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North Korea-US war would detonate Asia 'ecosystem'

By Anthony Rowley

The outbreak of a military conflict between the United States and North Korea would threaten the entire Asian "economic ecosystem", analysts have warned as the head of the Asian Development Bank urged the two sides to find a peaceful solution.

North Korea this week accused the US of pushing the Korean peninsula to the "brink of nuclear war" after a pair of bombers flew training drills with the South Korean and Japanese air forces in a show of strength.

Jesper Koll, a veteran Japan analyst and chief executive officer of investment company Wisdom Tree in Tokyo, said heightened country risk was a "clear negative for North Asia", with the Korea-Japan-China triangle at the centre of attention. "It is not just about one or two isolated markets, but the entire economic ecosystem is potentially threatened," Koll told *GlobalMarkets*.

While a conflagration is still seen as unlikely, even the war-like rumours threaten to damage Asia's image as an investment destination.

50 YEARS OF STABILITY

ADB president Takehiko Nakao told *GlobalMarkets* that the possibility of a confrontation over North Korea was a "very important issue both for the region and for the international community".

"I hope this issue can be resolved soon and in a peaceful manner," he said. "For 50 years, we have had geopolitical stability in Asia and if we cannot keep this stability we lose much. Leaders must make utmost efforts to ensure that we keep stability."

However Kim Eng Tan, senior director, sovereign ratings Asia Pacific, S&P Global Ratings in Singapore, said there was only "small probability" recent events could have a "lasting impact" on investor perception about Northeast Asia generally.

Kim Jong-un: warning of nuclear war

"People are not seeing risk rising in a meaningful way," Tan told *GlobalMarkets*.

Continued on page 23

Softer Trump talk fails to diffuse Asian trade conflict fears

By Elliot Wilson

A trade war with the United States would deliver a severe jolt to growth and employment across Southeast Asia, delegates at the Asian Development Bank annual meeting in Yokohama told *GlobalMarkets*.

Policymakers and corporate leaders across Asia remain fearful of the protectionist inclinations of Donald Trump despite signs the prickly and

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Trump: targetting 'cheaters'

Move over World Bank, all hail Global Bank

Exclusive

By Anthony Rowley

An innovative public-private approach to multilateral banking is set to revolutionise the development world and provide a new rival to the Asian Development Bank. Move over World Bank — Global Bank is taking centre stage.

The California-based entity is "in the final stages of [formal] announcement", its president and chairman Ron Nechemia told *GlobalMarkets* in a pre-launch interview in Yokohama, venue of this year's ADB annual meeting.

Much about the new institution, which describes itself as "accredited by the UN General Assembly on Financing for Development" and which has been under preparation for several years, is still under wraps.

But its approach to development banking in Asia and

Continued on page 3

[noun]

{factoring}

m. Econ.

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Trump

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impulsive US president had toned down his rhetoric in recent weeks.

Soon after coming to office, Trump slapped the label of trade "cheaters" on a host of nations that run large trade surpluses with America. He later signed an executive order designed, Trump said, to tackle "foreign importers that cheat", and which could trigger new anti-dumping duties. Among the regional nations singled out were Malaysia, Indonesia, South Korea, China and Japan.

Paul Sheard, chief global economist at S&P Global Ratings, said Trump's rhetoric suggested America was no longer willing to trade freely with nations that protected local industries. "The US is saying: 'We don't see our firms having the kind of access to your market that your firms have to ours. Those days are over. We want reciprocity.' The danger is this could descend into retaliations and protectionist measures that would negatively impact Asia's exporters."

Trump has softened his speech in recent weeks. After meeting Xi Jinping, he hailed his "great chemistry" with the Chinese president and appears to have shelved plans to label China a currency manipulator.

But the region remains wary. Kim Eng Tan, senior Asia director of sovereign debt ratings at S&P, warned of the threat a trade war would have on the region. "We've only just seen some pick-up in momentum, and if the Trump administration comes up with measures that hit the region's exports, the region will sink into another period of slow growth."

WHEN BIG BOYS FIGHT

Tan warned even the threat of trade restrictions would be enough to jolt the region. "Sentiment cannot be underestimated. Just the threat of a trade war would cut investment, even before we see a fall in trade numbers. Consumer sentiment would be next. This would not be a small thing."

Concern remains high across the region. Six times more Malaysians believe Trump's anti-trade rhetoric will have a negative effect on their jobs than those who said it will have a positive one, according to the World Bank.

Concerns are also running high in Vietnam and Taiwan, economies that are highly dependent on exports to the US and China. Joseph Jao, president of Taishin Financial Holding, one of Taiwan's largest financial conglomerates said: "It's a genuine cause for concern. If there is a trade war, Taiwan will suffer. When the big boys are fighting with each other, the little boys get kicked."

Trump's $1tr infra plans no problem for Asia investment, says ADB's Nakao

By Anthony Rowley

The Asian Development Bank's president, Takehiko Nakao, has dismissed fears that rising interest rates in the United States along with US president Donald Trump's promised major infrastructure spending initiatives could draw global funds away from Asian projects.

In an exclusive interview with *GlobalMarkets,* Nakao also said that while foreign funds were needed to finance Asia's vast infrastructure spending requirement, investment from domestic corporate and other investors would become increasingly important in the future.

The ADB estimates in a new report that the Asia Pacific region needs annual spending of $1.5tr between now and 2030 in order to maintain current growth and reduce poverty. This rises to $1.7tr annually, or $26tr in total, if projects are adapted for climate change.

Much of this is expected to take the form of public-private projects (PPP) but with Trump having promised infrastructure projects worth $1tr in the US and Europe and Japan also embarking on spending, fears have grown that global investors could prefer these destinations to Asia.

Nakao discounted this idea however. "I don't think PPP projects in Asia can be affected by the infrastructure spending of the US," he told *GlobalMarkets*. "There is a huge amount of money in the world and leverage can be increased.

"So, if there is a safe and profitable PPP project in Asia I don't think it would be so much affected. This move by the Trump administration [to champion infrastructure spending] will not change the landscape."

NO RATE HIKE FEAR

Infrastructure spending prospects in Asia are also often linked to the issue of rising interest rates elsewhere, Nakao noted. "But my view is that with infrastructure investment or foreign direct investment [in general] a change of interest rates by the Federal Reserve Board by 0.25% each time will not have much impact," he said.

The ADB president acknowledged that the figures given in the bank's latest infrastructure report — which are roughly double those estimated in an earlier ADB report (2009) — were "more estimates than targets". But they give an order of magnitude on required spending, he said.

Nakao: ADB estimates $26tr funding gap

He also noted that while emphasis is put on the need for external financing for Asian infrastructure, domestic private firms are likely to be become increasingly involved, citing infrastructure investments by San Miguel and the Ayala Group in the Philippines where the ADB is located.

"In many developed countries, railways, power, and communications have been provided mostly by private companies under concessions from the government. Most of the infrastructure in advanced nations was built by private companies, which means PPP because the government is always involved in granting concessions."

Global Bank

Continued from page 1

worldwide will be very different from the business model of existing multilateral development banks (MDBs). "What we want to do is to create a new development bank doing substantially similar work [to existing MDBs] but which has the ability to manoeuvre quickly and deliver services in a different way," said the development banker who serves on several UN and OECD committees.

The Global Bank's fuller title is the Bank for International Development and Reconstruction — resonant of the World Bank's International Bank for Reconstruction and Development.

Nechemia said the bank would have government shareholders but declined to name any individual states. But it is also eyeing high-profile private shareholders. He mentioned Pimco, the world's biggest debt market group, and also asset management giant BlackRock.

"There is room for sovereign wealth fund participation [in the new bank] and for special cases from the private sector," he said. "Not tapping these resources, which are available in huge amounts, is missing what the private sector is all about," he said.

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Nechemia: eyeing private investors

TAPPING PRIVATE RESOURCES

Nechemia quoted a McKinsey report suggesting that global spending on infrastructure of $49tr was needed between now and 2030. The ADB and other MDBs can supply only a fraction of this, he said. But the outlook can be transformed if private and public funds can be channelled through a new institution like Global Bank, he insisted.

The bank, which is already recruiting staff, marks a more radical departure than that represented by other entities such as the Chinese government-sponsored Asian Infrastructure Investment Bank (AIIB) and the New Development Bank.

Nechemia said the aim of Global Bank was to channel funds into "economically and socially responsible development projects" such as infrastructure, thus "freeing up" existing multilateral and bilateral funds into other areas of development such as health.

Global Bank is taking its first step into the public arena with the proposed launch of a semi-autonomous affiliate, the Infrastructure Project Preparation Fund (IPPF) which hopes to launch soon with a public offering of securities to finance its operations.

The "sponsor" of Global Bank is the EurOrient Financial Group (EurOrient), according to the bank's website. Founded in 1988, EurOrient is a "private sector global development finance institution accredited by the United Nations General Assembly on Financing for Development".

EurOrient's mission is to "support economic and social development efforts of less-developed countries as they seek achieve internationally agreed development goals, including those contained in the Millennium Declaration.

(*See IPPF launch, page 4*)

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Asia crisis anniversary marked by fresh debt warning

By Anthony Rowley

The 1997 Asian financial crisis is now 20 years behind the region but with corporate debt rising to record levels and market volatility threatening, key policymakers yesterday (Thursday, May 4) called for increased "vigilance" and monitoring in order to avert further catastrophes.

Sri Mulyani Indrawati, Indonesia's finance minister, said Asia had become "more resilient" to shocks but added: "We must be vigilant to the danger of [fresh] shock and volatility coming from inside and outside the region."

She stressed the need for better monitoring of corporate debt within the region. Her warning came in the wake of concerns voiced by the IMF, the Institute of International Finance (IIF) and others over soaring debt levels globally.

Global debt has reached $217tr, or a record 325% of world GDP, the IIF said recently, as a result of historically low interest rates, which have encouraged borrowing in expectation that the global financial environment will remain benign.

Debt accelerated sharply last year and much of the debt is located among emerging non-financial corporations, the IIF said. Singapore, Hong Kong, Indonesia and Russia have "high levels of foreign exchange-denominated debt".

David Rubenstein, co-chief executive officer of The Carlyle Group, the investment firm, also warned recently of a repeat of the 1990s crisis. He estimated there was $4.5tr in emerging market corporate debt that was dollar-denominated.

NEED FOR VIGILANCE

Asian economies have opened up to external capital flows, which have aided regional growth but at the same time exposed them to new financial shocks, Mulyani said at an ADB seminar on Thursday. "Globalisation has brought benefits but it can also create a disaster."

The need for increased "vigilance" was also stressed by Junhong Chang, director of the ASEAN+3 Macroeconomic Research Office (AMRO), the regional surveillance arm of the Chiang Mai Initiative Multilateralisation (CMIM) launched in 2010 as a form of regional IMF for the Asia region.

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Indrawati: Asia 'more resilient'

Mainly at Japan's insistence, the CMIM is prevented from disbursing more than 40% of its $240bn funds without approval from the IMF. But some ASEAN nations are pushing for this level to be raised so the CMIM can mobilise more liquidity in the event of further problems in Asia.

Ms Chang said "policymakers should remain vigilant in the face of globalisation [and of] growing risks in financial markets."

New public-private facility to get infra projects 'shovel ready'

By Anthony Rowley

A new facility funded by both private and public sector bodies aimed at ensuring infrastructure projects can be pushed through from financing to the construction stage is to be launched as soon as this week, *GlobalMarkets* can reveal.

The Infrastructure Project Preparatory Facility (IPPF) is one of a series of initiatives to be unveiled at this week's ADB annual meetings as the focus of policymakers and investors broadens from financing projects to getting them off the ground.

The IPPF is a semi-autonomous agency that will be part of a new public/private development bank known as Global Bank that will focus on infrastructure financing and other areas of development worldwide.

Global Bank is a California-based institution being set up and which, unlike other multilateral development institutions, is expected to include both governments and private investors among its shareholders, *GlobalMarkets* has learned.

It is also expected to tap the wealth of sovereign wealth funds and other sources of institutional money to fund a wide range of infrastructure and other projects in both advanced and developing economies. In this sense, it will more closely resemble the European Investment Bank than other multilateral development banks.

In March, the ADB more than doubled its previous estimate of annual investment needed for infrastructure in the Asia Pacific region to $1.5tr a year between now and 2030, or $1.7tr a year ($22.6tr in all), if projects are adapted to cope with climate change.

"Everyone recognises the fact that there is a huge global shortage of infrastructure but the problem is less one of finance but more one of there being few projects that are "shovel ready," said William Thomson, who will become non-executive chairman of the IPPF.

PPP MONITOR

He said it typically took around three years to get infrastructure project feasibility studies done, and get projects ready to break ground..

Thomson, a former ADB vice president said: "That is what the IPPF would be designed to do — to finance the initial work to get the project up and ready for finance."

According to Ron Nechamia, president of the Global Bank, the IPPF aims making infrastucture projects "bankable". "Few projects that are bankable will fail to attract finance."

Thomson: IPPF to finance initial work

The IPPF aims to receive "mobilisation" funds at an inaugural board meeting later this month, followed by a public offering of securities to raise "operating funds" from private and public sector investors.Typically clients — a government or agency — using the IPPF's services would do so on a fee-paying basis.

Ryuichi Kaga, head of the ADB's Office of Public-Private Partnership, said there was an urgent need to improve the infrastructure project "implementation capacity" of many developing countries in Asia.

"In my experience, viable and bankable projects for PPP are somewhat limited but we are able to increase [the number] if implementation capacity is increased in governments," he told *GlobalMarkets*.
(See story Global Bank. Page 1)

Asia fears US retreat will leave trade world leaderless

By Elliot Wilson

America's retreat from its role as global leader on trade will leave the commercial world "drifting" unless China steps up to the plate, the Asia Pacific chief economist of Standard & Poor's has warned.

Americans voted in a president who delivered on a pledge to remove the US from the Trans-Pacific Partnership, the trade agreement between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States (until January 23 this year) and Vietnam.

Donald Trump's rival in last year's election, Hillary Clinton, also promised to scrap plans to join the largest regional trade accord in history.

The permanent loss of the US as a global leader would have troubling consequences for Asia's many export-oriented economies. "One scenario — and a serious risk — is that we end up with leadership drift, with no one stepping in to replace America," said Paul Gruenwald, chief Asia Pacific economist at S&P. "The danger is that we move to a more nationalistic system that retards global trade and widens inequality."

With Europe missing in action and India still in its developmental phase, the spotlight has fallen on China to become the new *de facto* champion of the forces of free trade and globalisation.

Gruenwald: fears 'nationalistic system'

CHINA RAISES BARRIERS

Many fear that the country, although it has benefited more from globalisation than any sovereign state in history, is neither ready nor willing to take charge. "China doesn't want to lead," said Xiang Songzuo, chief economist at Agricultural Bank of China.

"It's not about being ready or not being ready. To be leader of the world, other countries have to want to follow you, and it isn't clear to me that many countries want to do that. And China still acts according to its own needs. It doesn't want to do things that are in other countries' best interests."

To some, China's willingness, in the wake of Trump's November election win, to promote itself as the chief global proponent of free trade, was also disingenuous. China protects a host of local industries, including steelmakers and banks, and imposes non-tariff barriers on products ranging from cooked food to car parts. Over the past year, it has tightened, not loosened, control over its capital account.

Chang Liu, chief China economist at London-based Capital Economics, said although China had been the "big beneficiary of free trade" over recent decades, it believed in free trade so long as it happens beyond its own borders. "But it's shown no willingness to lower any of the barriers it deems important to protecting local companies. So in terms of free trade, its attitude is mostly rhetoric."

Infrastructure IPO first step to rebuilding India

By Elliot Wilson

Bankers have hailed today's debut domestic listing by an Indian infrastructure investment fund as a key moment in the South Asian nation's quest to build a country fit the modern global economy.

IRB InvIT, owned by highway construction firm IRB Infrastructure Developers, kicked off its IPO on the Mumbai stock market on Wednesday, in which it aims to raise up to Rs46.5bn ($725m) from a mixture of institutional and wealthy retail investors. Books on the initial stock offering will close today (Friday, May 5.).

Investors and bankers said the IPO, underwritten by Credit Suisse, ICICI Securities, IDFC Bank and IIFL, was a defining moment in India's long and often frustrating attempts to drive capital into much needed infrastructure projects.

A number of major investors, including Singapore sovereign wealth fund GIC Private Limited, are keen to commit capital to the stock sale, bankers said. "Five years from now, people will look back and say this was a seminal offering, because it allows developers to get on with the huge and pressing job of rebuilding India," said one banker involved in the deal.

For local investors, the offering is a novel one. IRB InvIT, which is registered with India's stock regulator Sebi as a trust, is comprised of six special purpose vehicles, each containing a single, operational toll road asset operating in five Indian states including Gujarat and Rajasthan. The hybrid financial product mirrors equity investments and generates debt-like fixed returns, and is commonplace in Southeast Asia, but has yet to be rolled out in Asia's third largest economy

© IRB Infrastructure Developers Ltd.

IRB rolls into the IPO market

YAWNING GAP

However, there are risks inherent in the product. Unit holders bear the usual risks associated with infrastructure projects: revenues from toll roads typically suffer when inflation spikes and traffic flow slumps. While inflation is under control, India regularly suffers from long periods of uncontrollably rising prices.

If it is a hit, it is likely to presage a surge of interest, with other infrastructure investment funds set to tap the capital markets in the months ahead, led by GMR Group and Reliance Infrastructure. Finance minister Arun Jaitley said last year that India needed to generate more than $1.5tr in fresh capital over the next 10 years to bridge its yawning infrastructure gap.

The IPO comes at a time when interest in India's capital markets is at a multi-year high. In recent weeks, the once-moribund market for Masala bonds — debt listed offshore that allow foreign institutions to buy rupee-denominated notes without needing to apply for licences or investment quotas — has enjoyed an unexpected and welcome revival. In late April, the National Highways Authority of India organised an eight-day roadshow that visited Singapore, Hong Kong, and London.

OBOR 2.0: China prepares for May summit with global ambitions

By Elliot Wilson

China's global ambitions will be a lot clearer a week from now. On May 14-15, Xi Jinping will host an army of political leaders in Beijing, where China's president is set to tout the commercial benefits of his flagship One Belt, One Road (OBOR) project.

What is said and done there could set the tone not just for China's relations with the world, but also for wider global trade relations in the 21st Century. OBOR started out as an $8tr project to pump capital into infrastructure that will stitch together the great economies of Asia and Europe.

But those already vastly ambitious plans are being revisited. Observers say the Chinese government now sees OBOR as a manifestation of its international ambitions — and of its long-term hopes of redrawing global trade flows and rules in its own image.

SOFT POWER, HARD ASSETS

Jin Liqun, president of the newly created Asian Infrastructure Investment Bank, a Chinese state-backed multilateral, said the government had "fine-tuned" OBOR, making it more international in scale and reach.

"There do not seem to be geographical limits to the OBOR initiative," he told *GlobalMarkets*. "This is not just an issue of connectivity in Eurasia; it covers the entire world." He added that the upcoming meeting in Beijing, officially titled the Belt and Road Forum for International Cooperation, "could be inspiring, with 28 leaders expressing their views in the conference, without a time limit on their interventions".

Others said the world had consistently misjudged the value China placed on OBOR — and its potential to redraw trade flows and rules in favour of Asia in general and China in particular. According to Paul Sheard, chief global economist at S&P Global Ratings, OBOR is all about China "wrapping soft power around hard assets".

"China's leaders play a long game," Sheard said. "In recent years, they've begun to define and implement a global strategy, commensurate with their re-emerging status as a 'great power'. OBOR speaks to China wanting to achieve multiple goals, from increasing its global reach and influence and shaping global rules-of-the-game, to boosting returns on external financial assets and honing a narrative about China's role that conveys the image of a benevolent hegemon."

Bearing the load: finding the $23tr to fill Asia's infrastructure gap

The ADB has just doubled its estimate of the money needed for infrastructure investment from $750m a year to $1.5bn. But as ministers meet in Yokohama it is unclear where the cash will come from — and on what terms

By Anthony Rowley

Asia's urgent need for financial resources to meet its vast infrastructure demand has been a longstanding issue but a startling new report has revealed that the need is much bigger than had previously been imagined.

The Asian Development Bank has more than doubled its estimate of annual investment needed for infrastructure in the Asia Pacific region. In a March report, the ADB put the figure at $1.5tr a year between now and 2030, or $1.7tr — almost $23tr in all — if projects are adapted to cope with climate change.

Many of these resources will need to come from the private sector but there is a fear that unless Asia makes its investment environment more attractive, private investment could flow instead to the US and Europe.

The developing Asia region that excludes advanced nations such as Japan will need huge spending on power, transport, communications and other projects if the world's faster growing economies are to maintain growth and reduce poverty, the ADB said.

The upper estimates are more than double the $750bn annual spending the ADB estimated in 2009 would be needed between then and 2020. As the needs of more countries have been included (45 now against 32 in the earlier report) so the infrastructure bill that Asia faces has soared.

Not only are the sums much bigger than previously thought but also they are nearly double the $880bn that the 25 biggest Asia Pacific developing nations (home to 96% of the region's population) have actually been spending on infrastructure in recent years.

Where is the money going to come from? The public sector has been the major source of funding for infrastructure in the past and is currently funding some 92% of the region's infrastructure investment, Juzhong Zhuang, ADB deputy chief economist and deputy director general of the regional co-operation department at the ADB tells *GlobalMarkets*.

Governments will continue to be the big spenders but the private sector is going to have to step up to the plate in a much bigger way if infrastructure is to get built.

CREAKING SYSTEMS

This is where things become problematic: Asia is no longer the most attractive game in town when it comes to infrastructure investment.

The period after the Lehman Brothers bank crisis in 2008 was a "very lucky [time] for the Asian region because there were few investment opportunities in advanced economies, and interest rates were very low," says Ryuchi Kaga, head of the ADB's Office of Public-Private Partnership. But, he tells *GlobalMarkets*: "The landscape will change [from here on]. Private sponsors [of infrastructure projects] will have more options."

US president Donald Trump pledged during his election campaign to spend at least $1tr on renewing outdated public infrastructure in the US and building a nationwide network of high-speed rail projects. At the same time, Europe and Japan are also preparing to modernise or replace their often creaking infrastructure systems.

There is so much financial liquidity globally that there is probably enough money available, in theory, to fund all the infrastructure projects that the US, Europe and other advanced economies, plus Asia and other developing regions, can come up with. But the issue is not as simple in practice as in theory, according to the ADB's Kaga.

"Investment opportunities will increase in advanced countries and absolutely they will draw the attention of more private investors," he says. Revenues from advanced nation infrastructure projects may be smaller than those in emerging economies but they are perceived to be "easier and safer", with virtually no political or currency risk involved.

Lay of the land
Grappling with climate-adjusted investment needs

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Estimated infrastructure investment needs by sector, 45 DMCs, 2016–2030 ($bn in 2015 prices)

Sector	Baseline estimates			Climate-adjusted estimates			Climate-related investments (annual)	
	Investment needs	Annual average	Share of total	Investment needs	Annual average	Share of total	Adaptation	Mitigation
Power	11,689	779	51.8	14,731	982	56.3	3	200
Transport	7,796	520	34.6	8,353	557	31.9	37	–*
Telecommunications	2,279	152	10.1	2,279	152	8.7	–*	–*
Water and sanitation	787	52	3.5	802	53	3.1	1	–*
Total	**22,551**	**1,503**	**100.0**	**26,166**	**1,744**	**100.0**	**41**	**200**

* = not applicable

Source: ADB estimates

This could impact the relative attractiveness of public-private partnership (PPP) projects in developing Asia and elsewhere compared to those in advanced economies. In turn, this means that Asian nations need to step up their game in terms of producing "bankable" projects and improving their implementation capacity for infrastructure projects.

While there has been "good progress" in introducing regulatory and institutional frameworks for PPP at the national level in Asia, not least in countries such as India and the Philippines, the implementation capacity of governments in terms of dealing with PPP laws and procedures is often lagging, says Kaga. One example is how to handle project bidding.

This is all the more so where local governments — in Indonesia, Vietnam and the Philippines, for instance — are becoming involved in PPP schemes.

At the same time, governments are being pressured from outside to provide high quality infrastructure. The ADB, along with governments such as Japan, are pushing this theme and the OECD said in a recent report on Asia that "what matters is not just the volume of infrastructure but also its quality". Governments "need to address better the long-term social and environmental impacts of infrastructure investments," the OECD said.

"Investment opportunities will increase in advanced countries and absolutely they will draw the attention of more private investors"

—Ryuchi Kaga, Office of Public-Private Partnership, ADB

PPP VS ODA

The ADB and others are providing grants and technical assistance to governments to help them improve their implementation capacity for PPP schemes. But such schemes are time consuming and "complicated" experts say while transaction costs are also high.

This creates a temptation for host governments to spurn the PPP approach in favour of ODA (official development assistance) projects financed by countries such as China where, some say, quality is relatively low compared to PPP.

With PPP schemes, the private partner usually invests in and operates a project. In the case of an ODA project the host government takes on debt and operates the project and a foreign company undertakes construction. Government debt then rises and efficient operation is not assured because governments lack project operating capacity. It often comes down to a balance between "easy and very quick or efficient and debt-free," says Kaga.

Whatever the claimed shortcomings of state-funded provision, it has produced impressive results in terms of infrastructure coverage, the March ADB report makes clear.

The ADB's Zhuang says China needs to be taken out of the picture because it is so big relative to other countries in the Asia Pacific region and also because it is "very atypical" so far as infrastructure is concerned.

The actual and projected infrastructure gap between what is being spent now and what needs to be spent is much smaller in China's case (around 1.2% of GDP) than is the case elsewhere in the developing Asia Pacific region where it is nearer 5%, Zhuang says. This gap is particularly wide in South Asia and in some southeast Asian countries, and even more so in the case of the Pacific islands.

Frequently voiced criticisms of China-funded infrastructure projects do not apply to those undertaken by the China-led Asian Infrastructure Investment Bank (AIIB), despite initial fears that this might be so. "I think the AIIB's is very much a global standard," says one official. "I cannot find any specific differences between their policies from those of the ADB or World Bank."

One of the reasons for China's success in advancing infrastructure coverage at a rapid rate is that there are many domestic players such as state-owned enterprises and other lenders for PPP projects without relying on outside sources. "They can do everything within the country," says Kaga.

PROJECT LIFE COST

Elsewhere, the problem is that many infrastructure projects are not regarded by investors as "viable and bankable", he says. This means "there are only two ways to increase the supply of [project] funding: to improve the borrowing capacity of developing countries or increase the number of viable and bankable projects. Probably you have to do both."

Some experts say that "selling" the PPP concept is not easy because of the political and commercial risks that private investors need to take on operating a project in a developing country.

Some governments prefer the EPC (engineering, procurement and construction) approach whereby a contractor undertakes to provide plant engineering and construction, and procures equipment overseas. Project operation is not included.

The prime minister's office in Japan is pushing the high quality infrastructure concept that will create high quality projects in terms of environmental and other standards. But Japanese equipment is expensive, experts note, and cheaper equipment is available elsewhere.

To overcome this, the ADB is promoting a "project life cost" approach, which takes account of the fact that good projects prove more economic over the longer term. Even so, the "quick and cheap" approach is still preferred by some countries.

Whatever approaches are taken to infrastructure provision — whether state-funded or privately financed — and whatever vehicles are used to ensure that vital services are provided, the financing gap will need to be filled by both public and private sectors, the ADB said in its report.

Multilateral development bank (MDB) operations as a whole in Asia currently finance only around 2.5% of infrastructure in the region — although many kinds of non-financial help are also provided.

This means that government funding of infrastructure has to be stepped up, with the aid of public finance reforms, while private sector investment will become increasingly important, especially in power generation and telecommunication projects.

The load on the MDBs as facilitators or middlemen in this process can only increase, officials say. GM

Building on relationships: AIIB's mission to help solve global ills

Exclusive GM interview

The president and chairman of the Asian Infrastructure Investment Bank Jin Liqun tells *GlobalMarkets* he is eager to learn lessons from others as well as to pass on the lessons of China's own economic development

Present and accounted for Jin Liqun at the Boao Forum for Asia's Annual Conference, March 2017

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By Anthony Rowley

The Asian Infrastructure Investment Bank was seen initially by some as a brash newcomer intent on breaking into the world of development banking by throwing around the money of a nouveau-riche China on possibly sub-standard projects and securing multi-billion dollar contracts for Chinese firms.

It was feared that the AIIB would dole out money indiscriminately in order to secure infrastructure projects, more or less ignoring the strict environmental and other standards that the family of United Nations-founded multilateral development banks (MDBs) had developed over decades of experience.

But that was several years ago when the AIIB was still in the planning stage. Now, when talking about the way forward for the AIIB and other MDBs, its president and chairman Jin Liqun employs a quotation from Albert Einstein: "We cannot solve our problems with the same thinking we used when we created them."

These institutions must, says the former vice finance minister of China during an interview with *GlobalMarkets,* avoid "following the beaten track that leads to environmental degradation and global warming".

These are remarkable words coming from someone at the top of an institution which some saw initially as a potential wrecker of accepted economic development norms, as an environmental spoiler and an outcast among MDBs.

"We must leverage the collective experience of our member countries and draw upon that knowledge to support innovative infrastructure projects that are financially viable, environmentally friendly and beneficial to local communities," says Jin.

These words could easily have come from the leaders of the World Bank, the Asian Development Bank and other MDBs that initially closed ranks, issuing a warning that the entry of newcomers such as the AIIB and others could cause a lowering of development standards.

The fact that they come instead from the head of the AIIB underlines just how far the institution has gone out of its way since its formal launch in January 2016 to gain international acceptance and become a good team player.

"We have strong co-operation with other multilateral development banks," Jin notes. The AIIB, he says, will "use its relationships with other MDBs and private financiers to meet Asia's growing infrastructure demands".

Just how big these demands are likely to be was illustrated in a report by the Asian Development Bank (ADB) that said developing and emerging nations needed to spend $1.5tr annually on infrastructure between now and 2030.

If infrastructure is to be adapted to meet the threat of climate change — which Jin acknowledges to be a very real one — then annual spending must rise to $1.7tr, said the ADB, almost doubling its estimate some seven or eight years ago.

The bank has now attained the status of an established MDB itself with 70 countries from around the world in membership and more waiting to join.

Notable exceptions are the United States and Japan, with the US thought unlikely to be in a hurry to embrace new multilateral institutions under the Trump administration and Japan intent on promoting development through bilateral efforts and via the Asian Development Bank.

The AIIB is eager to learn lessons from others as well as to pass on the lessons of China's own economic development, says Jin. "We were delighted to partner with a number of MDBs on six out of nine projects in 2016.

"We have agreements in place to strengthen co-operation with the European Investment Bank, the World Bank,

"I am optimistic we will be able to generate sufficient demand for the instruments we plan to bring to market"

"All of our members, like China, have their own plans for infrastructure development and all are welcome to submit projects to AIIB for consideration and financing"

the Asian Development Bank and the EBRD. I have also presented to the board at the ADB to discuss ways for us to work together. There is very strong co-operation happening among the MDBs."

Co-operating with other development banks has allowed the Beijing-based AIIB to draw upon the expertise of the ADB and others and to get involved in a series of joint projects after little more than a year of operations and with a modest staff of only around 100 professionals so far.

FUNDING

There is more, however, to Jin's insistence on the need to be a good citizen of the development world. The AIIB needs to tap global debt markets to supplement its capital base. While China is rich it is not as flush with foreign currency reserves as it was when the AIIB was first mooted and some expected the AIIB to draw mainly on Chinese domestic funds.

Jin avoids comment on the issue of China's diminishing international reserves. He says only that "it would be inappropriate to comment on a member's internal policies". But he expresses confidence that the AIIB will be able to raise debt to supplement its $100bn equity base.

"Financial markets favour high grade credits like the AIIB and other multilateral financial institutions," he says. "I am optimistic we will be able to generate sufficient demand for the instruments we plan to bring to market."

Some analysts say that rising interest rates in the US and widening differentials with Asian rates could cause funds to flee emerging market credits. They also argue that President Donald Trump's plan to spend $1tr on US infrastructure could act as a magnet to draw funds away from Asia.

"It remains to be seen," says Jin, whether increased US rates and other factors will drive outflows from Asian markets. But "at this stage, it does not seem so," he adds.

ONE BELT, ONE ROAD

How will the AIIB sell itself to portfolio investors interested in getting a piece of the Asian infrastructure action? Are they likely to want to know whether it will simply be a competitor to the ADB, or is it a part of Chinese president Xi Jinping's grand plan to "connect" the Eurasian continent?

Jin hedges somewhat on this. The AIIB will "support innovative infrastructure projects that are financially viable, environmentally friendly and beneficial to local communities. We are currently concentrating our efforts in energy, transport and sustainable cities."

Pressed to say more about the relationship between the AIIB and President Xi's One Belt, One Road (OBOR) scheme for linking East Asia with Europe via Central Asia, South Asia, the Middle East and beyond, Jin again resorts to rather hedged terms.

"OBOR has major strategic implications in terms of opening markets and creating growth opportunities, both for the 65 countries it touches and beyond," he says. "As there is a large overlap between the [AIIB] membership and countries participating in OBOR [we] will consider projects [in] OBOR."

But, he says "it is important to keep in mind that AIIB's mandate goes beyond OBOR. All of our members, like China, have their own plans for infrastructure development and all are welcome to submit projects to AIIB for consideration and financing."

The AIIB, Jin says, "can finance projects which meet our policies, criteria and guidelines. Those criteria are strict, he says, countering initial fears that the emergence of the AIIB and of the Brics Bank (or New Development Bank) could result in a lowering of standards.

Another area where the AIIB has come into line with long established development banks is on the need for private capital to supplement the role of governments and MDBs in financing Asia's "infrastructure gap" on the gap between projected needs and current spending.

"What we need to do is to catalyse private capital," says Jin. "And we need to do so in partnership with governments if we are going to meet the infrastructure needs in the region."

There was speculation when President Xi first announced the planned formation of the AIIB in 2013 that China would use the bank to help launch the "internationalisation" of China's currency, the renminbi (RMB), and that it would make RMB-denominated loans in order to do that.

"In the early stages of the bank's existence, it is likely that our loans will be denominated mainly in US dollars," says Jin. "Over the course of the next two years, we will establish and increase our capacity to provide financing in other currencies, certainly including RMB."

The AIIB recently signed an agreement with the World Bank's International Finance Corporation on international swaps and derivatives. "This emphasises how AIIB will gradually build capacity to support its clients' requests for different currencies," says Jin.

Will the AIIB seek to raise funds in RMB or in dollars, and will it issue bonds denominated in other Asian and international currencies? "As a global player, the AIIB will generate and tap demand where it makes sense and where the bank can achieve the best possible terms to finance its mission," Jin says.

"Since the bank's functional currency is US dollars, it will come as no surprise that the bank also has the ambition, over time, to establish a curve of transparent pricing references in US dollars." GM

Diggers at the ready: Estimated infrastructure investment needs by region, 45 DMCs, 2016–2030 ($ billion in 2015 prices)

Region/ subregion	Projected annual GDP growth	2030 UN population projection (billion)	2030 projected GDP per capita (2015 $)	Baseline estimates			Climate-adjusted estimates**		
				Investment needs	Annual average	Investment needs as % of GDP	Investment needs	Annual average	Investment needs as % of GDP
Central Asia	3.1.	0.096	6,202	492	33	6.8	565	38	7.8
East Asia	5.1	1.503	18,602	13,781	919	4.5	16,062	1,071	5.2
South Asia*	6.5	2.059	3,446	5,477	65	7.6	6,347	423	8.8
Southeast Asia	5.1	0.723	7,040	2,759	184	5.0	3,147	210	5.7
The Pacific	3.1	0.014	2,889	42	2.8	8.2	46	3.1	9.1
Asia and the Pacific	5.3	4.396	9,277	22,551	,503	5.1	26,166	1,744	5.9

Source: 2015 Revision of World Population Prospects, United Nations; ADB estimates.

* Pakistan and Afghanistan are included in South Asia. ** Climate change adjusted figures include climate mitigation and climate proofing costs, but do not include other adaptation costs, especially those associated with sea level rise.

Trump's bellicosity fires up Latin America's love-in with China

Latin America's trade relations with China are utterly lop-sided, determined far more by what China needs than by what Latin America wants. However, as regional sovereigns cast nervous glances north at a bellicose and protectionist-minded Trump administration, clear sources of overlapping mutual need are beginning to emerge

© REUTERS/Lucas Jackson

By Elliot Wilson

For those who believe in symbolism, China's reaction to last year's US presidential election could not have been more auspicious. Within days of Donald Trump's surprise victory on November 8, Xi Jinping was on a flight to Latin America.

The Chinese president used his time wisely, dropping in on the Asia-Pacific Economic Cooperation (Apec) forum, an annual conclave of the economic leaders of 21 Pacific Rim economies. He visited three heads of state: Peruvian president Pedro Kuczynski, Chilean president Michelle Bachelet, and Ecuador's outgoing president Rafael Correa.

Each of those house calls was carefully and purposefully selected. Over the past decade, China has nurtured ties with a region that was, until recently, allied with Europe and North America. China has upended the status quo by using its commercial and development banks to lend huge sums to sovereigns and, increasingly, leading regional corporates.

Much of China's attention has focused on the region's poorest and most troubled states, notably Venezuela (which has secured $65bn in funding from China, repaying its debts in the form of subsidised shipments of crude oil) and Ecuador, whose debts to China make up more than 15% of domestic economic output.

But China's leaders aren't stopping there. Grand plans to build a $10bn rail project linking Lima with the Brazilian port of Acu are aimed at slashing the cost of shipping grain and minerals to the People's Republic. Chinese companies are financing and building two nuclear power plants in Argentina worth up to $15bn. And in March 2017, Nicaragua's Supreme Court gave the final go-ahead to the $50bn Interoceanic Grand Canal, a 273km, China-controlled channel that will cleave the tiny Central American state in two and allow Chinese tankers to bypass the US-controlled Panama Canal.

LOW KEY GLOBALISATION

In truth, Xi's visit to Latin America was remarkably low key, at least by recent standards. He did not arrive bearing lavish gifts. No fresh loans were extended to struggling corporates or sovereigns. Nor were any new defence or infrastructure deals signed — though Xi did remind Apec members of China's 10 year plan to double bilateral regional trade.

And he worked his soundbites carefully. Fully aware that Trump was committed to withdrawing his support for the US-led Trans-Pacific Partnership, Xi spent much of his journey talking up the Free Trade Area of the Asia Pacific, which some have long seen as an ersatz rival to the TPP, and which has already garnered support from the Australian government.

Sovereign leaders across Latin America were left with the distinct impression that of the world's two genuine superpowers, one was truly committed to globalisation while the other was content to devour its own tail, all the while grumbling about the inequities of free trade. And that, of course, is what Xi wanted all along: to portray China, not the United States, as the modern world's shining city on a hill.

Xi's visit also inadvertently reinforced a sad truism about the nature of trade relations between Latin America's sovereigns and the world's second largest economy. Over the past decade, the mainland economy has grown exponentially in both scale and ambition. China plans to build a permanent space station by 2020, and to send crewed expeditions to the Moon. Chinese cellphones are snapped up by customers across the developed and developing world.

Latin America by contrast remains a region lacking innovation or direction. Its economies, big and small, largely lack growth and direction. Its leading corporates,with some notable exceptions, are typically simplistic affairs, exporting low-margin and unprocessed foodstuffs or minerals, much of which wind up either on mainland dinner plates or powering Chinese factories.

MASTER AND SERVANT

Little wonder Sam Aguirre, senior managing director and Brazil country head at Washington-based business advisory firm FTI Consulting, describes the relationship between the two sides as "wholly subservient. Latin America creates the basic product then ships it to China, which transforms it into high-value manufactured goods. It's a master-and-servant relationship."

It's a state of affairs that's only likely to persist, reckons Joaquin Cottani, chief Latin America economist at Standard & Poor's. "Latin America is only competitive when it comes to producing commodities," he says. "That is unlikely to change. These imbalances are likely to be with us for a long time."

And if anything, China's value to, and hold over, the region is growing. Take Brazil. Until a

Trade vulnerabilities: Colombia and Mexico most vulnerable to US trade shifts; Brazil, Chile, and Peru sensitive to Asia

Vulnerable		Moderately vulnerable		Less vulnerable	
Export Concentration ≥ 30%		30% >Export Concentration ≥ 15%		15%> Export Concentration	
China+Asia	US Protectionism	China+Asia	US Protectionism	China+Asia	US Protectionism
Brazil, Chile, Peru	Colombia, Mexico	Argentina	Peru	Mexico, Col	Brazil, Argentina, Chile

Source: HSBC

little over two years ago, Latin America's largest economy had a simple relationship with China. It exported everything from ore to orange juice, and potash to pork, and imported low-grade homeware and industrial goods. But in 2015, the People's Republic pledged to invest up to $50bn in the country's infrastructure. In early 2016, China Development Bank, a major policy lender, handed troubled energy giant Petrobras a $10bn loan, repayable in either cash or oil.

There is a pattern at work here, experts say: China spots a country in distress, then gallops to the rescue, bearing much-needed capital that it extends to needy sovereigns or corporates at low rates of interest. (Petrobras's cash-for-oil loan facility echoes similar deals that China has struck with Venezuela, a country for which the word 'troubled' barely does justice). But typically the beneficiary doesn't care: it is just happy to have a new friend with deep pockets. And China gets what it wants: another accommodating sovereign that it can absorb into its ever-expanding supply chain.

China's latest push into Brazil coincides with the latter's decision to allow foreign corporates to finance and build major infrastructure projects. In April, two mainland transport groups, China Railway Engineering and China Communications Construction, said they planned to bid for two new and very different rail lines projected to cost a combined $4.2bn.

The Fiol project in northeast Brazil will link settlements in northeast Brazil to the Port of Salvador in the eastern state of Bahia, while the Ferrogrão railway is scheduled to cut through and across the Amazon, linking the food producing region of Mato Grosso with seaports in the northern state of Pará.

China's interest in funding the projects comes at a time when domestic engineering and construction firms, many caught up in a nationwide investigation into corporate corruption, are struggling for traction and capital. "You're getting to the point now where, in terms of inward M&A deals into Brazil, basically the only money that's flowing in is Chinese," says FTI Consulting's Aguirre.

Nor is Brazil the only target of ambitious and capital-rich mainland corporates. Shandong Gold, a state-backed miner based in the eastern city of Jinan, recently agreed to pay $960m for a 50% stake in Barrick Gold's Veladero miner in Argentina, which is tipped to produce 830,000 ounces of gold in 2017.

China-backed corporates are even making inroads into Mexico, a country heavily dependent on investment from US corporates. State-run Anhui Jianghuai Automobile recently said it is joining forces with Mexican tycoon Carlos Slim to invest $2.2bn in a joint venture in the central state of Hidalgo, with the aim of manufacturing more than 250,000 cars a year for the Mexican and American markets.

THE ONLY GAME IN TOWN?

Does this offer undeniable proof that the economic bonds between Latin America and China are permanent and unbreakable? And has China really become the only game in town? Does Latin America's future lie with the world's second largest economy rather than with old friends in Europe or the United States?

Well, yes and no. Mainland policy lenders are busy channelling more cash than ever into the hands of Latin American sovereigns and corporates. But it's worth remembering that this remains a complex region, with old and robust trade ties and alliances. Argentina's biggest trade partner, according to the Observatory of Economic Complexity (OEC), a data tool created by the MIT Media Lab in Massachusetts, is its neighbour Brazil.

Colombia and Ecuador, meanwhile, both send more finished goods to the United States than to anyone else. And fully three-quarters of Mexican-made goods — $291bn out of a total of $391bn — headed north over the Rio Grande in 2015, according to the OEC.

As Marie Diron associate managing director of Moody's Sovereign Rating Group, notes, Latin America's pivot to Asia "is still at a very early stage. While Asia's vast markets and rising incomes present vast opportunities for Latin American exporters, deepening trade relationships will likely take some time. Our baseline assumption doesn't assume significant changes in the nature of trade flows between the two regions."

There are of course no guarantees that the US will remain the most valued trading partner for any of Latin America's nation states. America has dominated the region for nearly two centuries, ever since the fifth president of a young United States, James Monroe, announced his intention of opposing European colonialism across the Americas.

US LOOKS ELSEWHERE, EVEN MICHIGAN

But successive presidents have focused their attentions elsewhere: Bill Clinton on Asia and Europe; George W. Bush on the Middle East and Africa. Under Trump's predecessor Barack Obama, notes Standard & Poor's Cottani, "there was very little effort to get involved in the region at all. So I can't believe that it can get any worse under President Trump."

That of course depends much on Trump's state of mind — and whether the changeable US president decides to follow through on some or all of his threats, which have at various times included plans to shred the tri-nation North American Free Trade Agreement, to cut funding to global development institutions and to return production and jobs to US soil. Often this is more than mere bluster. In April, the United States opted not to renew its contribution to a key Inter-American Development Bank fund that supports pilot development projects across the region. GM

"A land full of vitality and hope"
1. President Xi Jinping at the APEC Summit in Lima, Peru, November 2016 **2.** HKND Group chairman Wang Jing at the inauguration of works for the Interoceanic Grand Canal in Brito, Nicaragua **3.** The compression layer in a stretch of track of the East-West integration (FIOL) project in Tanhaçu, Bahia Brazil **4.** Veladero goldmine Argentina **5.** "Grand Canal" celebrated by Nicaraguan school children **6.** Ferrogrão railway between Mato Grosso and Pará

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Indonesia's borrowers ready to reap rewards of deeper debt markets

As one of the fastest growing economies of all the G20 countries, Indonesia is on the up. Having taken some difficult decisions after coming to power in 2015, Joko Widowo's administration is reaping the rewards with growth accelerating, a budget deficit below 3%, and inflation tamed. The benign economic background has helped the Indonesian government become one of the most sophisticated sovereign borrowers in the international market. At *GlobalCapital*'s roundtable in Jakarta in early April, hosted by Standard Chartered, leading bankers and issuers gathered together to look at the impact of reforms to state-owned enterprises, potential US interest rate rises, and changes to tax laws on the potential to make a deeper, more effective debt market.

GlobalMarkets: Let's begin by talking about Indonesia's growth and growth prospects.

Aldian Taloputra, Standard Chartered: From the market's perspective the country has one of the fastest rates of growth of all G20 countries. Only China and India have faster rates of growth.

Since 2015 and the arrival of the new administration, the government has been trying to revamp the investment climate to move from a commodity-based economy to a more value added industry one.

It has forced the country to take some short term, bitter pills such as the not very popular policy of cutting the fuel subsidy, which resulted in higher inflation and forced Bank Indonesia to increase interest rates.

After those difficult measures, the economy now appears to be in a good position, having stabilised. We saw momentum begin to build in 2016.

For this year we believe the prospects are better. Commodity prices have started to show some recovery and although we don't expect oil to be back to $100 per barrel and revive strong investment in the mining sector, it at least provides relief because the economy is still heavily reliant on the commodity sector.

However, we believe reforms like infrastructure and structural reform will be the backbone of growth in the medium to long term. So, while the government probably thinks growth can be better, compared to other countries in the region and elsewhere, it is not at all bad.

Aaron Gwak, Standard Chartered: The Indonesian Republic recently conducted a number of roadshows in the US, London, the Middle East and Asia.

The reactions from institutional investors, globally, were very positive, not only on the economy, but also on the bond issuance programmes that the Indonesian Republic has been maintaining. And if secondary asset prices are any guide in terms of their satisfaction, one of the most recent issuances by the Republic of Indonesia — the $3bn dual tranche sukuk — is trading a good shade above par in today's market. Since the beginning of the year, from an asset price perspective, it is one of the best performing assets across the Asian curve.

Susiwijono Moegiarso, Indonesia Eximbank: The government is confident in its strong growth levels and is supported by the fact that Indonesia has become one of the three countries among G20 members with the highest growth rate in recent years. It will be challenging to achieve the 6% growth rate in 2018, for it will need not only growth from the domestic economy, but also a conducive global macroeconomy.

GlobalMarkets: Robert, when you are on your roadshows, what kind of questions are you fielding about the country's economy?

Robert Pakpahan, Republic of Indonesia: Regarding the performance of our economy in the eyes of our investors on our roadshows, most of them appreciate and think we are quite far ahead compared to many other countries.

Some of them even think that we should be able to achieve higher economic growth if we are willing to increase our borrowing and relax our spending limits. However, other investors are appreciative of our efforts and think we are doing the right thing because economic growth above