

Virtual Roundtable

Financing Sustainable Infrastructure in the Asia-Pacific Region

20 April 2022

ROUNDTABLE REPORT

Introduction

The central purpose of the roundtable was to provide recommendations to APEC Finance Ministers to unlock and channel sustainable finance in the region for infrastructure while addressing barriers. The roundtable also discussed how APEC could support the development of bankable and sustainable infrastructure projects in the region. Infrastructure challenges present an opportunity for APEC countries, and specially for emerging economies, to achieve a stronger and sustainable growth to recovery after the COVID-19 pandemic.

There is a critical shortage of infrastructure financing in the trillions, while at the same time global economies are in the process of transitioning to a more sustainable path with SDG oriented criteria. Between 2022 and 2040, an estimated 30 trillion US dollars will be needed to bridge the infrastructure gap in APEC member economies¹. Bridging this gap will provide much needed economic stimulus for recovery but will simultaneously promote long term growth. Focusing on sustainable infrastructure will strengthen economies' resilience, contribute to the reduction of GHG emissions and the realization of the SDGs. With limited fiscal space and financing constraints, developing economies will need to attract substantial private

sector lending and investment to finance this effort. This will require addressing and mitigating risks arising from exchange rates, trade barriers and geopolitics compounded by climate events, which prevent infrastructure projects from becoming bankable. In addition, it will also require addressing specific impediments of using ESG financing in a variety of diverse regions with widely different levels of development and dependence on fossil fuels. These impediments include a lack of commonly accepted taxonomies or criteria with which to transition to carbon neutrality, standards, metrics, and good quality data. These are complex and difficult challenges but are not impossible to overcome. There are a good number of ongoing international efforts that address many of these impediments, including efforts to make these taxonomies and criteria interoperable across jurisdictions, align reporting standards and disclosure, and improve the availability and quality of data. There are tools and delivery mechanisms already in place, that are effective should they be adopted and utilized, and enable project sponsors to prepare projects that are aligned with both SDGs and the needs of their economies. They have also provided investors and lenders with data and information needed to identified projects across markets and make their financial decisions.

¹ Refer to <https://outlook.gihub.org>, from the Global Infrastructure Hub

SESSION 1: Identifying the Challenges

A. The Landscape of Sustainable Infrastructure

The investment market, which include the projects and their financing, operates by supply and demand, and is supposed to reach and deliver through a price. However, markets often fail to do so, and this is probably the situation in the infrastructure market. On one end there are investors seemingly willing to finance projects and on the other, countries needing more infrastructure to be financed, but in fact, projects are not always financed at the rate that would be expected or needed. One of the reasons for that is the lack of information and/or data needed in the infrastructure sector.

The aim is to get governments to record and provide information at the national accounts on infrastructure, which would be needed to better understand the actual public spending on infrastructure, and the extent to which this need to be matched by private sector financing. First, a consistent definition of infrastructure is needed. The OECD defines infrastructure for data collection purposes as the *“Set of fundamental facilities and systems that support the provision of goods and services essential to enable, sustain, or enhance societal living conditions and protect the surrounding environment from erosion and other disasters that reduce the usefulness for economic*

purposes”. It also divides it into Economic infrastructure (transport, utilities, flood protection and water management, IT and communications related infrastructure) and social infrastructure (education, health, public order and safety, culture, and recreation related infrastructure).

To better understand ESG, infrastructure and seek out areas of convergence, the OECD is currently undertaking 21 initiatives² in sustainable finance and infrastructure, which are aimed at assessing the sustainability dimension of infrastructure investments. These 21 initiatives are widely recognized in both the financial and infrastructure context. Several of them have been developed by multilateral development banks while others are private sector initiatives. The OECD analyzed the convergence across them and looked up for commonalities in terms of assessment approaches of ESG nature of infrastructure investment. They found more specificity in environmental factors (resulting in more granular assessment approaches), given that many of those initiatives focus uniquely on climate metrics. One of the limitations of these initiatives is that many of them only list the areas of consideration and do not specifically elaborate on how this could be assessed. There are a number of those initiatives that provide a risk-based approach, but the number is quite limited. This is reflected in several assessments that are merely based on the ‘yes’ or ‘no’

² These include; Asian Development Bank – Investment principles and Eligibility Criteria, Aligned Set of Sustainability Indicators for Infrastructure, CEEQUAL, Equator Principles, Climate Bonds Initiative, Climate Policy Initiative, EU Green Taxonomy, GIB, Green Bonds Principles, Green Loan Principles, GRESB, Harmonized MDB Frameworks on Climate Finance

Tracking, IDB: Sustainable Infrastructure Framework, IFC Definitions and Metrics for Climate- related activities, Environment and Social Performance Standards, Inf. Sustainability Council of Australia, ISI Envision, Social Bonds Principles, Sustainability Linked Loan Principles, UN social and environmental standards, UNDP SDG Impact Standards for SDG Bonds

response. In a way, this leads to a binary approach like a tinderbox assessment. While this approach is helpful in terms of ensuring that the issue is considered, it may not encourage projects to improve their performance on ESG overtime.

Infrastructure data collection, a key component of investment decisions, is limited to several fee-based data vendors. Preqin, Refinitiv, EDHECinfra, Moody's and IJ Global manage data related to infrastructure assets, while only Preqin and Refinitiv have databases with an ESG approach for the infrastructure sector. One aspect that is prevalent in all databases is that valuable data is skewed towards advanced financial markets and is limited for emerging markets and developing economies markets. Significantly less observations on infrastructure investment and deals are available when selecting the regions of Africa, Latin America, and the Caribbean, compared to North America and Europe. Reliability of data remains a major issue in the infrastructure sector. To fix this, it is advised to start with the national accounts. Countries should start collecting statistics on investments they are making into infrastructure using an agreed definition. The OECD has already carried out significant work on this in four countries and are planning to expand further. Meanwhile, there should be a restriction on which assessment approaches are valid to have a more quantitative approach to sustainable infrastructure. Finally, a consensus needs to be reached on how ESG assessment is done, and which data is suitable. As this will be provided by private vendors, there is a need to discuss and agree on what private vendors would consider worth providing. Governments cannot impose on data vendors what data to collect, but they could facilitate this. Partnerships between

governments, project managers, fund managers and data vendors are crucial to achieve this.

B. Impediments to Financing Sustainable Infrastructure:

Why is investment in sustainable infrastructure lagging, even though the potential supply of long-term finance is ample?

For PIARC, the World Road Association, sustainable infrastructure requires a strong multi-dimensional approach as it is essential to engage in dialogue with the users of transportation, road transport and constituents. Uncertainty also needs to be better incorporated as climate change has unknown impacts on weather events, while planning carefully for networking infrastructure. It is important to include maintenance of assets in the project, as it can be easy to forget the recurring investments that are needed to maintain the assets over the lifespan of infrastructure. In 2015, PIARC started to develop several frameworks to help operators address climate change. They are refining the frameworks with new studies and adding developments to identify all hazards and threats of infrastructure, how to increase resilience, and how to identify economic, social, environmental aspects of risk measurement. PIARC is also working on the engineering side of road projects. Planning good project management performance has significant positive impacts on budget delays and quality of projects.

It is important to understand how a global situation affects infrastructure development, materiality, double materiality, and how the company or the project affects its context, but also how the context impacts on the project.

Government institutions are becoming weaker in emerging markets. Health and Safety have become an increasing factor after COVID-19. On the other hand, there is a significant gap in education in emerging markets, which limits the transition of the workforce in the construction industry to undertake new roles which may require a more advanced skillset. In emerging markets, a gap exists between indigenous communities and developed urban cities and their perspective of how infrastructure is impacting their lives. Ecosystems are at risk when dealing with infrastructure. It is important not only to address climate change, but how the interventions are managed on the ecosystems. Infrastructure is not just beneficial for developing the world's economies; it also must enable, maintain, and improve the life of society. Investment in infrastructure is essential for poverty reduction. It also correlates positively and significantly with economic growth, considering that the provision of infrastructure has a significant impact on resource use, environmental quality, and overall quality of life. There is a very good example of a wind farm in Oaxaca, Mexico that did not address these issues and failed to achieve its objectives. Developers did not address correctly what indigenous communities were demanding on site and the project remains closed after 20 years of development. It has become a business case on the challenges faced in sustainable infrastructure.

While planning a project, it is important to consider the full cycle of infrastructure to understand the problem of each stage to be financed. With its eight stages: Governance, Planning, Procurement, Detailed Design, Financing, Construction, Operation and End of Life, the project developer is led through all the

details such as: the financial scheme, modes of partnership, the feasibility studies, the environmental, social, technical, geological, hydrological aspects, the bidding process and more. A developer should consider the whole circle of the infrastructure cycle, with these eight dimensions analyzing a project characteristic, from an integrated reporting perspective.

Sustainability is a holistic concept. Generally, investors/developers think about one specific outcome of a project rather than the holistic impact of it. Sustainability implies reliability and affordability and is based on a real sense of engagement. There are two key considerations. The first is from the side of the private sector, to be mindful of the economic and social realities in the context of the projects and looking beyond the normal financial models' due diligences. The second is involvement in conversations, making sure government approvals are in place, even if the surrounding community is engaged; having a broader awareness of what are the economic fundamentals driving the project, what is the impact of the project, and if it has a social positive or negative impact. What is often found is investors or developers engaging in specific government agencies or authorities that may be very keen on a project happening, but who might not consider all the various impacts of that project. Another important consideration is velocity as private sector timelines and windows on investing are relatively short, driven by the various market dynamics.

Several challenges can arise while financing sustainable infrastructure. On the financial side, concerns are about the ability of the relevant off-taker in terms of performance and payment obligations. There are some countries that have found different solutions to that. Indonesia, for example, set up an infrastructure guarantee fund.

There are other jurisdictions which found solutions through the involvement of political risk insurance or other types of coverage but by large, that is an issue mostly ignored. More emphasis should also be placed towards the more fundamental aspects of a project such as the capability of relevant off-takers to meet their financial obligation, performance obligations and other potential risks instead of documentation processes which can provide a better picture of the health of the project. When going into specifics, there can be inconsistencies in approaches, different institutions or ministries can have differing solutions, risk allocation outcomes, capacities, and constraints which form a significant challenge. An interesting point in this context is the opportunity for leadership that can come forward from specific jurisdictions and countries. A good pilot project could be the best way to take it forward as it forces people to focus on the immediate obstacles and overcoming them. The pilots give the possibility to establish a footprint for successful implementation of similar types of projects in a country or in a sector. The last challenge to be mentioned is political pressure. Often there is a lot of political pressure from the ministries (most frequently in election times) to issue tenders when they are not ready. The market gets geared up and when the tender comes out, lose market credibility and developers and investors realize that the country is not ready yet and they will look at another country.

It is important to raise awareness on adaptation and resilience because there is a tendency to focus on mitigation in discussions. Resilience is key, especially as Asia Pacific is in a high-risk area. Another important point is the long-term financial sustainability when developing sustainable infrastructure which is pertinent as

projects can incur cost overruns. It is also crucial to address the timeline friction that exists between public and private finance. While public finance has a longer-term view, private investors think more about the immediate returns.

General reflections and discussion

It is important to have projects ready in the early stages and vital that a holistic project preparation includes funding for greenfield projects or pre-feasibility studies. There are many tools and methodologies available to help operators, administrations and even funding organizations to navigate this. The key message is that there are ways to address these issues and to make sure that resilience is integrated into all projects and that key social factors are considered during the preparation of a project. Compared to the more traditional asset management class, infrastructure investment is a more complex investment structure, where it is relatively more difficult for investors to jump in. Investors are reluctant to invest in developing markets as there is a lack of knowledge due to data unavailability especially historical data that is crucial in mapping financial performance over time. Private sector investment needs to be backed up by a focus on good, structured data, and time series data to look at the performance over a longer period. A mapping of available tools and innovative approaches would be useful to ensure that investment decisions are made in a way where they are leveraging better data that is organized and structured.

Sustainability is not simply about financial sustainability, as it requires a holistic approach and the necessity of mapping both positive and negative impacts. Sustainability should not be

left behind for the sake of speed; it is essential to have integration and a more coordinated approach with government and or public institutions. Piloting is important to address inconsistencies and could bring in leadership. Payment capacity of the off taker is vital for the private sector and there are examples of solutions in different countries to address this. For good investment decisions, selection of operational and accommodating methodologies is key. Coordination on data is vital while not

forgetting adaptation to climate change and resilience. Finally, project preparation is pinnacle and should be incorporated into a process aligned with sustainability principles that considers uncertainties from the very beginning. Governments can take better steps forward in their planning by mapping risks, being more coordinated, being mindful of data, and focusing on project preparation, if they wish to tap into sustainable finance from the private sector.

SESSION 2: Meeting the Challenges

A. Leveraging Available Tools and Delivery Mechanisms

The lack of data has been a key gap curbing the flow of investments needed towards infrastructure projects. These data gaps can range from price issues, amount of investment needed, quality of preparation, all the way to capacity needs and more. This is often compounded by the reluctance of the private sector in disclosing information which creates a knock-on effect slowing down the use and implementation of ESG indicators. The Global Infrastructure Hub, SOURCE and The FAST Infra Platform are some of the organizations working to accelerate investments to infrastructure projects by leveraging data. The ability to analyze trends, aggregate and process data globally will better monitor funding pipelines and infrastructure utilization, and aid decision-making. This is especially useful for greenfield investments which has seen stagnation due to the hesitation of investors in banking on these projects. Standardization has also been effective in attracting institutional investors. A globally

applicable labeling system such as the Sustainable Infrastructure Label, can increase the investor's confidence in a labeled asset while also creating an asset class.

While bank loans are still used in most projects in the capital markets, especially green bonds, bank loans might not be suited for more complex infrastructure projects. Nonetheless, it is crucial to keep incentivizing local players who play a key role in financing.

The roundtable also noted the lack of detail and granularity in infrastructure expenditure especially since it relates to actual investment figures. In most G20 countries, it is difficult to assess how these assets will transition towards carbon neutrality. Thus, it is imperative that governments accelerate the creation of transparent plans and a comprehensive system for taxonomies. At regional level, the default rates of infrastructure investment are much lower than typical corporate loans. And yet, looking at banking regulations, they are treated the same way. Data accuracy, authentication and transparency is also a noted challenge. There is a need for a digital platform to provide real

authenticated data and a workflow for the entire community connecting various industry partners across the lifecycle value chain. This will create a trusted data source for the transacting parties and will also be able to facilitate the end-to-end sustainable finance infrastructure project process. The use of innovative software such as SOURCE to provide a holistic view of projects will help boost sustainable infrastructure. Using software for end-to-end management has the potential to reduce delivery risk, facilitate procurement, increase private sector mobilization, and encourage the digitization of the entire process. This can then lead to further action, if needed, such as capacity building to patch identified gaps.

B. The Role of APEC

The discussion above has highlighted many initiatives which have been pursued for sustainable infrastructure, proving that sustainable financing is essential. To summarize, sustainable infrastructure financing can be viewed as a triad of issues. Firstly, economies still need more infrastructure investment, both physical and digital infrastructure to serve connectivity and other development needs. As economies are recovering from the COVID-19, governments should play their role for investing in infrastructure to keep economic activities rolling, creating jobs, and launching economies on the long-term growth path. This investment must be done in the fiscal sustainability office and public debt management which are on the radar as economies are trying to pick up pieces in the post pandemic era. Secondly, infrastructure investment must serve sustainability related purposes, concentrating not only on climate related actions but also the creation of social goods. While we focus on

climate adaptation and mitigation activities, we also need to keep balanced between various development goals, including, for example, several challenges presented in the SDGs. Thirdly, there are several ways to achieve sustainable infrastructure financing while being flexible and avoiding fragmentation. There is a need to crowd private capital into sustainable financing by encouraging the private sector to issue more sustainable bonds and engage private investors for public private partnerships to do so. Also, organizing capacity building for investors and regulators producing templates and roadmaps for investors and forcing/encouraging them to utilize disclosure standards in the capital market. Realizing that there is no one-size-fits-all route to sustainable finance, it could first and foremost be a forum where best practices and lessons could be shared. A menu of best practices can be drafted and created for member economies to make informed decisions on what is best for them in the pursuit of sustainable financing. As far as common nomenclature is concerned, taxonomies and standards on sustainable financing should be created to keep up supply and demand and to address the information asymmetry problems between project owners and investors.

The Finance Ministers Process (FMP) in APEC has several differences with other finance ministers' processes in other forums. Firstly, the private sector is involved in the discussions of senior finance officials, deputy finance ministers, and even at the finance ministerial level. Secondly, the participation of international organizations is organized in a way that enables them to provide structured inputs to the whole process. The ADB, IMF, OECD, World Bank Group, together with IPAC are constant

participants in the whole process, called policy initiatives. These are extremely practical initiatives that are designed to provide specific outcomes in terms of implementing what the finance ministers have identified as deliverables. While the finance ministers are a very diverse group, they are instrumental to the support especially in facilitating project preparation.

The tools and delivery mechanisms exist, but the challenge is in promoting the uptake of these tools consistently, especially among member economies, or APEC.

Pilot projects are important to provide examples for the market to better understand the risks and to identify projects to invest in. The challenge is how to encourage and help economies promote the development of these projects. One recommendation could be proposing to use the APEC Finance Ministers process to provide that platform. There are already several documents that the Finance Ministers have issued over the years, including a roadmap in 2014 under China's leadership, where they identified very specific steps that economists should undertake to develop bankable infrastructure projects.

Guaranties is a topic that could not be overlooked. Governments should engage with MDBs regarding guarantees. MDBs can provide guarantees to private sector participants, but more importantly governments can counter indemnify the ADB or the MDB. This means that a guarantee can be priced at a sovereign financing level, which is a policy-based level normally provided when there is lending to government, which is very different than when the private sector lends at market interest rates. The instruments that are available to countries from the MDBs are designed for supporting this type of financing.

Transparency is another topic that should not be overlooked. Governments must be encouraged to be forthright in three areas: sustainability, private sector financing or private sector participation, and infrastructure. In that space, those initiatives or suggestions or ways forward will be one where government should be very transparent.

Finally, leadership and political will are crucial and should be considered while developing a sustainable infrastructure project.

APEC Business Advisory Council

The APEC Business Advisory Council (ABAC) was created by the APEC Economic Leaders in November 1995 to provide advice on the implementation of the Osaka Action Agenda and on other specific business sector priorities, and to respond when the various APEC fora request information about business-related issues or to provide the business perspective on specific areas of cooperation. ABAC comprises of up to three members of the private sector from each economy.

Sustainable Finance Development Network

The Sustainable Finance Development Network (SFDN) was set up within the Asia-Pacific Financial Forum (APFF) as recommended by the APEC Business Advisory Council (ABAC) in 2020. It serves as an international platform for private-public sector collaboration, accelerating the convergence of sustainable finance policies among APEC economies and strengthening the region as they develop a common global sustainability framework. This is done primarily through activities supporting the APEC Finance Ministers' Process and assisting ABAC in developing its high-level recommendations to the Finance Ministers. The United Nations Development Programme (UNDP) Financial Centres for Sustainability (FC4S) provides the secretariat for the network.