DIALOGUE CAPITAL

International Infrastructure Dialogue 28th to 29th June 2017 in Frankfurt

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International Infrastructure Dialogue 2017 – Frankfurt

Day 1, 28th June
14:15 – 15:15pm, Salon 1
Road Infrastructure in Germany and abroad – Financing, Hurdles & Solutions?
Strassen-Infrastruktur in Deutschland und global – Finanzierungen, Huerden und Loesungen?
Summary

- The greater public should have more positive attitude towards PPP in Germany. It is a good lesson learned from other countries in the EU regarding the infrastructure financial solutions.
- Different noises still exist among Germany for PPP. Although, supported by the federal government, the fear of private investors is not lessened.
- The Netherlands are very approachable in turns of accepting PPP in EU, and the emerging markets in the world have more consensus and respect towards PPP.
- The public funding is sufficient to support German infrastructure projects, but the lack of knowledge and management in the public sector could pose a question mark on how to get the deal into the markets. Relying unilaterally too much on just a few giant players in the market, for example, DB, is not positive to PPP.

Day 1, 28th June
14:15 – 15:15pm, Salon 2
New technologies & Smart cities – Investment potential, threat or reaching for the stars?
Summary

- There is no standardized commonly accepted definition for 'smart city'. Generally, a smart city is an innovative city that uses new technologies to improve quality of life, efficiency of urban operation, services and competitiveness. For developing countries, smart infrastructure applications provide a way for cities to achieve leapfrogging in technology. In developed countries, smart city applications may focus more on facilitating the optimal use of existing infrastructure resources and monitoring the operations of such legacy resources.
- Smart infrastructure provides the foundation for all of the key themes related to a smart city, including smart buildings, smart mobility, smart energy, smart water, smart waste management, smart health and smart digital infrastructure. A city is made up of different infrastructure verticals from a system of systems, thus smart cities need an integrated approach in order to harness the full potential of smart infrastructure.
- Smart infrastructure projects require pooling public and private resources through creative financing and public-private partnerships models. If efficiency gains via smart city applications can be measured through appropriate smart technologies and monetized through business models, then a part of smart infrastructure investment costs may be recovered through such gains. Another possibility for raising revenue is to establish

customized user fees or congestion charges during peak hours in certain public spaces or city centres, enabled through sensor networks and cameras, which may help to reduce traffic congestion and promote safe pedestrian traffic.

14:15 – 15:15pm, Salon 3

Infrastructure debt investments – how to generate good returns?

Summary:

The discussion of this salon is expanded from three intrinsic questions:

1)What is the good return?

2) How can we achieve good return?

3) How can we keep the debt investment flexibility and balance?

The financial modelling is not always the underlying basis for infrastructure investment, and governance is also prominent. Regarding the definition of the good return, it actually depends on the benchmark or reference point of the assets, the balance of risk adjustment and economic return.

To achieve a good return, we need to realise that the intrinsic feature of the market is that the market is evolving fast. The governance of fund and good portfolio management are the basis of good return. For example, the balance of green and brown field assets. At this stage, there is excessive capital pouring into the field of infrastructure investment, and the challenge is to choose assets, align the objectives of different stakeholders and keep the consistency of fund management. Meanwhile, there are some tools that we can use to enhance credit and mitigate the sovereign risks, such as CDS (credit default swap). The selection of tools also depends on the geography, political framework and economic-social context.

The debt flexibility and balance rely on three fundamental factors: good strategy, timing and stability of cash flow. Good strategy requires global investment spectrum to diversify the assets in both emerging and mature markets. The period of investment, the entering and exit time point are the core considerations for timing. Risk management and preliminary financial planning is the key to guaranteeing the stability of cash flow, in particular on the balance sheet.

15:45 – 16:45pm, Salon 1

What is infrastructure – (Re-) Defining the asset class?

Summary

- Infrastructure defined as a public good which could be public/private owned. It serves anyone in the country. but organized publicly through decision making.
- It could also be referred as the surroundings which makes your real-estate asset valuable.
- The essential associated services are the continuously growing features in the infrastructures asset class. It is connecting and supporting the economic community.
- From the concession side, although it is difficult to define; it was associated the finance purposes before, but now, it is a continuously growing feature in the digital economy. The

associated services planning, gets itself a larger share of the economy.

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15:45 – 16:45pm, Salon 2

PPP's in mature & emerging markets – How to best minimize risks?

Summary

- The risks associated with infrastructure PPPs generally arise from the nature of the underlying infrastructure assets and the environment in which infrastructure operates. The magnitude of a risk for infrastructure PPPs varies, depending on the country (and its underlying investment climate), sector (and its institutional environment) and project (and its complexity).
- The definition of 'emerging markets' in global infrastructure industry is different from that in the context of economic development, given the complexity of infrastructure PPPs markets in different countries. Emerging markets have historically been the domain of infrastructure investors willing to take on the high risk/return profile. The Philippines, for instance, is actively pursuing an anti-corruption agenda and has established a dedicated PPP unit to engage private finance models to fast-track national infrastructure development. China has a particularly dynamic domestic market – population growth accompanied by increases in urbanisation and the rise of the middle class, should result in significant opportunity for private investors – however, concerns around government transparency and attitudes to foreign investment, hamper progress to some extent. Main risks for PPPs in emerging markets are: corruption risk, country risk, currency risk, regulatory risk and project risk.
- The status of infrastructure PPPs in mature markets varies from country to country. Canada is seen as the standard-bearer for good practice, with dedicated provincial infrastructure units and a strong project pipeline. Its immediate neighbour – the US is now emerging as the next major global infrastructure PPP player. Collectively, North America is increasingly becoming one of the most attractive PPP markets globally. By comparison, Europe's infrastructure project pipeline – and PPPs in particular – may have peaked following a decade of strong investment. Despite a pressing need for maintenance and new infrastructure builds, weak economic growth and falling productivity restrict development.
- Emerging markets face obstacles in mobilising private investment to finance their infrastructure needs. Hence, efforts are being made to provide financial instruments such as investment funds, blending and risk mitigation instruments to attract private investors who might otherwise be deterred from entering these markets. In addition, multilateral development banks (MDBs) can play an important role in facilitating investments for an institutional investor in emerging markets. They can attract capital from the private sector by playing a part in syndication or other co-financing mechanisms, or issue risk guarantees and project insurance against risks such as civil disturbance or government non-payment.

15:45 – 16:45pm, Salon 3

New mechanisms for Infrastructure investors – how to make projects bankable, speed up processes and create new markets?

Infrastructure projects are considered bankable if lenders are willing to finance it. Bankability is perceived and managed differently among stakeholders. The various players in this market seem

to agree on the importance of bankability, and the term started to be used widely. The bankability of projects depends on the risk profile of different investors.

The risks consist of:
Construction and Completion Risk
Operating Risks
Demand Risk
Force Majeure and Change in Law
Political and Regulatory Risk and Expropriation and Nationalisation Risk
Environmental Risk
Social Risk
Tenor and Refinancing Risk
Currency Exchange Risk
Interest Rate Risk

In practice, IFC project financing department is promoting bankability test for projects so as allow the following process can meet the bankability test. Besides, the guarantee of the government matters regarding bankability as it can mitigate some of the risks above. If a project faces bankability issues, the authority may be tempted to consider providing guarantees. For example, the ADB initiated infrastructure credit rating and issue project bonds in local currency. Bankability is perceived and managed differently among public and private stakeholders in both emerging and mature markets.

Day 2, 29th June
09:30 – 10:30am, Salon 1,2,3
Keynote: Carsten Brzeski, Chief Economist, ING-DiBa: "Global markets – digesting European and US politics, turning to economics again?"
Summary

- According to the Economic surprise index, the first quarter of 2017 has seen the growth returning in Eurozone, USA, China and Emerging Markets. But digesting and coping with political risks will continue, even though volatility remains low. Despite the UK has voted to exit the EU, the cascade that other European countries follow suit never happened. The balancing act in Europe will go on and the EU exit risk is still there, therefore Europe is at the crossroads once again facing choice between break-up and superstate. In addition, the President of the United States Donald Trump and the President of the European Central Bank Mario Draghi also could influence the fate of the EU in future. Currently the Industry 4.0 remains uncharted territory. While traditional infrastructure starts crumbling, modern infrastructure also needs a boost in Germany and many other countries in the world.

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Day 2 Salon 1

10:30-11:30
Market conditions for lenders? Are new financing models having an impact?

Following an abrupt decline since 2007/8 and much discussion. The viability of capital markets financing for infrastructure has rebound and is expected to grow significantly over the coming decade. The tipping point will happen when the next crisis happens. The emerging market, such as Asian-pacific will represent the majority of global infrastructure spending. And megacities in both emerging and developed markets—reflecting shifting economic and demographic trend. New regulations imposed by authorities will also change the market conditions and ratings for players. Currently, there is so much liquidity in the market but the key issue is finding good quality assets. The competition has started between not only banks but also funds and insurance companies. In order to catch the trends, players are obliged to figure out innovative financing models to outstanding as it has become clear that banks' balance sheets may not be able to support the need to finance infrastructure, the focus has increasingly turned to institutional investors. The involvement of project finance (PF) or public, private partnership (PPP) model can be the ways for institutional investors to participate directly or indirectly in infrastructure investment.

10:30 – 11:30am, Salon 2
Fundraising – How have the dynamics between LPs & GPs changed?
Summary

- The fundraising environment remains extremely competitive; with fewer funds typically reaching a final close each year, managers must be willing to spend a significant amount of time fundraising and making sure their offering is attractive to investors.
- The number of funds managing to reach a final close has declined. Last year around 50% of capital secured was raised by just five funds, indicating an ongoing trend of capital concentration, with investors placing their faith in the deal-sourcing capabilities of the largest managers.
- The increased availability of debt financing and a number of investors looking to invest directly in infrastructure have led to increased competition, which in turn, has driven up the price of infrastructure assets. With strong competition for core assets in developed markets, managers are increasingly looking outside the traditional developed markets of Europe and North America when looking to put capital to work.
- Institutional investors continue to see strong risk-adjusted returns from their infrastructure portfolios and remain committed to the asset class. In the current financial environment dominated by low returns from traditional investments, investors are looking to assets such as infrastructure that can produce strong risk-adjusted returns, while at the same time providing downside protection and portfolio diversification.
- Despite strong returns in recent years, there are concerns from all players in the infrastructure industry about competition for assets pushing up pricing and eating into

eventual returns. However, the pipeline of infrastructure deals going forward looks strong, with countries looking to add and improve existing infrastructure as well as address challenges such as meeting Paris Agreement obligations. With a large number of countries having significant budget deficits, they will likely look to private capital to fund a number of these projects.

10:30 – 11:30 am, Salon 3

Emerging regions – What's hot, what drives the markets?

What conditions are needed to attract private sector investors?

Summary

- Five big main emerging markets in the world are in East Europe, South Africa, Indonesia, the Indians, South America.
- But the definition of the emerging countries now should be viewed as whether those countries are interested in becoming the emerging markets instead of defining themselves according to rules and principles from the associations. Based on technical capacity and the willingness to change, the vision and commitment of the government to move ahead and change and later to become the players in the global system are the drivers instead of the draggers of the infrastructure economy.
- On transporting infrastructure aspects, African, southeast Europe, central Asia, Latin American are very promising. On purely concession activities, Chinese competitors are more aggressive competitors in those areas.
- South American Chile, Columbia, Mexico is mature, but Southeast Asia, countries are very difficult. Since the needs for infrastructure of the people are the key points which is not clearly found. Many countries no matter they are emerging countries or sophisticated countries, the valuable numbers in "what the government wants" and "what is needed" for the people" are still open for discussion.
- Many of those emerging countries still have the strong inclination of corruption. Sovereign risks are longer term topic. These countries need to be educated in terms of safety investment environment. Peer pressure could be of a good leverage.

11:50 – 12:50am, Salon 3

Direct- and co-investments in infrastructure – Where are the low hanging fruit?

Summary

- The unlisted infrastructure fund model has, almost by default, become the primary route to market for most investors over the past decade. However, as many of the larger and more sophisticated infrastructure investors look to expand and develop their portfolios, there is a growing trend away from unlisted funds and towards direct investment strategies.
- These investors are turning to direct investments in order to gain closer control over the assets held in their portfolios, as well as to avoid paying expensive fund manager fees. It also allows assets to be held more easily over the long term rather than being restricted to the lifespan of an infrastructure fund.
- Direct infrastructure investments are gaining in popularity among sovereign wealth funds

and pension funds. Many are increasing their allocations to directs as a way to reduce fund management costs and to gain control over assets. Such investors are also increasingly developing their own asset management capabilities through recruiting experienced infrastructure investment professionals and expanding their in-house investment teams.

- Despite this, in reality direct investment requires significant internal resources and capital available to invest, which is not an option for the vast majority of institutional investors. Those investors with the resources capable of sourcing, executing and managing direct investments internally will certainly continue along that path, but unlisted funds still have a key role to play, meaning fund managers must continue to adapt their fee and fund structures in order to attract investor capital.

14:30 – 15:30 pm, Salon 1

Investing in high price environments - How do investors respond?

The core of the strategy of investors to invest in high price environment depends on the selection of markets, selection of projects and gearing ratio. For example, Allianz is trying to increase its alternative equity funds through Allianz Capital Partners. The gearing ratio can reach 50/50 due to the insurance regulation. Regarding the gearing ratio, the interest cover, profit margin, pay-out ratio etc. all are the factors need to be considered. Meanwhile, the valuation of the equity, the exit is also necessary to analyse before investing. Regarding infrastructure sectors, energy, transport and other type of shifting type of infrastructures, such as real estate project deal in the form of the concessionaire. Relating to the geography of infrastructure, the funds from the mature market now are also looking at the emerging market and the cooperation with other financial institutions from emerging market.