable participation by active stakeholders in the company's governance via limits to shareholder control. A portion of income from this privatization will revert to the national energy development fund, lowering costs eventually to be passed on to consumers. The measure proposed further entails the allocation of significant financial resources for revitalization of the São Francisco River watershed, and proposes contractual changes curtailing government intervention in setting energy prices and defining other commercialization variables.

3. Finance Mechanisms for Infrastructure

Historically, infrastructure development and improvement in Brazil has been financed chiefly by the National Bank for Economic and Social Development (BNDES). Since 2011, measures have been adopted to encourage private financing and reduce the bank's involvement. A legislative measure to promote bond issues for infrastructure, Federal Law 12.431/2011, is as of 2016 scaling down BNDES participation.

Under this measure, tax incentives for bond issues to finance infrastructure projects designated as priorities by the federal government benefit all logistics and energy sectors. In response to the law's adoption, the volume of bond financing — heavily impacted by the 2014 and 2015 crisis — saw vigorous growth in 2017 (illustrated in Table 1).

With the approval of a new market-based benchmark interest rate for long-term financing, the TLP⁵, and revised BNDES operational policy, the expectation is that the bank will take a greater role in inducing and facilitating infrastructure financing than as primary source of finance.

Volume of Infrastructure Bonds Issued 2012 to 2017 (USD million)

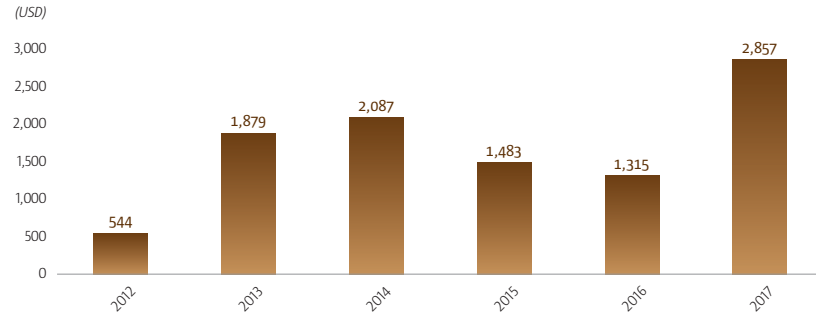


TABLE 1
Source: Anbima

The tax incentive additionally lowers costs for bond-issuing entities, and extends deadlines for issuance. (Table 2 compares real interest rates and the average term of infrastructure bonds, by sector).

Infrastructure Bonds: Real Interest Rate and Duration (by sector)*

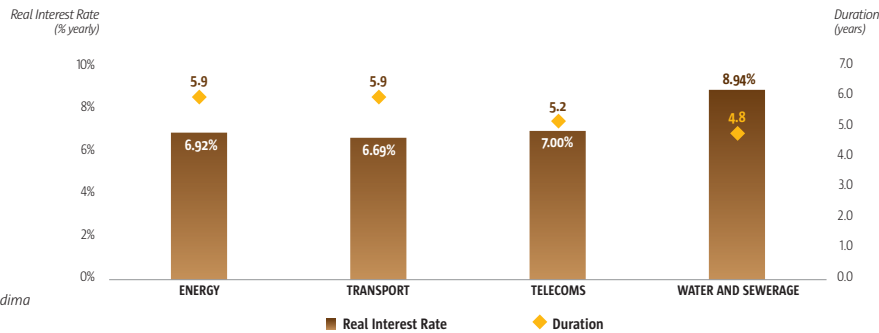


TABLE 2
Source: Andima

(*) Average real interest rate at issuance and duration at issuance for all inflation-linked infrastructure bond issued between 2012 and December 2017.

A further measure to increase investment in infrastructure and improve economic growth was Decree 8,874, 11 October 2016, facilitating the issuing of debentures to finance projects qualifying under the PIP.

The decree provides that all investment projects under the PIP – in infrastructure or intensive

economic production areas in research, development and innovation – and relating to concession, permission, leasing, authorization or public-private partnerships are eligible, subject to consideration by the appropriate ministry, for such bond financing. Additionally, the decree clarifies that costs incurred in securing contracts for priority infrastructure may qualify for such financing also.

5 - See easyBrasil booklet The New Brazilian Economic - Policies, Second Edition

4. Maintaining a Regular Concessions Schedule

Establishing and adhering to a regular schedule for concessions, with due official advance notification, enhances private entities' ability to participate with foresight and long-term planning, while encouraging entry into the national market by new competitors. In this regard, Brazil's oil and gas sector is the most advanced.

In 2017 the National Council on Energy Policy (CNPE) published a multi-year plan (CNPE Resolution 10/2017) for tenders for bids for exploration of offshore blocks, and for fields for oil and gas production for the 2018-2019 biennium. The proposal contemplates participation by operators active in the global sector, and anticipates periodic auctions of varying profiles so as to enhance projects' appeal to investors.

establishment of a fixed offering of offshore gas and oil blocks for exploration and production (CNPE Resolution 17/2017). This initiative entails renewed access to de-concessioned fields, and fields in the process of deconcessioneing, as well as such access to offshore blocks offered in prior rounds and not leased or since reverted to control by ANP. The inception of this continuing program and ANP's publication of protocols for these tenders, with technical and economic parameters, are anticipated for late April 2018.

An additional CNPE initiative of 2017 was the

5. Evolution of Investment in Logistics Infrastructure Concessions Schedule

PIP projects designated as priorities include private investment in rail transport, highways, ports and airports. In the interest of reducing public expenses and ensuring efficient management of infrastructure, PIP further considers and evaluates public assets as candidates for private concession; selected undertakings are then made a national priority. The agencies and enterprises involved are required to act so that necessary project structuring, approval and execution proceed with efficiency and cost-effectiveness.

In the course of these efforts, concessions have already been awarded for the airports serving Florianópolis (Santa Catarina), Fortaleza (Ceará), Porto Alegre (Rio Grande do Sul) and Salvador

(Bahia). Auctions granted these concessions to companies based in Germany, France and Switzerland, whose bids carried an average premium of 93%.