Accelerating Infrastructure Investment in G20 countries

Alok Sheel

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Overview

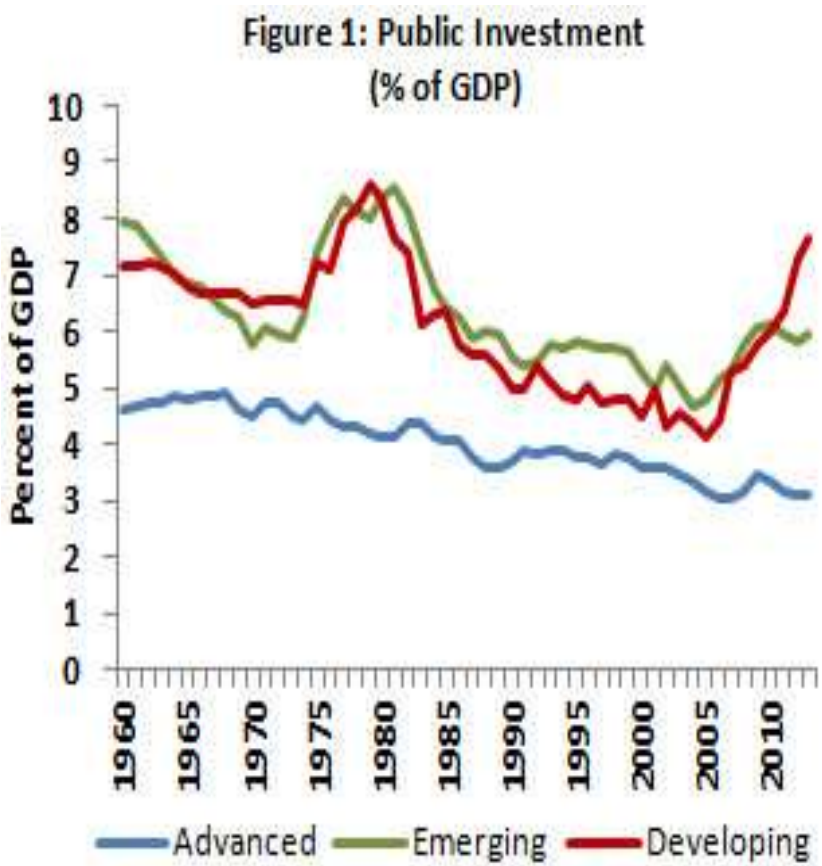
- Stylized facts on Infrastructure
- Infrastructure across G 20 Summits
- Assessing G 20 interventions
- Way Forward

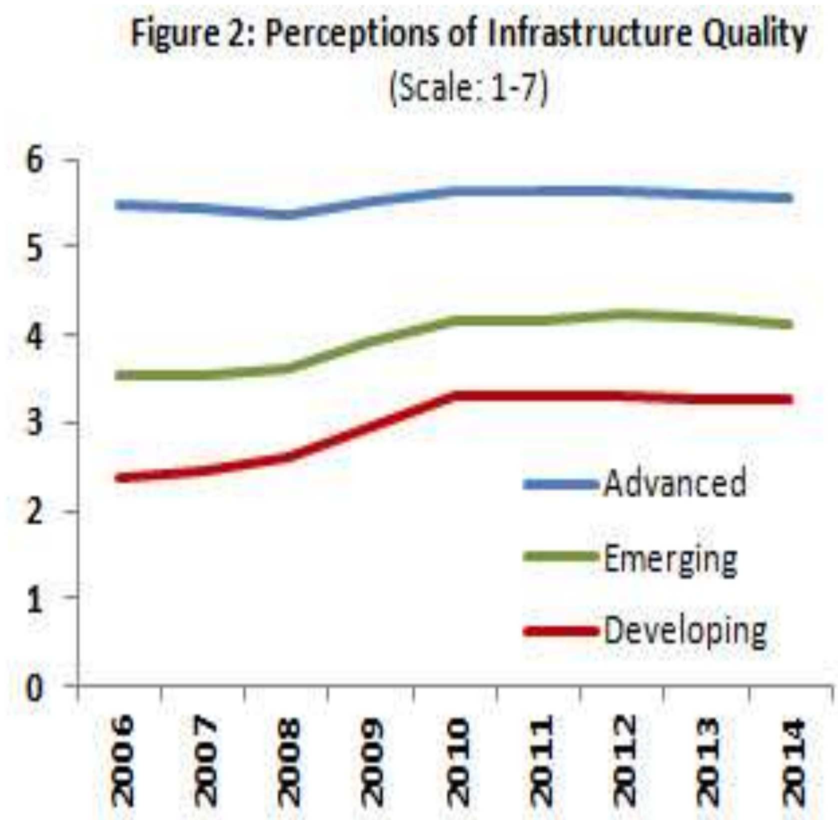
1. STYLIZED FACTS ON INFRASTRUCTURE

Infrastructure: *Characteristics*

- Has capacity to improve productivity and trend growth in a sustainable manner: ***borrowing for infrastructure pays for itself*** through higher revenues.
- ***Building ahead of demand justified*** on account of multiplier, productivity and crowding-in effects of infrastructure investment. Chinese proverb: if you want to go anywhere you need to build a road first.
- ***Large , lumpy investments***
- ***Need time*** to develop a shelf of projects and long gestation period: Not a natural countercyclical policy tool – difficult entry and exit, unlike automatic stabilizers.
- ***Iron law of infrastructure***: 'over budget, over time, all the time' -- Even in advanced economies High Risks – Not a natural area for private investment
- ***Special role for the State***: WB study – less than 15% investment in Emerging Markets has come from the private sector, mostly in power, telecom and toll roads.
- Public investment ***crowds in, rather than crowds out***, private investment.
- By indirectly boosting incomes (through job creation) might address Ricardian Equivalence and ***improve fiscal multipliers*** in recessions.

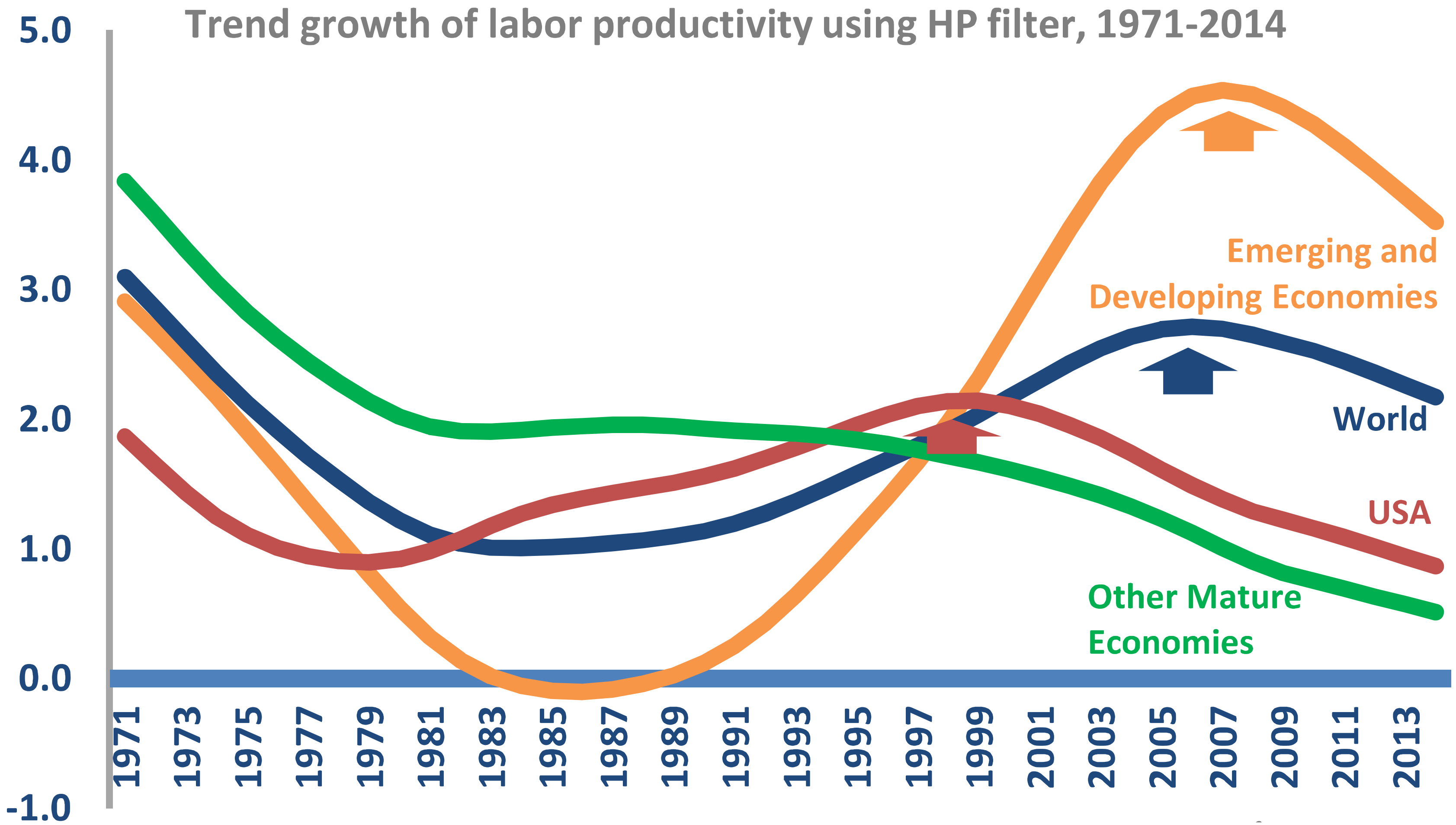
Infrastructure: *Trends*





Source: **IMF**

Productivity Trends



Source: **Conference Board**

Infrastructure: *Investment Gaps*

- Developing countries ***need large investments*** in new infrastructure, especially urban. Advanced countries need to upgrade existing infrastructure.
- In 2009, the ***ADB put Asia's infrastructure needs at $8 trillion over the present decade***. In 2011, the WB estimated India's decadal infrastructural gap at $ 1.1 – 1.7 trillion. *This excludes soft infrastructure such as health and Education.*
- ***Numbers put out by the Australian Presidency for the Brisbane Summit*** in 2014 on global infrastructural gaps based on OECD and World Bank data:
  - **OECD estimates** US$70 trillion is needed up to 2030 to address the growing infrastructure gap - and build the roads, ports, power and communications infrastructure.
  - The **B20 Infrastructure and Investment Task Force** estimated in July 2014 that, with current policies, only around $45 trillion of this investment may be realised.
  - The **World Bank estimates** that an additional US$1-1.5 trillion each year will be required through 2020 to meet growth targets in emerging and developing economies.

Infrastructure: *Financing Challenge*

- Historical experience and current trends indicate that infrastructure investment the ***most challenging***. Cross-border infrastructure even more so.
- ***Advanced economy budgets in disarray***: foreign aid could shrink in real terms.
- ***IFIs scale of financing*** pales in relation to EME infrastructure needs.
- Most of accumulated ***global savings with EME Central Banks*** rather than with governments.
- Bulk of the investment would have to be ***publicly funded/guaranteed*** in the best of circumstances.
- ***Risk thresholds for private investment need to be lowered***, and comfort levels raised. Even so, private investment likely to be limited, and may need to be directly/indirectly guaranteed by governments.
- ***EMEs have two options/models:***
  - ***greater sophistication in financial intermediation*** and moving away from financial repression to attract long term private capital.
  - ***Redirect private savings to the State*** through financial repression. Case of China.

2. INFRASTRUCTURE ACROSS G 20 SUMMITS

I Washington DC: November 2008

- Set the tone: Role for Infrastructure in crisis management ***limited to developing countries***.
- Help EMDEs gain access to finance in current difficult financial conditions by encouraging the World Bank and other MDBs to use their full capacity in support of their development agenda.
- Welcomed the introduction of new facilities by the World Bank in the areas of infrastructure and trade finance and resolved to take steps to ensure that the World Bank and other MDBs have sufficient resources to continue playing their role in overcoming the crisis.

II London: April 2009

- ***MDB lending increased*** by 100 billion to fill in the gap created by withdrawal of private capital and to support countercyclical spending, inter alia, in infrastructure
- IMF’s resources on the other hand were enhanced by 750 billion.

III Pittsburgh: September 2009

- ***Framework*** for Strong Sustainable and Balanced growth launched: ***No special role for infrastructure investment.***
- The World Bank, working with the regional development banks and other international organizations, should strengthen support for private-sector led growth and, *inter alia*, infrastructure to enhance economic growth.
- Resources of MDBs to be enhanced.

IV Toronto: June 2010

- ***Took credit for fulfilling the Pittsburgh Summit commitment*** on enhancing MDB resources by $350 billion (85%) through capital increases for MDBs (ADB, AfDB, IADB, IBRD, IFC & EBRD) to enable them to nearly double their lending, from $37 billion per year to $71 billion per year.
  - World Bank: 30% capital increase by $ 85.5 billion, from about $ 287 to $ 375 billion. Lending increased from $ 12.1 to 15 billion per year.
  - ADB: 200% capital increase from $ 55 to $ 165 billion.
  - Mostly (over 90%) callable capital.

V Seoul: November 2010

- ***Infrastructure the first pillar of the new 'development agenda'*** injected by Korea in the G 20 process.
- The target remained developing countries, especially low income.
- High Level Panel on infrastructure formed.
- Indian PM linked infrastructure investment to to global demand rebalancing, a priority area for the G20.

Indian PM at the Plenary Session of the Seoul Summit, November 12, 2010

- ***…… there is a strong case for supporting long term flows to (developing) countries to stimulus investment, especially in infrastructure …. which would inject much needed demand into the global economy. Multilateral Development Banks have an important role to play in this process through recycling of global savings…. Recycling surplus savings into investment in developing countries will not only address the immediate demand imbalance, it will also help to address developmental imbalances. In other words, we should leverage imbalances of one kind to redress imbalances of the other kind. The G20 would convey a powerful signal to markets if we commit ourselves to a second stage MAP process aimed at coordinating policies in these areas.***

Recycling of External Surpluses

- ***What does history tell us***: Imbalances destabilize financial systems when they go into non-productive channels.
  - The recycling of petrodollars for consumption in Latin America in the 1970s should have served as a warning: The debt crisis and lost decade.
  - Japanese recycling of surpluses into real estate and stocks led to a financial crisis from which it is still recovering
  - Chinese Surpluses since its entry into the WTO recycled to finance a leveraged consumption boom in the US a driver of the Global Financial Crisis.

VI Cannes: November 2011

- ***High Level Panel on Infrastructure*** submitted its Report:
  - 11 mega, transformative projects listed in the AP.
  - Underscored the role of MDBs alongside private investment in their Action Plan.
  - No additional funding raised to implement the Action Plan.
  - Action Plan fails to gain traction.

VII Los Cabos: June 2012

- ***Major shift in G 20 approach to infrastructure***: incorporated in the Framework as a policy tool to rebalance and boost demand and growth in both developing and developed countries
- The Los Cabos Action Plan identified investment in infrastructure to increase productivity and living standards in the medium term by addressing bottlenecks in Argentina, Australia, Brazil, India, Indonesia, Mexico, Saudi Arabia, South Africa and UK .

VIII St Petersburg: September 2013

- ***Infrastructure investment seen as part of country growth strategies*** to lift growth and create jobs.
- Endorsed the ***G20/OECD High-Level Principles*** of Long-Term Investment Financing by Institutional Investors and asked Finance Ministers and Central Bank Governors to identify approaches to their implementation by the next Summit.
- Finance Ministers tasked to identify measures to develop domestic capital markets and improve the intermediation of global savings for productive long-term investments, including in infrastructure, by the next Summit.
- MDBs asked to develop new approaches to optimize use of existing resources, including through leveraging private capital, to strengthen their lending capacity.

IX Brisbane: November 2014

- Recognized that members committed to a wide range of structural reform measures in previous Action Plans to boost growth, including in infrastructure, but implementation an issue.
- ***Brisbane Action Plan*** set a goal of lifting G20 GDP by more than 2 per cent above the trajectory in the October 2013 IMF *World Economic Outlook* baseline by 2018 by including, inter alia, ***country specific commitments on public and private investment in infrastructure*** as a priority area to support near-term demand and supply capacity in the medium-term ***and promote global rebalancing.***

IX Brisbane ....

- ***New Global Infrastructure Initiative based on the high level principles***:
  - A new **Infrastructure and Investment Working Group** (co-chaired by Germany, Indonesia and Australia) ***.***
  - A **Global Infrastructure Hub** headquartered in Sydney with a four year mandate, funded by the Australian Presidency. A knowledge sharing, networking platform between governments, private sector, development banks and other IOs. To attract private sector capital by matching potential investors with projects, addressing data gaps, improving information on project pipelines. Mobilizing long-term financing by institutional investors including through the G20/OECD effective approaches and working with MDBs (especially with World Bank Group's new Global Infrastructure Facility to attract private investment in developing countries) and NDBs to use their balance sheets for additional lending.

(*Towards*) **Antalya:** November 2015

- ***3 meetings of the IIWG held so far under the Turkish*** Presidency. In Ankara, Singapore and Berlin.
- **FMCBG at Wash DC, April 2015 reaffirmed commitment to boost infrastructure investment as an important driver of growth** and to develop concrete country-specific investment strategies including through policies to improve the investment ecosystem, foster efficient infrastructure investment and support sound long term financing opportunities by facilitating development of appropriate financial vehicles including asset-based financing structures. Welcomed the progress made in establishing the Global Infrastructure Hub and looked forward to the delivery of an initial **business plan to the next meeting in September 2015**.

G 20's Current Stance on Infrastructure

- ***In advanced economies fiscal policy*** consolidation should be paced to enhance infrastructure investment to bridge economic output gaps and upgrade existing infrastructure. Attract private investment.
- ***In emerging economies investing in infrastructure is crucial to ease supply bottlenecks***. These economies can use the crude oil price fall to shore up their public finances and use the money to invest in infrastructure projects, including PPPs.

3. ASSESSING G 20 INTERVENTIONS IN INFRASTRUCTURE

Assessment I: **Shift in Stance**

- ***Initially G 20 saw Infrastructure Investment relevant only for developing economies*** that had large supply gaps and faced a funding constraint as a result of the financial crisis.
- ***Shift in stance from the Seventh Summit*** at Los Cabos, where it was ***mainstreamed through the Framework*** as a growth enhancing and demand rebalancing policy tool in advanced economies as well.
- Possible explanation for shift: The decline in growth no longer seen as simply cyclical but structural

Assessment II: **Rebalancing?**

- ***Indian PM pointed to the role of infrastructure in demand rebalancing*** at Seoul: the latent demand for infrastructure in developing countries could countervail the decline in demand in advanced economies.
- ***Second rebalancing hinted at in the Brisbane declaration?***: expenditure switch from consumption to investment in AEs to increase demand and growth in a sustainable manner.

Assessment III: **Limited stimulus role**

- G 20 appears to ***rely more on private investment in infrastructure in AEs*** than what historical experience and stylized facts about the infrastructure sector warrant.
- Possible reasons: ***Ideological and parlous state of public finances***
- ***In hindsight, a greater portion of the stimulus should have been spent on infrastructure*** investment than on bailing out the financial sector, trying to boost consumption directly through tax breaks (subject to Ricardian Equivalence) and letting money creation (QE) inflate asset prices. Precedent: President Roosevelt's 'New Deal' during the Great Depression in the 1930s.
- ***China, the G 20 country that had a large infrastructure fuelled stimulus***, needed to expand consumption expenditure and not investment to rebalance its economy to adjust to external demand shock. Initial benefits, long-term problems?

Assessment IV: **U of Toronto**

- University of Toronto has been conducting independent third party studies on compliance of G 20 Summit commitment.
- In general it has found compliance declining after peaking at 79% after Los Cabos.
- The interim compliance 6 months after Brisbane is 62% (63% at the same time after St Petersburg)
- Has nevertheless ***found 93% compliance on Brisbane's GII*** with all countries except France, Italy and South Africa taking *steps to mobilize* both private and public investment in infrastructure.

Assessment V: **AIIG or AIIB?**

- In supporting infrastructure investment in developing countries, the ***G 20 did not put its money where its mouth was:*** MDB resources only enhanced marginally, even as IMF resources were increased five times. Except China, no major public funded infrastructure push in AEs.
- Not surprising that ***China is stealing a march on the G 20*** through its AIIB and Silk Road initiatives, leveraging its large stock of savings,: putting money where its mouth is, whatever may its the strategic consideration.
- However ADB meets 2 per cent of Asian infrastructure needs, and the AIIB will only match this at best. ***Most of the resources have to be domestic.***

4. WAY FORWARD

Way Forward I

- Need to ***rethink role of infrastructure as a countercyclical tool*** alongside automatic stabilizers.
  - **mainstreamed as a countercyclical policy tool in developing countries**, through stepping up expenditure, although they need to invest in infrastructure even in non crisis situations because of large gaps.
  - **In advanced economies infrastructure investment should be seen as a structural policy tool** as the current decline in growth is not simply cyclical. Time for a new Marshal Plan and/or New Deal? Red flag: Pork barrel politics.

Way Forward II

- ***Greater role for public investment in infrastructure*** to crowd in private investment.
- **Public expenditure switching** from consumption to investment as most of the funding would need to be domestic.
- Using the ***fiscal space created by lower oil prices*** for stepping up infrastructure investment.

Way Forward III

- ***External surpluses and excess liquidity need to be diverted*** to infrastructure investment.
- ***MDBs need to be adequately resourced*** to enable them to intermediate global savings on a larger scale -- incomplete G 20 agenda.
- MDB micromanagement to be reduced so that asset expansion does not lead to runaway staff expansion: ***shift from project finance to budget support***.
- ***Improved incentives and climate for long-term savings and investment*** -- G20/OECD High Level Principles – to attract more private investment.

THANK YOU FOR THE PATIENT HEARING