Brazil: São Paulo Roads

The State of São Paulo is often called “the locomotive of Brazil” because it’s responsible for almost one-third of the nation’s GDP. But the symbol of economic progress might be about to change: These days, it’s not a train but São Paulo’s roads that are driving the next phase of infrastructure investment in Brazil.

IFC’s Transaction Advisory team supported the Government of São Paulo to structure a large-scale road concessions program consisting of four roads with expected private investments upwards of $5 billion. Totaling 1,500km, the highways are critical transport arteries that connect the State of São Paulo’s industries with national and international markets.

The first two roads were auctioned in 2017 and the third road in 2018. The PPPs set records for concession fees to the government: bidders for the first two roads offered a combined $860 million in fees and $3 billion in investment; the winner bidder for the third road offered more than $270 million in concession fees and will invest about $180 million during the 30-year concession.

IFC’s advisory work was undertaken in partnership with the Brazilian National Development Bank (BNDES) and the Inter-American Development Bank (IDB). The three development banks work together in Brazil through the Brazil PSP Program to fund and foster innovative PPPs that meet Brazil’s critical economic and social infrastructure needs.
BACKGROUND
The State of São Paulo is the largest economic and industrial hub in the Southern Hemisphere and holds enormous influence in Brazil as a model for innovation in infrastructure development through private sector participation. The State of São Paulo has been structuring road PPPs since 1990s, however, the results from previously concessions were below expectations (deteriorated road conditions with little incentives for the concessionaire to make investments or improve services).

The project took place during a challenging time amid political instability and a significant economic crisis. This prompted São Paulo State officials to search for original ideas to attract a wide range of investors. The State Government asked IFC to introduce global best practices and attract international players through a competitive and transparent process. As a result, IFC helped design a new model for road concessions—bringing in massive private investment and expertise from international investors.

IFC’S ROLE
As the lead transaction advisor, IFC’s work included:
• Reviewing and verifying technical studies previously performed by the State Government;
• Leading additional technical, financial and international legal due diligences, encompassing all key aspects of the project;
• Recommending a new risk matrix based upon extensive market sounding;
• Introducing contractual provisions to strengthen project bankability features;
• Supporting market consultations with potential sponsors and lenders, which were a key factor as the deteriorated economic and political environment could have limited the attractiveness of the transaction.

TRANSACTION STRUCTURE
The program entails a 30-year toll road contract for each of the four brownfield roads to design, finance, build/expand, operate, and maintain the roads.

The State of São Paulo and IFC—in partnership with BNDES and IDB through the Brazil PSP Program—implemented a programmatic approach by introducing a set of innovations to the country’s private participation implementation framework across all of the road projects, such as more detailed early termination provisions, a FX protection mechanism based on the project’s cash flow generation, three-party direct agreements which improve lenders’ rights regarding the concession performance, technological improvements that benefit users of the roads.

BIDDING
To date, three of the four roads have been bid, with two reaching commercial close and one in the award stage (São Paulo North Beltway).

1. The ‘São Paulo Midwest Roads’ was awarded to Patria-Blackstone in March 2017 and includes 570km in extensions, linking some of the most economically active cities in São Paulo. The winning bidder offered a US $410 million concession fee, which was a 130% premium over the minimum set upfront. It also entails private investments of approximately US $1.2 billion.

2. The ‘São Paulo Shoes Industry Road’ was awarded to Arteris, a JV between Abertis and Brookfield, in April 2017. The road includes 747km in extensions, connecting important cities in the countryside. Arteris offered a US $450 million concession fee, a 438% premium over the minimum, and private investments of approximately US $1.5 billion.

3. The third road, the “North Beltway”, is the final part of São Paulo Beltway (the South, East, and West sections are in operation). This concession was awarded to Ecorodovias, a subsidiary of Italian Gávio Group. With the main goal of reducing heavy traffic, this project has been structured primarily as a public works project. The concession will entail minor remaining capex investments and full operation and maintenance being transferred to the concessionaire. Ecorodovias bid more than US $270 million in concession fees for the North Beltway.

EXPECTED POST-TENDER RESULTS.
• Huge commuter and cargo traffic flows will benefit from improved service and reduced travel times.
• Estimated $5 billion mobilized in private sector investments throughout the life of the concessions.
• Introduced new market entrants and financing schemes for infrastructure projects, with the first fully non-recourse financing structures coming to fruition;
• Long-term investments incentivized to improve services for drivers and maintain public roads.