Overview of Global Infrastructure Investment — Estimating Needs, Investment-Friendliness & Efficient Achievement

(From the Report "*Third Global Infrastructure Investment Index 2016, Bridging the Investment Gap*" Provided by Arcadis and Discussed in the World Economic Forum)

By *Japan SPOTLIGHT*

Introduction

The need for infrastructure in the world is today growing significantly, not only because of the increasing need for economic development among emerging economies and most developing nations but also because rapid urbanization requires better mobility for citizens and climate change is being taken evermore seriously, with COP21 seeing countries committing to lowering greenhouse emissions. As a result, the urgency for new and improved sustainable infrastructure in countries is increasing drastically. However, even though the appetite to invest in infrastructure is self-evident, whether it can be provided smoothly and efficiently is another question, as important infrastructure projects are continually delayed by lack of investment.

In 2016, Arcadis, a consultancy company, issued its *"Third Global Infrastructure Investment Index 2016"* report and provided this to the World Economic Forum. The report provides answers to such questions as how great will be the current and future global investment gap between supply and demand for infrastructure, which markets in the world are most attractive to investors and how efficiently this investment gap can be filled.

According to Rob Mooren, Director Global Solutions at Arcadis, there is a growing global awareness that private investment in infrastructure can deliver much-needed projects more cost effectively, and crucially quicker, than government-sponsored schemes. In addition, tighter government spending in core markets means that project sponsors are increasingly turning to private finance to bridge the investment gap. The infrastructure market is truly global. Contractors and operators alike are looking for new market frontiers, with investors searching further afield for assets to invest in. However, structuring the deals to be "bankable" remains a challenge for many organizations. Here we introduce the essence of the report.

Estimates of the Global Investment Gap for Infrastructure

Arcadis estimates that the current global investment gap for infrastructure is $1 trillion per annum against an annual global investment demand of $3.7 trillion. Between now and 2030 the world is facing a vast $14 trillion shortfall.

A greater focus is placed on climate change and global urbanization, with increasing population density. This is further driving infrastructure demand, meaning that sustainably building and effectively operating the kind of infrastructure that boosts economic growth is more vital than ever before. Better transit, efficient freight networks, reduction of congestion, improved connectivity, greater capacity, better communications, more efficient water systems, clean energy, stable power supplies and growing aviation assets are vital tools in creating stronger, better connected economies.

For many reasons there remains a shortage of projects that are structured in a way that gives investors the long-term certainty that they need, and there is a growing desire among the public sector to tackle this. The investment gap can be closed by structuring projects in a way that satisfies all stakeholders, from governments to the general public and investors. To lower risks private investors pay increasingly more attention to benchmark projects on sustainability. For existing portfolios they look to improve their returns by optimizing the operations of their existing assets through asset management. Contractors are focusing on ways to improve their processes and control their costs better, for example by implementing new technologies or by restructuring their supply chain.

Most Attractive Markets for Investors

The findings of the *"Third Global Infrastructure Investment Index 2016"* highlight that the most attractive markets for investors remain those with the strongest growth potential, most secure business environments, well-established legislative and regulatory systems and stable political environments. As a result, markets such as Singapore, Canada, Qatar, the UAE, Norway, Sweden, Malaysia, the United Kingdom, the United States and the Netherlands remain the top 10 locations in the world in which to invest in infrastructure *(Chart)*.

In general Asian countries at the top of the index like Singapore and

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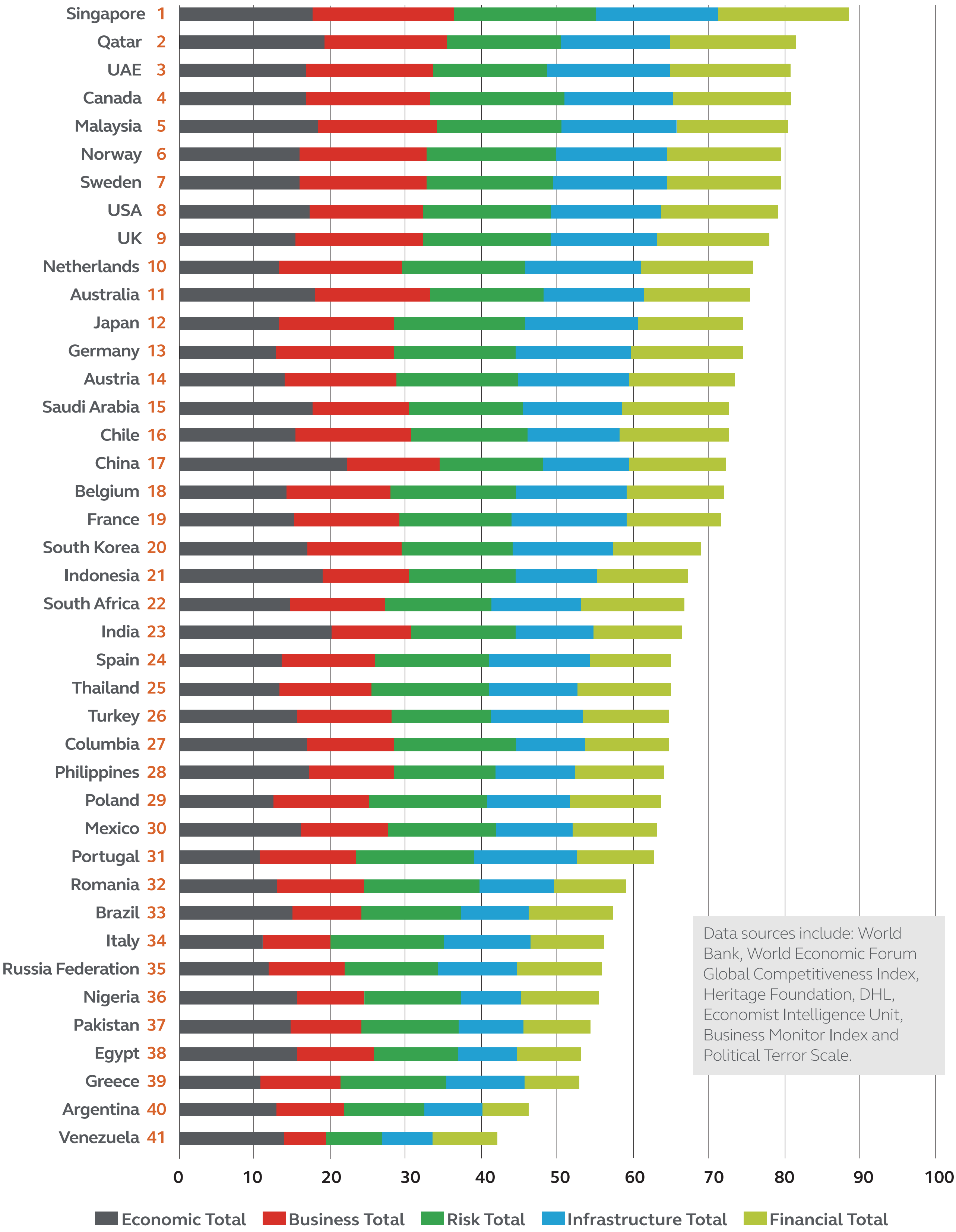
Global Infrastructure Investment Index 2016



Data sources include: World Bank, World Economic Forum Global Competitiveness Index, Heritage Foundation, DHL, Economist Intelligence Unit, Business Monitor Index and Political Terror Scale.

Source: Third Global Infrastructure Investment Index 2016 (by Arcadis)

Malaysia have set out long-term plans for infrastructure. However, as you go further down the index it becomes a little more haphazard and less transparent. This makes these markets less attractive to investors who don't have all the facts to hand to enable them to make decisions. At the bottom of the index are a number of countries that are struggling with poor economic performance, political instability and high-risk business environments.

The index ranks countries according to their relative attraction to infrastructure investors in the long run (5+ years). This assessment is based on national statistics and open source data focused on anticipated demand for infrastructure investment, ease of doing business and comparable levels of investment risk. A high weighting is given to indicators of dynamism in a national economy. The ranking uses 24 indicators across five categories: 1) Economic environment (relative strength of demand for infrastructure investment, based on indicators such as GDP growth, population growth, etc.), 2) Business environment (how attractive a country is for investment, based on indicators such as ease of doing business and freedom from corruption), 3) Risk (how much risk a country poses to the security of investment returns, based on indicators such as the political terror scale, strength of investor protection etc.), 4) Infrastructure (relative scale of infrastructure opportunity and capacity to deliver, based on indicators such as overall quality of infrastructure, local supplier quality, etc.), and 5) Financial environment (degree of support to infrastructure investment provided through the financial environment, based on indicators such as extent and effect of taxation, availability of financial services, etc.).

The index measures the long-term attractiveness of countries as destinations for infrastructure investment. However, short-term fluctuations in commodity prices and political stability, for example, could potentially introduce short-term turbulence affecting investment decisions related to specific countries. In the 2016 index, additional indicators for strength of currency, credit rating, political stability and dependence on commodity earnings are used to highlight the degree to which a country has been exposed to short-term economic turbulence. The author's view is that these factors could potentially have a material effect on investment decisions over the next two or three years, and as a result are an important aspect of a country's overall ranking.

For a better overall picture of the potential to invest in a country's infrastructure, the short- to medium-term risks which act as a barrier to investment were also considered in the report. These barriers include currency devaluations, exposure to weak commodity prices, loss of credit worthiness and increased insecurity, as well as the global slowdown driven by China's deceleration in growth.

How to Drive Infrastructure Projects Efficiently & Effectively

Key to the success of any infrastructure project is a strong supply chain, and the world's leading concessionaires and contractors have long understood that by getting this right, risk is low and investors more forthcoming. Generating long-term income through the range of public-private partnership (PPP) structures, which requires a significant early capital investment from contracting teams, is a highly attractive proposition for firms. So it is therefore not surprising that contractors today are using a number of strategies to enter into emerging high potential markets, deemed to have a big future in PPP/PFI (private finance initiative) or Design, Build, Finance, Operate and Maintain (DBFOM) projects and major project investment.

Whatever the market, world scale concessionaires and contractors are carefully weighing up the risks and the opportunities before investing in new territories and bringing in their investors. For countries with huge infrastructure backlogs this is a very welcome development, but to succeed these markets must work on strengthening their institutional readiness and ensure that government agencies are prepared to place the risk with the parties most able to manage it.

Overall there is an urgent need for dialogue between the public and private sectors to close the funding gap, and unlock the huge community and business benefits from infrastructure investment. Political leaders need to scrutinize their preferred rules of engagement with the private sector, and then set about creating the best possible conditions to deliver the targeted investment. As there are investors covering most risk profiles and infrastructure asset classes, the opportunity for improved infrastructure is huge, both in the short and long term. Contractors and concessionaires must also embrace new technology and understand local market nuances to achieve success. Only then can the best social, economic and environmental outcomes be achieved for all parties. JS

Formatted by Naoyuki Haraoka, executive managing director and editor-in-chief of *Japan SPOTLIGHT*.