Investors should get good returns from infrastructure projects

Naoyuki Yoshino, dean of Asian Development Bank Institute, tells The Daily Star

SAJJADUR RAHMAN

INVESTORS have to be given a fair share of the revenue generated in the economy surrounding an infrastructure project to boost public private partnerships, said an expert.

Naoyuki Yoshino, dean of the Asian Development Bank Institute, a global think tank, said PPPs in infrastructure have failed in many countries because the rate of return relies only on user charges, which are nominal.

As a result, the rate of return remains very low. This does not motivate the private sector to come and invest in infrastructure projects, he told The Daily Star in an interview in Dhaka recently.

The economics professor said it is well known that good infrastructure has a huge spillover effect in the region around a project.

Railways bring manufacturing factories into a region by making the shipping of products faster and safer and connect manufacturers to markets and ports, he added.

New industry creates jobs in the region. Eventually, the service sector businesses, such as restaurants and hotels, are constructed to meet the increased demand, he said.

Farmers and small businesses too can sell their products at train stations, he added.

Studies show that good educational opportunities together with infrastructure investment create qualified workers who enhance regional productivity.

Yoshino said the spillover effects of infrastructure investment will increase revenue from corporate, income, and property taxes. In the past, all these tax revenues were collected by the government and not returned to the investors in infrastructure.

The economics professor has used a method called the difference-in-difference to compute the effect of spill over on tax revenue in places where infrastructure investment occurred compared to ones where no infrastructure investment took place.

It has been estimated that returning a part of the additional tax revenue to the construction companies and investors would raise the rate of return on infrastructure investments by 33 percent to 40 percent in case of Japan and by 14 percent to 16 percent in case of Uzbekistan, according to Yoshino.

He said 50 percent of the tax revenue raised should be shared between the government and the construction companies, which will take the rate of return for the latter to over 60 percent.

"If the businesses do better, the rate of return will be much better. Then it will become attractive for the private sector."

The model has not been implemented anywhere so far. But the ADBI chief said he wants to start it somewhere.

"If the rate of return on infrastructure is increased by injecting spill over tax revenue generated in the areas surrounding the infrastructure investments, much more long-term private capital could be forthcoming."

The ADBI chief also said fewer public sector funds would be needed for infrastructure investment. Meaning, the government could increase the total amount of infrastructure investment by attracting private finance when incremental tax revenue from the spillover effects are used to raise their rate of return.

"The higher the expected rate of return, the more private funds would be attracted."

Naoyuki Yoshino

In Southeast Asia, $8 billion in infrastructure investments are implemented every year against a requirement of $40 billion. But public money is insufficient to satisfy Asia's infrastructure needs, said the economics professor.

He said PPPs have been promoted for infrastructure development in India, Thailand and other parts in Asia. However, most PPP projects were disappointing since the rate of return on infrastructure depends mainly on user charges, such as train fares and highway tolls.

In order to narrow the gap between investment needs and actual government disbursements, the rate of return on infrastructure investment has to be increased.

Also a professor emeritus at Keio University in Japan, Yoshino said utilising private funds to develop infrastructure has the advantage of increasing the pressure to shorten the period of construction, completing it with minimal costs, and operating the project profitably after completion.

He said complex land ownership is a challenge for infrastructure development. In India, Bangladesh and Pakistan, land ownership is stringent, where many people claim their ownership to a single piece of land. As a result, construction cost becomes high.

Leasing is the answer to this problem, according to the economist. The land owners will get user fees every year from construction or road companies and as the change in ownership will not be required, construction will speed up, he added.

Yoshino backed enhanced access to finance for small and medium enterprises as they are the engine of growth.

He talked about a new form of financial intermediation called hometown investment fund that can be used to encourage start-ups and SMEs, as they often have trouble getting bank loans.

The fund has now been adopted as a national strategy in Japan.

The fund is project-driven. Firms and households decide to invest here by getting to know the borrowers and their projects. In this way, the fund distributes the risk but not so that it renders risk intractable, he said.

It contributes to economic recovery by connecting firms and households with SMEs that are worthy of their support. It also creates employment opportunities at the SMEs, as well as for the pool of retirees from financial institutions who can help assess projects.

The fund model has been adopted in Cambodia and Vietnam and is set to start in Mongolia. China, Malaysia and Thailand are also interested, said Yoshino.

He also called for putting in place a credit guarantee system so SMEs can access loans. If borrowers go bankrupt, the guarantors would pay up to 80 to 90 percent of the loans to the banks. "It is very important for SMEs to work."

The ADBI chief said a database of SMEs should be prepared, which will classify them as good, medium and risky; this will enable SMEs' credit rating.

Yoshino said post offices can be used to sell private financial products. Post offices are present nationwide, while financial institutions have offices in only large cities.

Post offices become agents where private banks, insurance companies and brokerage houses set up their small offices on the premise of the post offices. Thus, they can be used as a channel to generate revenues.

20 years of tie-ups and break-ups among EU carmakers

AFP

Opel cars, *left*, are transported from Vauxhall's production plant in Ellesmere Port, in Cheshire, north-west England.

AFP, *Paris*

EUROPE'S auto sector has witnessed two decades of takeovers, alliances and break-ups, the latest being PSA's purchase of Opel for 1.3 billion euros ($1.4 billion).

France's PSA, which owns the Peugeot, Citroen and DS brands, said Monday that it would buy General Motors' European subsidiary, which includes Opel and Vauxhall, to create the second-biggest European automaker, behind Volkswagen.

Here is a look at other major deals, some of which floundered, beginning in the 1990s.

DaimlerChrysler, a flop

In 1998 the German group Daimler-Benz struck a deal to fuse the troubled US automaker Chrysler with its prestigious Mercedes brand. It was presented as a merger of equals, but Daimler invested 36 billion euros in the affair, and ran the show from the start.

By 2005, the combination had soured; Daimler boss Juergen Schrempp stepped down and his successor, Dieter Zetsche, announced in February 2007 that Daimler would sell most of its shares in Chrysler. It did so three months later, ceding 80.1 percent to the US investment firm Cerberus Capital Management for 5.5 billion euros.

Renault-Nissan, an enduring alliance

In 1999, French carmaker Renault acquired a 36.8 percent stake in Nissan, a Japanese group that was close to bankruptcy, and the Romanian brand Dacia.

Renault boss Carlos Ghosn succeeded in pulling the three companies together and became head of all of them in 2005. Dacia blossomed from a derided east European carmaker to a respected low-cost brand that contributes regularly to the parent company's bottom line.

A cross-shareholding deal has put 43 percent of Nissan's shares in Renault's hands, while the Japanese group owns 15 percent of Renault. In October 2016, Nissan took a controlling stake in Japan's Mitsubishi Motors, bringing total production for the Renault-Nissan group to nearly 10 million vehicles a year.

Volvo: First to Ford, then Geely

In 1999, when Ford was the most profitable US automaker, it bought Sweden's storied Volvo brand for $6.45 billion (about 4.64 billion euros at the time).

A few year later, however, a combination of Japanese competition and rising oil and steel prices convinced Ford that it was time to look for a new buyer. In December 2009, it said it would sell Volvo to the Chinese group Geely for $1.8 billion.

Fiat: If at first you don't succeed

In the late 1990s the ailing Italian group Fiat, which is controlled by the Agnelli family, went looking for a partner. In 2000 it agreed to hand over 20 percent of its shares to US giant General Motors in exchange for six percent of GM's stock, then worth about $2.4 billion.

But Fiat's situation did not improve, and in February 2005, GM bailed out of the deal, paying $2.0 billion (1.55 billion euros) to cancel a so-called put option that would have required it to buy the rest of Fiat's equity.

In mid-2009 a fitter Fiat struck a deal approved by US president Barack Obama to rescue Chrysler by start purchasing shares in the US group.

Fiat completed its takeover of Chrysler in January 2014, and Fiat Chrysler Automobiles (FCA) now sells about five million vehicles a year. In 2016, FCA's net profit leapt to 1.8 billion euros from 93 million euros in 2015.

India becomes front in global e-commerce proxy war

REUTERS, *New York*

GLOBAL tech giants are heading for a proxy war in India. Alibaba is leading a $200 million investment into Paytm's marketplace, creating a new Indian unicorn. It confirms the intention of the Chinese behemoth to take on Amazon, which is aggressively ramping up, investing $5 billion into its local operation as other homegrown rivals flail. Only one of the tech big boys will emerge victorious.

The $255 billion Chinese group and Paytm have already invested together to build a dominant mobile-wallet payment business, now worth around $5 billion. Their smaller e-commerce unit is now being separated out to meet Indian regulations. After the latest fundraising, Jack Ma's Alibaba and its own payments affiliate Ant Financial will effectively control the e-commerce company and continue to own a large stake in the payments arm, which must be majority Indian-owned.

REUTERS/FILE

Advertisements of Paytm, a digital wallet company, are seen placed at stalls of roadside vegetable vendors in Mumbai.

Local rivals Flipkart and Snapdeal, backed by New York investment firm Tiger Global and Japan's SoftBank, respectively, helped to establish the domestic e-commerce industry. But their future roles look uncertain as these global tech giants, with deeper pockets, get stuck into the market.

Privately owned Flipkart is fighting hard to maintain a narrow lead; investors now reckon it is worth as little as one third of its $15 billion peak in 2015. Meanwhile, the founders of Snapdeal are cutting costs and headcount; an email to employees admits errors in executing its strategy. Talk of a possible merger between Snapdeal and Paytm keeps surfacing in local media. That makes sense, given SoftBank already owns a near 30 percent stake in Alibaba and could lose a fortune fighting head-to-head to build market share.

For now, Indian e-commerce has become a free-for-all, and a stark contrast to China where foreign companies have struggled. But there isn't room for everyone to financially succeed.

Alibaba's new commitment to Paytm E-commerce, following its success in building out a local mobile wallet business, puts it in a strong position. Fold in Snapdeal, and Amazon's Jeff Bezos would face a significant obstacle in the road to global domination.

Funds expect Saudi Aramco to be valued around $1-1.5tr

REUTERS, *Dubai*

FUND managers and institutional investors expect oil giant Saudi Aramco to have a market capitalisation of $1 trillion to $1.5 trillion when it sells shares to the public next year, a survey by regional investment bank EFG Hermes showed on Monday.

The valuation of Aramco, the world's biggest oil firm, has been the focus of intense speculation since the Saudi government last year announced plans to sell up to 5 percent of it and list the shares in Riyadh and at least one foreign stock exchange.

Deputy Crown Prince Mohammed bin Salman, who oversees the kingdom's economic policy, has said the sale is expected to value Aramco at $2 trillion or more, making it by the far the world's largest initial public offer.

The EFG Hermes survey, conducted at an investment conference organised by the bank in Dubai, found 39 percent of respondents predicted the market would value Aramco at between $1 trillion and $1.5 trillion.

Thirty-six percent expect a valuation below $1 trillion, and 24 percent a figure above $1.5 trillion, the bank said. EFG Hermes said it polled 510 international fund managers and investors from 260 institutions at the conference, as well as 147 other companies. It did not say how many of them had replied to the question on Aramco.

The company's ultimate valuation will depend on decisions that are expected to be made by Saudi authorities in coming months, including the tax rate that Aramco will pay as a public company, and the portion of Aramco's huge and diverse array of assets that is included in the listed entity. Saudi officials have given no concrete indication of how they will decide these questions, so any estimate of Aramco's value remains tentative.

REUTERS/FILE

A Saudi Aramco employee sits in the area of its stand at the Middle East Petrotech 2016, an exhibition and conference for the refining and petrochemical industries, in Bahrain.

The EFG Hermes survey suggests a higher valuation than some estimates by private analysts. Last year Foreign Reports, a Washington-based oil industry consultancy, calculated Aramco could have a market value of $250-460 billion, excluding the value of refining assets and guaranteed access to oil and gas.

Aramco's valuation is important for Saudi Arabia because it will determine how much money the government makes from the IPO and the size of foreign fund flows that are expected to enter the country to buy the shares.

The huge IPO looks likely to strengthen the case for Saudi Arabia to join the emerging markets indexes of international index compilers such as MSCI, a step which could attract tens of billions of dollars of fresh foreign money to the kingdom. The EFG Hermes survey found 16 percent of respondents expected Saudi Arabia to join MSCI's emerging markets index next year, 34 percent in 2019, 22 percent in 2020 and 27 percent at a later date.