

Closing the Infrastructure Gap

Mobilising Institutional Investment into Sustainable,
Quality Infrastructure in Emerging Markets and
Developing Economies (EMDEs)



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Foreword

The coronavirus pandemic is a test of global resilience – whether of health, the economy, or society as a whole. Infrastructure investments are at the core of a society’s ability to absorb shocks. They provide access to basic public services, such as water, sanitation, transportation, and power systems. Economically, they create jobs and enable inclusive and sustainable long-term economic growth. Emerging markets and developing economies (EMDEs) are among the most vulnerable from a health and economic perspective to a global pandemic. Now more than ever, sustainable, quality infrastructure can strengthen the pandemic response today, support economic recovery tomorrow, and strengthen a society’s resilience going forward.

A focus on “building back better” is urgently needed, including for EMDEs. Previous crises have demonstrated that governments must avoid rushing to build lower-quality, more expensive, higher-carbon, and less resilient infrastructure assets. Instead, governments have an exceptional opportunity to launch green stimulus packages that prioritise sustainable infrastructure designed to mitigate the next public health crisis, bolster long-term economic growth after COVID-19, and adapt to the effects of climate change.

Infrastructure development in EMDEs is a USD 920 billion per year investment opportunity for institutional investors. Yet, only about USD 100 billion of private infrastructure investments were made in primary markets globally in recent years, with the overwhelming majority going to high-income countries.¹ As EMDE public budgets will likely remain under pressure, mobilising private capital – particularly the approximately USD 80 trillion of assets held by long-term oriented institutional investors – will be key to delivering infrastructure at the quality and scale required.

However, infrastructure investment is not only about the supply of finance. The biggest constraint to unlocking private finance is the shortage of well-structured, bankable project pipelines. Solutions to this challenge exist. Global platforms such as the Global Infrastructure Facility (GIF) foster pipelines of bankable, well-structured, sustainable infrastructure assets that are attractive to private capital.

Closing the infrastructure investment gap is a collective effort: governments need to promote the development of quality and sustainable infrastructure; Multilateral Development Banks (MDBs) to leverage tools such as credit enhancements to create risk-adjusted investment opportunities; and the private sector to prioritise investments that adhere to environmental and social best practice.

Times of crisis have the potential to create transformative change. We can plan now for the future we want through careful infrastructure project preparation and targeted investment. Together with our partners across the public and private sectors, we have the power to build back better with green, inclusive, sustainable infrastructure for long-term economic growth and resilience in EMDEs.



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¹ *Infrastructure Monitor 2020*, Global Infrastructure Hub, October 2020.

Executive Summary

Infrastructure is crucial for economic development: It enables sustainable economic growth and social progress, and it connects individuals to services, goods, and markets. Particularly in emerging markets and developing economies (EMDEs), sustainable and quality infrastructure plays a critical role in improving social, economic, and environmental outcomes in ways that collectively contribute to advancing the Sustainable Development Goals (SDGs) and Paris Agreement commitments. Amidst the economic recession induced by the coronavirus pandemic and the continued threat of the climate crisis, public investments in infrastructure can also enable more inclusive growth and improved resilience against future disruptions to economic activity, boosting long-term economic productivity, real gross domestic product (GDP) growth, and job creation.²

However, inadequate infrastructure continues to hamper economic and social growth, and overall sustainable development. The economic impacts of the global coronavirus pandemic have only further contributed to EMDE's infrastructure investment gaps, where already constrained public budgets have been directed towards addressing the public health crisis at hand. As EMDEs begin to look past the peak of the coronavirus pandemic, investments in sustainable and quality infrastructure will be one of the necessary and critical levers to provide needed services, and lift economies to higher sustainable growth paths. Considering the economic impacts of COVID-19 on global markets, this is an even more critical time for private investment in EMDE infrastructure. Sustainable, quality infrastructure can shorten economic recovery, support low-carbon pathways, and enhance climate, as well as social resilience.

Although the case for infrastructure investment in EMDEs is well known, public budgets have become even more cash-strapped and unable to meet the growing infrastructure demand needed to stabilise domestic economies. Public investments in infrastructure as a share of GDP in EMDEs have trended downwards due to increased public sector debt and lack of investment efficiency, contributing to an ever-growing "spending gap" by the public sector.³ To close the investment gap, EMDE governments have increasingly turned to the private sector to provide critical financing to support infrastructure development. With over USD 80 trillion in assets, institutional investors – such as pension funds and insurance companies – have increasingly been viewed as alternative sources of financing to help fill the infrastructure investment gap.⁴

Now, more than ever, private investment in sustainable, quality infrastructure is critical to boost economic growth in EMDEs and promote resiliency – resiliency against the current public health crisis and climate-related risks, as well as future global and national shocks. Evaluating demand-side perspectives and supply-side responses, this report highlights five "Action Areas" to mobilise institutional capital into sustainable, quality infrastructure in EMDEs. While there are many factors that influence the channelling of institutional capital into EMDEs, this report narrows the scope to five specific actions that investors and EMDE governments can take to promote greater private investment in infrastructure: (1) Expand infrastructure pipeline development through high-quality project preparation by governments; (2) promote standardisation of new/greenfield projects; (3) increase use of credit enhancement products by development finance institutions (DFIs); (4) create aggregation platforms; and (5) enhance the rigorous integration and disclosure of environmental, social, and governance (ESG) factors across the infrastructure lifecycle, including during upstream project preparation carried out by EMDE governments, as well as during downstream private investment.

² Bovino, B. A., Das, D., and Maguire, J. *Infrastructure: What Once Was Lost Can Now Be Found – The Productivity Boost*, S&P Global, 2020.

³ Fay, M., Han, S., Lee, H.I., Mastruzzi, M., and Cho, M., *Hitting the Trillion Mark: A Look at How Much Countries Are Spending on Infrastructure*, World Bank Group, 2019.

⁴ *sigma 3/2020, Power up: investing in infrastructure to drive sustainable growth in emerging markets*, Swiss Re Institute, 2020.



Key Messages

- The consequences of climate change – including rising sea levels, more frequent and extreme weather events, and increasing global temperatures – can have lasting, damaging effects on existing and planned core infrastructure, with a disproportionately damaging effect on small island developing states and least developed countries.
- Infrastructure investment plays a crucial role in stabilising EMDEs and providing access to basic services and will become an even more important driver for economic development in the aftermath of the COVID-19 pandemic. As such, priority must be given to not only driving more investment, but also to ensuring that such investments fill critical infrastructure service gaps.
- Despite the growing need for accelerated investments in sustainable, quality infrastructure, such activity, particularly among institutional investors, remains staggeringly low – hovering at around 0.7 percent of total private participation across debt and equity investments.

Sustainable and quality infrastructure is a key driver of economic growth and social progress and a critical enabler to achieving the SDGs and Paris Agreement commitments. Nowhere are infrastructure needs greater than in EMDEs, where infrastructure deficits are large at best and staggering in many countries.

Addressing the infrastructure deficit – and ensuring sustainability and quality of infrastructure investments and underlying assets – has become even more complicated as a result of climate change. Rising sea levels, more frequent and extreme weather events, and increasing global temperatures can have lasting, damaging effects on existing and planned core infrastructure. Transportation networks, power systems, and water and sanitation resources thus risk being adversely impacted. For existing brownfield infrastructure, climate change can decrease performance, as well as overall safety, functionality, and longevity of the asset itself, resulting in increased expenses associated with rehabilitation, repairs, and replacement. For planned infrastructure, climate change can significantly affect the project's overall planning and design modalities, contributing to higher design and retrofit costs to withstand the impacts, and – due to increased variability in climate-related events – potentially decreasing reliability for users. The potential of stranding of infrastructure assets also takes on new meaning in light of climate change.

Although climate change impacts the long-term viability of infrastructure globally, the consequences disproportionately affect small island developing states (SIDs) and least developed countries (LDCs). Such countries often have more limited institutional capacity and public resources to finance sustainable and quality infrastructure, capable of mitigating and proactively adapting to the risks posed by climate-related events. In SIDs alone, climate-related disasters have contributed to a loss of 2–3 percent of GDP annually over the past 30 years.⁵ Many LDCs that are not SIDs – primarily those located in Sub-Saharan Africa and the Asia-Pacific region – are also highly vulnerable to climate variability, including earthquakes, floods, and droughts, making adaptation and resilience ever more critical. Despite China, the United States, and India being among the largest emitters of greenhouse gases (GHG),⁶ it is SIDs and LDCs that ultimately bear the brunt of the adverse consequences of climate change while contributing the least to emissions. To mitigate and adapt to climate variabilities, EMDEs – particularly those in the most vulnerable regions – must scale up investments in low-carbon, climate resilient infrastructure.

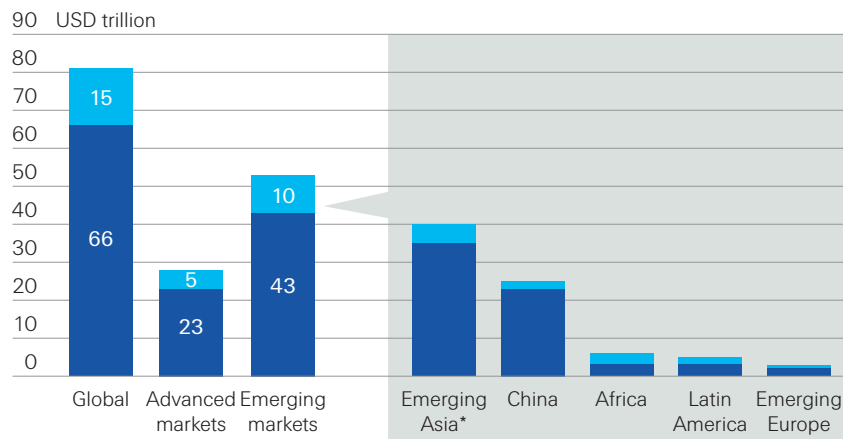
⁵ *Building Resilience in Developing Countries Vulnerable to Large Natural Disasters*, IMF, 2019.

⁶ DataBank: Total Greenhouse Gas Emissions, World Bank Group.

Global efforts to address infrastructure deficits, particularly against the backdrop of climate change, hinge on increased investment in quality, low-carbon, climate resilient infrastructure beyond what governments alone can provide. According to the World Bank, infrastructure investment needs in EMDEs are estimated at 4.3 percent of GDP, approaching USD 1 trillion per year.⁷ For EMDEs, the spending need is roughly 4.5 percent of GDP to achieve the SDGs and limit climate change to 2 degrees Celsius, let alone the 1.5 degree Celsius goal. Beyond investments in the development of new infrastructure, a steady flow of resources for the operations and maintenance (O&M) of up-and-running infrastructure also serves as a necessary condition for sustainable and quality infrastructure investment over the long-term. The World Bank estimates that ongoing O&M would cost EMDEs an additional 2.7 percent of GDP each year.⁸ Capital requirements are further compounded by needed investment in rehabilitation and expansion, as well as ensuring adaptation and resiliency of existing infrastructure to climate change. It is estimated that an average of 3 percent additional upfront capital investment is required to build resilience into infrastructure.⁹

In addition to needed capital investment, the EMDE infrastructure gap has an enormous and more acutely felt impact on access to services. The World Bank estimates that 940 million people live without electricity, 663 million lack improved sources of drinking water, 2.4 billion lack improved sanitation facilities, 1 billion live more than 2 kilometres from an all-season road, and 4 billion people lack internet access.¹⁰ Capital investment alone is not enough; rather, ensuring that sufficient resources are dedicated to O&M for both current and future infrastructure assets is critical for the long-term provision of services – particularly to underserved areas. Recognising the crucial role of infrastructure in the provision of basic services, global conversations around infrastructure investment have evolved from strictly focusing on the “investment gap,” to greater awareness of the “service gap” – that is, from the need to simply invest more, to the importance of spending better on quality infrastructure that closes access gaps and improves economic and social outcomes.

Figure 1:
Estimated Total Infrastructure Investments and Gap in Emerging Markets (2021–2040), in USD trillion

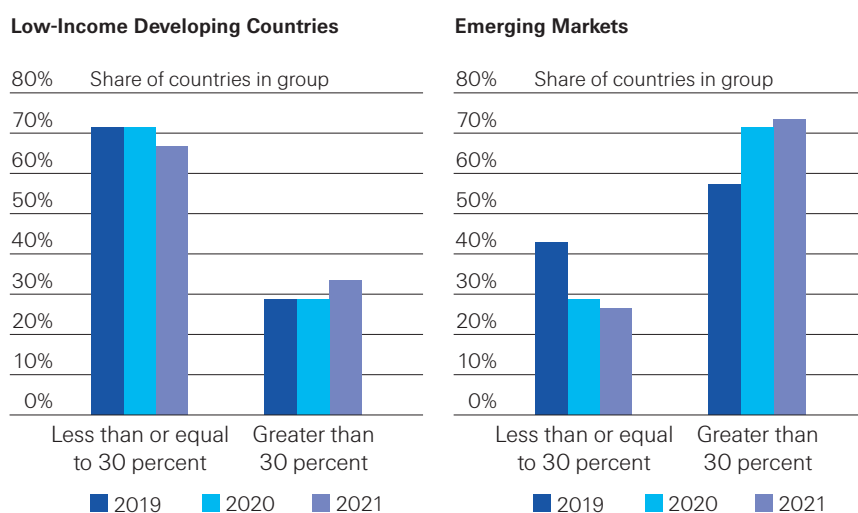


* Emerging Asia includes China

⁷ Rozenberg, J., Fay, M., et al. *How Much is Needed? Infrastructure Investments for Sustainable Development*, World Bank Group, 2018.
⁸ Rozenberg, J., Fay, M., *Beyond the Gap: How Countries Can Afford the Infrastructure They Need while Protecting the Planet*, World Bank Group, 2019.
⁹ J. Haley, *Why it’s time to invest in climate resilient infrastructure*, World Economic Forum, September 2019.
¹⁰ Rozenberg, J., Fay, M., *Beyond the Gap: How Countries Can Afford the Infrastructure They Need while Protecting the Planet*, World Bank Group, 2019.

With ever-tightening fiscal constraints and higher upfront costs associated with transitioning away from carbon-intensive infrastructure, public budgets alone are insufficient to fund the current and growing infrastructure needs across EMDEs. The COVID-19 outbreak is further constraining public budgets as governments channel resources towards their pandemic response. The likely downward revisions to potential growth also imply a smaller tax base over the medium-term than previously anticipated, which will only exacerbate difficulties in servicing debt obligations. The low interest rate environment will predominantly support advanced economies with large proportions of negative-yielding sovereign bonds. In several EMDEs, the ratio of sovereign debt service to tax revenue (see Figure 2), is expected to increase. This will hinder the ability of governments in providing support to critical areas such as social spending and infrastructure.

Figure 2:
Ratio of Public Debt Servicing Costs to Government Tax Revenue



Note: The figure shows countries whose ratios of sovereign debt service to tax revenue fall in each group.

Source: *World Economic Outlook*, IMF, October 2020.

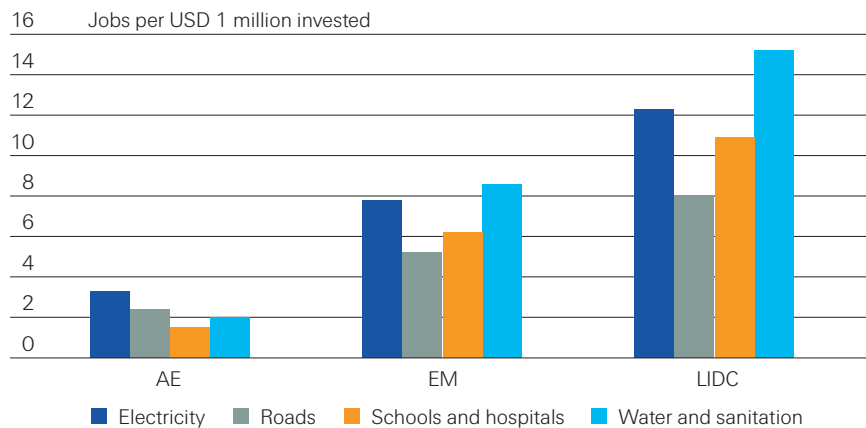
It is of utmost importance that governments work to cushion the social and economic impacts that arise as a result of the coronavirus. However, looking beyond the events that have unfolded due to the pandemic, it is also key for countries to reach higher growth paths. Sustainable, quality infrastructure will play a crucial role in stabilising EMDEs in the aftermath of the pandemic by increasing the long-term productive capacity of economies, lifting growth rates, promoting equitable access to basic services, and advancing shared prosperity. Importantly, infrastructure investing also creates jobs, with low-income developing countries¹¹ seeing the highest job intensity per USD 1 million of additional investment (see Figure 3). Within the energy sector, renewable-based electricity generation and energy-efficiency-enhancing investment are the most job-intensive,¹² with many of these jobs having low barriers to entry.

¹¹ Defined by IMF's *Fiscal Monitor* as countries that have per capita income levels below a certain threshold (currently set at USD 2,700, as of 2016, as measured by the World Bank's Atlas method), structural features consistent with limited development and structural transformation, and external financial linkages insufficiently close to be considered as emerging market economies.

¹² *World Economic Outlook: A Long and Difficult Ascent*, IMF, October 2020.

Hence, infrastructure investments can also support broader-based and inclusive economic growth. The disparity between the constrained fiscal budgets across EMDEs and the vital need for sustainable, quality infrastructure highlights the important role private capital must play in closing the infrastructure investment gap. Unlocking the approximately USD 80 trillion long-term investor asset base, which includes assets under management (AUM) from insurance companies, pension funds, and sovereign wealth funds, for example, would substantially help finance the gap through debt and equity instruments. This will be particularly important given the relative retreat of bank lenders from many markets.

Figure 3:
Job Content per USD 1 million of Additional Investment in Selected Infrastructure Sectors



Note: The figure shows for different sectors, types of investment, and for country groups, the estimates of the job content of USD 1 million of investment. AE = advanced economies; EM = emerging economies; LIDC = low-income developing countries.

Source: Fiscal Monitor, IMF, October 2020

While institutional capital has enormous potential to fill infrastructure investment gaps in EMDEs, this potential has not translated into significant movements of money. The current level of institutional investor activity in new infrastructure deals for both debt and equity investments is extremely low, at only 0.7 percent of total private participation in infrastructure investment in EMDEs,¹³ with bank loans the most prominent funding source. The demand-side factors leading to this staggeringly low level of participation from institutional investors stem from a broad range of perceived risks – which have only been amplified by the economic ripple effects of COVID-19 in EMDEs. With a particular focus on institutional investors, this report addresses the demand- and supply-side dynamics that have historically hindered institutional investors from putting capital to work in EMDE infrastructure and provides five key “Action Areas” to unlock this pool of capital.

¹³ *Behold the White Knights! New research on institutional investor participation in financial EMDE infrastructure*, World Bank Blogs, 2018.

How to Close the Gap: Demand-Side Perspectives and Supply-Side Responses

Key Messages

- Institutional investors, given the long time-horizon of their liabilities, are ideally positioned to provide necessary funding to help reduce the infrastructure gap.
- While allocations to EMDE infrastructure investment have increased, greater allocations are needed to sufficiently close the investment gap.
- Infrastructure needs in EMDEs have grown considerably and will continue to accelerate to support expected economic growth rates – yet attracting institutional capital requires that EMDE governments create the necessary conditions to facilitate such investments.

Infrastructure, by nature, is a long-term investment with a useful life of 20 to 100 years, depending on the underlying infrastructure asset. And with large upfront capital costs, infrastructure requires long-term investment horizons to generate sufficient revenue. Many institutional investors, given the long time-horizon of their liabilities and with enough long-term capital to commit, are ideally positioned to help provide the necessary funding to significantly reduce the infrastructure financing gap in EMDEs. As a signal of increased investor appetite for infrastructure as an asset class, an EDHEC Institute survey of 186 asset owners representing about USD 7 trillion in assets¹⁴ indicated that those investors plan to allocate more to infrastructure in general.¹⁵ Moreover, about 60 percent of such investors already active in EMDEs are expected to increase their allocation to infrastructure in developing countries. Further, a World Bank report¹⁶ highlights that investing in resilient infrastructure delivers net benefits in low- and middle-income countries, with USD 4 in benefit for each USD 1 invested. Despite these positive signals, the channelling of sizeable private investment into EMDE infrastructure is still lacking. The challenge then is to better translate the positive intent to invest into greater allocations to EMDE infrastructure investments.

¹⁴ *2017 Investor Preferences and Valuations Survey: From Investment Plans to Price Discovery*, EDHEC Institute, 2017.

¹⁵ Roughly 80 percent of investors would like to increase infrastructure investment (EDHEC 2019). Survey respondents represent USD 10 trillion in assets under management, more than 10 percent of the global total.

¹⁶ *World Bank Report Illustrates Benefits of Resilient Infrastructure*, SDG Knowledge Hub, a project of IISD, 2019.

How to Close the Gap: Demand-Side Perspectives and Supply-Side Responses

Developing countries require more than USD 2 trillion in annual infrastructure investments over the next 15 years to support expected economic growth rates.¹⁷ Unlocking private sector infrastructure financing on a large scale is therefore key to both emerging and developed economies. The five action areas identified below highlight how EMDE governments and DFIs should approach infrastructure projects (brown and greenfield) to ensure demand-side preferences are met. The ultimate goal is to support institutional investors in obtaining optimal investments that match their investment criteria, all the while ensuring governments can lock in the much-needed capital for infrastructure projects.

Table 1:
Summary of Action Areas

| Action Areas | Description |
|---|--|
| 1. Expand Infrastructure Pipeline Development through High-Quality Project Preparation | Dedicate more resources into upstream project preparation to create pipelines of quality, bankable infrastructure programmes, and projects capable of mobilising institutional capital. |
| 2. Promote Standardisation of New/Greenfield Projects | Move away from standalone, bespoke infrastructure transactions towards standardised contract terms, procurement, and disclosure requirements that, collectively, achieve cost efficiencies and accelerate the timeline in bringing projects to market. |
| 3. Increase Use of Credit Enhancement Products | Deploy credit enhancements to mitigate risks for institutional investors and enhance the overall affordability of infrastructure assets. |
| 4. Create Aggregation Platforms | Build aggregation platforms that pool smaller and/or below-investment-grade infrastructure assets into single securitised vehicles to improve risk-return profile and overall financial attractiveness to institutional investors. |
| 5. Enhance Integration and Disclosure of ESG Alignment | Integrate ESG and climate adaptation/resilience considerations at the earliest stages of project preparation, and enhance associated disclosure to demonstrate both the ESG and financial value of infrastructure investments. |

¹⁷ *Unlocking private sector financing in emerging markets infrastructure*, McKinsey & Company, 2019.

Action Area 1: Expand Infrastructure Pipeline Development through High-Quality Project Preparation

Key Messages

- Dedicating resources to upstream project preparation helps to allocate risk between the public and private sector actors and promotes robust pipelines of high-quality, sustainable, and bankable infrastructure projects that are commercially attractive to institutional investors.
- Project preparation facilities (PPFs) facilitate private investment in infrastructure by offering targeted support at each stage of the infrastructure project lifecycle – from the earliest planning stages through the tendering phase.
- Serving as an intermediary between MDBs, government entities, concessionaires, and project owners, PPFs play a critical role in aligning incentives among diverse stakeholders and enhancing conditions and overall bankability of infrastructure projects in ways that consider the local operating environments of EMDE governments, while still optimising risk-return profiles for institutional investors.

Among the well-documented challenges faced in mobilising private finance for infrastructure in EMDEs is the lack of bankable pipelines of investment opportunities. Whereas institutional investors demonstrate a growing demand to channel their patient capital into long-term infrastructure assets, the public sector has struggled to furnish sufficient supply in the form of bankable project pipelines to match long-term institutional capital. With public infrastructure services falling under the domain of national and subnational governments, the fundamental reason for the dearth of pipeline opportunities is attributed to EMDE governments' lack of capacity and resources to prepare, plan, and prioritise infrastructure projects that are attractive to private investment.

Addressing the perennial and growing infrastructure investment gap in EMDEs requires that governments build robust, investment-ready pipelines that are attractive to institutional capital. To meet the SDGs and commitments under the Paris Agreement, the G20, the Organisation for Economic Co-operation and Development (OECD), the World Economic Forum (WEF), and other international fora have supported continued collective action in delivering pipelines of well-prepared and high-quality bankable infrastructure projects that mobilise private capital. To that end, upstream project preparation serves as a critical first step in making infrastructure projects bankable – that is, having infrastructure projects prepared up to a stage where risk is appropriately allocated between the public and private sector such that institutional investors are willing to engage.

The Global Infrastructure Facility: Building Pipelines of Quality, Sustainable, and Bankable Infrastructure through Project Preparation

The Global Infrastructure Facility (GIF) was created in 2014 as a G20 initiative to increase private sector investment in sustainable infrastructure in EMDEs. Using a “more than money” approach that couples funding with hands-on, flexible, technical expertise, the GIF supports end-to-end, comprehensive advisory services to client governments and multilateral development bank partners to build pipelines of bankable and sustainable infrastructure investments that are attractive to private capital. The GIF’s Advisory Partner network of more than 50 investors and financiers – collectively representing more than USD 13 trillion in AUM – are called upon during market soundings on GIF-supported projects to maximise attractiveness to private capital when investment opportunities are brought to market. As a global collaboration platform, the GIF enables collective action among a wide range of partners – including donors, development finance institutions, client country governments, and members of the private sector – to leverage both resources and knowledge to find solutions to sustainable infrastructure financing challenges. In its first four years of operation, the GIF has supported over 100 infrastructure programmes and projects across 50 countries. Overall, through pipeline preparation support provided thus far, the GIF anticipates mobilising total investment on the order of USD 76 billion, including USD 50 billion from the private sector. The GIF is currently supported by Australia, Canada, China, Denmark, Germany, Japan, Singapore, and the World Bank.

In efforts to bring more bankable infrastructure projects to market, EMDE governments have increasingly turned to project preparation facilities (PPFs) housed in multilateral development banks (MDBs) to provide needed support for creating policy, regulatory, and institutional environments conducive to private investment in infrastructure, as well as provide funding and technical support for designing and structuring specific infrastructure projects (or programmes) for the market.¹⁸ PPFs provide support at each stage of the infrastructure project lifecycle – from planning to selection, pre-feasibility through feasibility, design, choice of procurement, structuring, and contract development through to financial closing. To meet the investment preferences of institutional investors, PPFs have also played an integral role in promoting programmatic approaches to project preparation – transitioning away from standalone transactions to a scaled-up collection of investments at larger ticket sizes that utilise standardisation to enable replicability. Through their work with government entities, concessionaires, and project owners, PPFs also enhance the enabling environment for infrastructure project preparation in EMDEs by developing standardised bidding frameworks, procurement documents, and concession agreements. Such heavy lifting by PPFs at the upstream project development stage¹⁹ can optimise the conditions and overall bankability of infrastructure projects in ways that account for the unique operating environments of EMDEs while still meeting the investment preferences and risk profiles that private lenders and financiers desire. Demonstrating the critical value-add of PPFs in improving bankability, investors who have used PPFs have expressed mostly positive experiences.²⁰

¹⁸ Runde, D.F., Moser, H., Nealer, E., *Barriers to Bankable Infrastructure: Incentivizing Private Investment to Fill the Global Infrastructure Gap*, CSIS, 2016.

¹⁹ Fida Rana. *Preparing Bankable Infrastructure Projects*, World Bank, 2017.

²⁰ *Investor Perceptions of Infrastructure*, EDHEC infra, 2017.

The European Bank for Reconstruction and Development (EBRD) Infrastructure Project Preparation Facility (IPPF): Promoting the Efficient Delivery of Infrastructure through Project Preparation and Policy Dialogue Support

Created in 2014, the IPPF provides high quality project preparation, policy support, and institutional strengthening for public and private sector infrastructure, as well as public-private partnerships (PPPs). The IPPF was designed to improve the efficiency and replicability of infrastructure projects, as well as accelerate investment in infrastructure across the countries in which EBRD is active. The IPPF features two windows – a Sustainable Public Sector Infrastructure Window (SIW) for public sector projects, as well as a PPP Window to support the development and delivery of PPP projects. The SIW focuses on building pipelines of infrastructure programmes and projects that are well-structured, bankable, and responsive to the needs of beneficiaries. Since its establishment, the SIW has delivered over 50 investment projects in the public sector, estimated at EUR 2.3 billion. Through the PPP Window, the IPPF has provided PPP transaction advisory services to public and private sector clients, with one project launching a PPP tender and two in the tender preparation stage.

Action Area 2: Promote Standardisation of New/Greenfield Projects

Key Messages

- Infrastructure transactions often include bespoke financing structures, adding complexity, time, and higher upfront costs to the due diligence process.
- The standardisation of loan contracts can alleviate the cost associated with due diligence and accelerate the time to capital deployment.
- Standardising PPP contracts not only enhances the efficiency of project preparation, but also increases the overall ticket size of infrastructure transactions – making them commercially attractive to private investment.

Individual infrastructure transactions are often brought to market with bespoke financing structures. These structures are therefore underpinned by unique documentation, making the due diligence part of the investment decision-making more difficult, time consuming, and hence, more expensive. For infrastructure PPPs, transaction costs – encompassing legal, financial, and technical advisory – can range from 1 to 10 percent of the overall project cost and can amount to between USD 40–400 billion per year in expenses for low- and middle-income countries.^{21 22} Therefore, when investing in illiquid asset classes where due diligence is key to a successful investment, institutional investors have a preference for simpler processes to minimise costs and capital deployment timelines.

European Financial Services Roundtable: Providing Available Global Best Practice Blueprints for Infrastructure Investment Contracts

The 2018 European Financial Services Roundtable (EFSR) strategic paper on “Facilitating European Infrastructure Investment” provides a template for documentation and disclosure requirements, which should be universally applied. Despite the paper being initially written for European infrastructure, the framework can be replicated around the world, including to EMDEs. The proposed template can act as a starting point towards a shared public-private sector understanding and lead to the implementation of a standard market practice. In particular, it includes four key elements:

1. Disclosure and reporting requirements: An industry standard template has been developed.
2. Debt terms and documentation: A common governing standard, representing an important step towards harmonising contract terms across jurisdictions.
3. Administration and arbitration: Information on project monitoring, such as cash flow and collateral management, and a commonly agreed-upon arbitration mechanism.
4. Third party advisors: Setting out common standards for the engagement, liability, and disclosure requirements for third-party advisors, such as technical advisors, consultants, and auditors.

²¹ Oberholzer, B., Schneider-Roos, K., Boulanger, C., van Staden, M., *Summary of Good Practice of Successful Project Preparation Facilities*, City Climate Finance Leadership Alliance, 2018.

²² Estimates are an average of total transaction costs borne by both public and private partners.

The World Bank, GIF, and Global Infrastructure Hub: Collaborative Efforts to Promote Standardisation of PPP Contracts

The GIF collaborated with the World Bank and Global Infrastructure Hub to promote the standardisation of PPP contracts. The bespoke nature of different legal systems and the need for “tailor-made” solutions to deal with individual project characteristics make an all-encompassing standardised contract on an international basis unrealistic. However, there is merit in focusing on contractual provisions that are likely in all PPP contracts such as force majeure, step-in rights, termination rights, and dispute resolution alongside the EFSR proposal. The World Bank Group with support from the GIF and other development partners developed the [2019 Guidance on PPP Contractual Provisions](#) to provide a standardised approach to these essential provisions in PPP contracts. These efforts also address themes such as environmental and social issues, and climate change in the context of PPP contracts. Looking ahead, MDBs and regional development banks’ use of “best practice” promotion would lower barriers for private sector investments – though ultimately a shared public-private understanding to shape market practice remains crucial.

Large and complex infrastructure projects in any country are time consuming and costly for host governments to prepare and bring to market. This situation is particularly pronounced in EMDEs, where public funds and capacity are more constrained. The standardisation of PPP contracts thus not only reassures investors with regards to due diligence, but also increases efficiency of project preparation and market delivery for governments. In addition, standardised contracts enable loans to be packaged together more easily. Such an approach increases the overall size of an investment opportunity and promotes diversification within a single transaction, which helps to both attract private investments and strengthen investor rights. Despite this, it is important to recognise that although contracts can be standardised, not all underlying risks can be standardised to the same degree, requiring the need for credit enhancement at the asset-level.

Scaling Solar: Mobilising Private Investment in Solar Projects Through Standardised Approaches

[Scaling Solar](#), through the International Finance Corporation (IFC), is a “one-stop shop” programme for EMDE governments to rapidly mobilise private investment in grid-connected solar projects at competitive tariffs. The programme brings together a suite of World Bank Group services under a single engagement based on a standardised approach to create viable markets for solar power in each client country. Templates are offered for all processes and documents to enable rapid preparation, tendering, and financial close. Balanced, bankable documents can be offered to bidders on a non-negotiable basis with the comfort of pre-approved financing available to all suitable bidders. Tenders are designed to attract competition among top-tier investors and minimise resulting tariffs.

Action Area 3: Increase Use of Credit Enhancement Products

Key Messages

- Given the longer time-horizons of infrastructure assets, ensuring that such assets are managed for risk over the long-term and take into account the asset-liability matching considerations of institutional investors are critical to mobilising greater private investment in infrastructure.
- The COVID-19 pandemic has brought into focus the struggle EMDE governments face in obtaining and maintaining an investment-grade sovereign rating; however, the strategic use of credit enhancement products can help mobilise private capital by de-risking investments.
- The provision of risk mitigation tools, including the use of credit enhancement products, optimises the risk-return profile for institutional investors and enhances the overall affordability and bankability of infrastructure assets.

Channelling institutional dollars into sustainable, high-quality infrastructure requires that such projects are structured to meet the investment preferences and risk appetite of institutional investors. Institutional investors – including pension funds, insurers, and other asset owners – desire stable returns and have long-term investment goals, such as the funding of long-dated liabilities. Therefore, ensuring assets are managed in line with long-term horizons is critical to achieving institutional investment goals, which in turn ensures financial support for the assets. COVID-19 has put into stark relief the importance of managing long-term risk; already, there are examples across developed markets demonstrating how the pandemic has put stress on the cashflow stream, particularly affecting certain assets such as airports and railways affected by strict lockdown measures. However, the long-term and essential nature of such assets to both society and the economy nonetheless ensures that investors are willing to pump additional cash into the investments to provide needed support to the assets.

The Renewable Energy Independent Power Procurement Programme (REIPPP): Promoting Locally Designed and Standardised Renewable Energy PPPs

The REIPPP – developed by South Africa's Department of Energy – is a competitive tender programme intended to facilitate private investment in grid-connected renewable energy generation in South Africa. REIPPP is structured as a public procurement programme that allows independent power producers to submit cost-competitive bids – through an open, transparent, and standardised request for proposals process – to design, develop, and operate large scale renewable energy power plants across the country. The REIPPP has helped to create the platform through which the private sector can develop renewable energy projects in South Africa and enter into power purchase agreements with the state owned utility, Eskom. Since its establishment, the REIPPP has procured more than 100 projects from five bidding round windows, with further windows expected to be announced in the future. The projects are located across the country, leveraging a variety of renewable energy technologies, including: biomass; landfill gas; hydro; solar (concentrated solar power and photo voltaic); and onshore wind.

Action Area 3: Increase Use of Credit Enhancement Products

Additionally, institutional investors are required under applicable local regulatory environments to safeguard returns in order to fund future liabilities, which is achieved by directing capital into investment-grade debt securities. There is, however, an increasing trade-off between investing in investment-grade securities and generating income from such investments. The COVID-19 outbreak has pushed many central banks across developed economies with available monetary space to reduce target interest rates, as well as begin or step up asset purchases through quantitative easing programmes. This, alongside the rising fiscal debt burden from the astonishing fiscal packages deployed in these economies to provide support to households and businesses, will result in the current low rate environment persisting for a long time to come. Central bank activism has also expanded into the corporate bond realm across a number of advanced economies in response to the COVID-19 induced liquidity crunch of 2020. Institutional investors therefore face a challenge in their search for yield across many developed economies and will be increasingly looking for “alternative” investment opportunities to traditional asset classes to generate additional return, diversify portfolios, and provide stable, long-term cash flows. Providing opportunity for higher returns, EMDE infrastructure is increasingly emerging as an attractive asset class for institutional investors.

Despite potentially attractive returns, macroeconomic and political uncertainty in EMDE markets often impacts the quality and bankability of infrastructure projects. Lacking capacity and resources, EMDE governments are often constrained by their sovereign ratings and are unable to address political and regulatory risks, rendering it difficult for rating agencies to give investment-grade ratings. According to *S&P Global Ratings' Industry Top Trends 2020*, sovereign ratings among EMDEs show negative outlooks – particularly in the Middle East and North Africa and in Sub-Saharan Africa.²³ These outlooks have been further compounded by the COVID-19 pandemic; saddled with rising debt, EMDEs have had to reckon with the economic shocks brought on by the pandemic and have been even more hamstrung to meet sovereign bond payments, downgrading credit ratings further across key markets.²⁴ With few investment-grade-rated EMDEs, institutional investors are left with a shortage of risk-adjusted infrastructure investment opportunities that appeal to their balance sheets.²⁵

To attract institutional capital into EMDE infrastructure, MDBs and DFIs should expand the use of risk mitigation tools and the strategic use of blended finance and credit enhancement products. MDBs and DFIs play a critical role in this regard by serving as intermediaries between EMDE governments and private sector investors – equipped with the tools to support policy-setting and institutional reform efforts with governments to reduce market risks, build bankable infrastructure pipelines, and develop and execute risk mitigation instruments.²⁶ As noted in a 2017 outlook report from Moody's, “MDBs are in a unique position to provide...financing support that will change the balance of risk and reward sufficiently to attract private sector capital to infrastructure investment opportunities in developing countries.”²⁷ The strategic role of MDBs and DFIs in the provision of credit enhancements has also been reinforced by the G20 Eminent Persons Group (EPG), which identifies MDB credit enhancements as a more efficient use of their capital relative to direct lending.²⁸

²³ Roberto H. Sifon-Arevalo, *Global Sovereign Rating Trends 2020: Sovereign Debt Buildup Countries*. S&P, 2020.

²⁴ Soliman, M., and Campos, F., *The day after COVID-19 and saving emerging markets*, The Atlantic Council, May 2020.

²⁵ *EM Compass: Crowding in Capital Attracts Institutional Investors to Emerging Market Infrastructure Through Co-Lending Platform*, IFC, 2018.

²⁶ *Better Finance Better World: Consultation Draft of the Blended Finance Taskforce*, Blended Finance Taskforce.

²⁷ Andrew Vitelli, *MDB-backed credit enhancement plays growing role*, Infrastructure Investor, 2017.

²⁸ G20 Eminent Persons Group report on Global Financial Governance: G20 Eminent Persons Group on Global Financial Governance, October 2018.

Action Area 3: Increase Use of Credit Enhancement Products

Particularly against the backdrop of the COVID-19 pandemic where public budgets are even more constrained, the provision of credit enhancements not only mitigates risks to investors, but also provides a pathway to enhance the overall affordability of infrastructure assets – thereby helping EMDEs make more efficient and cost-effective investments in needed infrastructure. Risk mitigation instruments such as guarantees are particularly well suited for mobilising resources because they enable MDBs and DFIs to strategically de-risk investments while crowding in private investment. The strategic use of guarantees – largely offered by MDBs in the form of partial credit guarantees and partial risk guarantees²⁹ – can provide lower borrowing costs and longer loan tenors to borrowers, and cover potential payment-related, counterparty, regulatory, and political risks, among others.³⁰ In addition, the maturity of guarantees is usually considerably shorter than with the traditional long-term MDB loans, allowing MDBs to recycle their equity capital more quickly into new infrastructure projects.³¹

The GIF Downstream Financing Window (DFW): Reducing Private Investment “Bottleneck” Risks through Credit Enhancement Instruments

Although there are various risk mitigation instruments provided by different organisations in the market, there remain important risk mitigation gaps that hamper projects from accessing private finance. As such, the DFW aims to fill such gaps by making available patient, greater risk-taking capital, which will allow MDBs and other DFIs to avail risk mitigation products that would otherwise not be offered on their balance sheets. By doing so, the DFW’s suite of credit enhancement instruments will complement – not crowd out – existing instruments and provide more comprehensive solutions to address major “bottleneck” risks that hamper private investment. As such, the DFW targets the following three initial instruments: (1) a counterparty risk cover facility to mitigate payment risk of perceived less-creditworthy public entities by providing liquidity to prevent defaults and first-loss risk coverage; (2) a foreign exchange liquidity facility to help manage foreign exchange risk by covering short-term impacts of nominal exchange rate fluctuations with appropriately sized liquidity to cover temporary cash flow shortfalls; and (3) a contingent refinancing facility to address the challenge of raising long-term commercial debt for infrastructure projects by providing a conditional refinancing option for short-term loans. Institutional investor capital – which is ideally suited to infrastructure given long-term investment horizons – will serve as a critical segment of investors to mobilise through the DFW’s instruments. To remain market responsive over time, the DFW will adapt its offerings or provide additional instruments based on market-led demands.

²⁹ A partial risk guarantee covers an obligation triggered by a specific event, while a partial credit guarantee may be called once credit obligations have stopped being paid.

³⁰ Pereira dos Santos, P., Kearney, M., *Multilateral Development Banks’ Risk Mitigation Instruments for Infrastructure Development*, Inter-American Development Bank, 2018.

³¹ Humnphrey, C., Prizzon, A., *Guarantees for Development: A Review of Multilateral Development Bank Operations*, ODI, 2014.

Action Area 3: Increase Use of Credit Enhancement Products

Despite the potential attractiveness of these instruments and their effectiveness in mobilising private resources, overall usage has been relatively limited. According to private estimates, guarantees represent only 5 percent of MDB operations, although they account for 45 percent of total private resource mobilisation. The main conclusion from a recent analysis is that, while MDBs seek to increase the use of guarantee products as a viable path to leverage private investment, their business models can impose significant limitations on the further use of guarantees. To maintain their high credit rating, MDBs often employ a conservative approach to guarantees by minimising the number of under-collateralized guarantees outstanding with low capital allocations on their balance sheets.³² On the demand side, private investors have contended that MDB guarantees have struggled to deliver desirable risk-adjusted outcomes. Lengthy negotiation and bespoke structuring, lack of flexibility and transferability, high financial costs, and partial risk coverage often associated with MDB guarantees hinder the overall attractiveness of these instruments.³³ Creating off-balance sheet vehicles to offer guarantees has been proposed as an option, as highlighted in the EPG report. At the same time, MDBs also appear interested in expanding the use of guarantee products on their balance sheets as an enabler of private investment.

GuarantCo: Mitigating Infrastructure Project Risk Through Local Currency Credit Enhancement Solutions

GuarantCo was established as part of the Private Investment Development Group (PIDG) to mobilise local currency contingent credit solutions, primarily guarantees, to support projects and companies in order to raise debt financing for the development of infrastructure in lower income countries in Africa and Asia. GuarantCo provides a variety of contingent products that may be required for a particular infrastructure project including: partial credit and partial risk guarantees; first loss guarantees; tenor extension or liquidity guarantees; and joint guarantees or counter guarantees. These guarantees are structured to protect lenders and investors, providing debt in the event of a loan default caused by the borrower. Since its establishment in 2005, GuarantCo has provided credit enhancement solutions for 55 transactions in 22 countries, unlocking USD 5.6 billion in investment opportunities and improving access to infrastructure for 43 million people.

³² Perera, O., Uzsoki, D., Wuennenberg, L., *Credit Enhancement for Sustainable Infrastructure*, International Institute for Sustainable Development, 2018.

³³ Pereira dos Santos, P., and Kearney, M., *Multilateral Development Banks' Risk Mitigation Instruments for Infrastructure Development*, Inter-American Development Bank, 2018.

Action Area 4: Create Aggregation Platforms

Key Messages

- EMDE infrastructure pipelines primarily comprise individual, smaller volume transactions that are not ideally suited to institutional investors in search of long-term, investment-grade assets with large ticket sizes.
- Aggregation platforms, which securitise several smaller and/or below-investment-grade assets into a single, pooled vehicle, can improve the risk-return profile and overall financial attractiveness to institutional investors.
- Over the short-term, EMDE governments can package existing, brownfield infrastructure projects on a domestic or regional scale; over the longer-term, EMDEs can warehouse greenfield assets in existing vehicles and aggregate them over time so that the revenue flow from greenfield and brownfield assets can be pooled.

While bankable, sustainable, high-quality infrastructure pipelines are a critical component in mobilising private capital, infrastructure projects must be well suited to the capital deployment preferences of targeted investor segments. Institutional investors typically own or manage large asset bases, preferring to deploy large amounts of capital into a single transaction to reduce overall costs. However, EMDE infrastructure pipelines often comprise individual infrastructure projects and are largely driven by increased infrastructure needs concentrated at the municipal level – according to the World Bank’s *2019 Private Participation in Infrastructure* report.³⁴ While recognising the growing need for more infrastructure investment at the city level, such projects tend to be smaller – diverging from the preferences of institutional investors, who typically look for long-term, liquid, investment-grade assets with significantly large ticket sizes.³⁵

While individual infrastructure projects often lack the big ticket size that institutional investors typically require, aggregation platforms – which pool several smaller and/or below-investment-grade assets into a single securitised vehicle – can improve the risk-return profile and overall financial attractiveness to institutional investors. Such an approach increases transaction sizes, improves the liquidity of long-term assets, diversifies risks, and enhances the underlying creditworthiness of infrastructure assets.³⁶ Rather than executing infrastructure projects on a bespoke, deal-by-deal basis, aggregation can multiply private capital and increase the MDBs’ overall lending capacities.³⁷ The potential for MDBs to securitise infrastructure assets has already gained traction and had been brought forward as a proposal by the G20 EPG as a key driver to mobilise private investment. Through their ability to influence governments and as a result of their multilateral ownership, MDBs are uniquely positioned to manage risks and provide credit enhancement products. In efforts to promote the G20 “Infrastructure as an Asset Class” agenda and optimise their respective balance sheets, MDBs will play a central role in pushing for securitisation as a way to attract institutional investors to finance infrastructure assets.

³⁴ *Private Participation in Infrastructure (PPI) 2019 Annual Report*, PPIAF, 2019.

³⁵ *Private Participation in Infrastructure (PPI) H1 2019*, PPIAF, 2019.

³⁶ *Better Finance Better World: Consultation Draft of the Blended Finance Taskforce*, Blended Finance Taskforce.

³⁷ These factors were also highlighted by the most recent G20 Eminent Persons Group report on Global Financial Governance: G20 Eminent Persons Group on Global Financial Governance, October 2018.

Action Area 4: Create Aggregation Platforms

EMDE governments, through national development banks, can package existing, brownfield infrastructure projects on a domestic, or potentially regional scale, and provide credit enhancements as needed to increase the overall risk profile of the underlying assets. Investments in operational infrastructure assets, such as PPP projects, can offer investors such as pension fund managers the opportunity to earn an attractive yield alongside the benefit of stable capital values derived from long-term, fixed-price contracts from EMDE governments that match their own long-term liabilities. However, given that governments and concessionaires cannot unilaterally change the underlying contracts or overall structure of existing infrastructure projects, finding a viable, commercially attractive pool of infrastructure assets to bundle can be a challenge. Identifying a pool of brownfield infrastructure assets in need of rehabilitation and/or expansion can provide an entry point for EMDEs to play a more substantial role in the aggregation process, however credit enhancement may well be required to sufficiently de-risk the assets and, in turn, make the pool more attractive to investors. For a longer-term play – but for which immediate action is needed – EMDEs can warehouse “first generation” (greenfield) assets in existing vehicles and aggregate them over time so that the ultimate stock of brownfield assets and revenue flow from first-generation assets can be pooled and credit-enhanced, as needed. A critical aspect for the “first generation” assets is to ensure that such projects are bankable, sustainable, and as standardised as possible in the first instance.

Table 2:
Examples Overviewing the Benefits of Aggregation Platforms

| Benefit | Example | Example Description |
|--|--|---|
| 1. Improve financial attractiveness | Bayfront Infrastructure Management’s securitisation platform ³⁸ | Building on Clifford Capital’s success of the first securitisation of infrastructure and project finance loans in the Asia-Pacific region through its 2018 USD 458 million take-out facility by Bayfront Infrastructure Capital, this securitisation platform acquires performing infrastructure loans from banks across Asia. It was reported earlier in 2020 that the warehousing vehicle would combine loan portfolios from more than 20 international banks into diversified pools with the acquisitions, warehousing, and monitoring of loans done by Bayfront Infrastructure Management. |
| 2. Expand accessibility to infrastructure as an asset class | International Finance Corporation’s (IFC) Managed Co-Lending Portfolio Program (MCP) | The programme allows investors, such as Swiss Re, which partnered with IFC in 2018, to pledge capital upfront, which IFC then allocates to eligible deals alongside its own capital as per the terms of the agreement. The MCP builds a loan portfolio for an investor that mirrors the portfolio IFC is creating for its own account – akin to an index fund. This enables investors to increase exposure – or get first-time entry – to infrastructure as an asset class without needing the breadth of in-house expertise which would otherwise be necessary. In addition, IFC provides first-loss coverage on the portfolio by taking a junior tranche so as to give investors investment-grade exposure. |
| 3. Promote innovative financing | African Development Bank’s (AfDB) Room2Run (R2R) | Room2Run is a synthetic securitisation of a portfolio of seasoned AfDB private sector loans. The model, which will catalyse private capital in developing markets, may serve as a model for other lenders, help reduce costs, and shorten execution time. R2R will free-up space on balance sheets for further lending by MDBs towards renewable energy projects. |
| 4. Support asset recycling | FONADIN’s asset recycling ³⁹ | The GIF is working with the World Bank to support Mexico’s national infrastructure fund issue debt backed by revenue flows from toll road projects, with the potential of a USD 500 million credit enhancement from the World Bank. The debt issuance proceeds will be used to finance the development of municipal water and sanitation projects, urban transport, and toll road infrastructure projects through FONADIN 2.0. |

³⁸ Bayfront Infrastructure Management is Clifford Capital’s lending and origination platform. The securitisation platform was a collaboration between Clifford Capital and the Asian Infrastructure Investment Bank.

³⁹ FONADIN is Mexico’s national infrastructure fund.

Action Area 5: Enhance Integration and Disclosure of ESG Alignment

Key Messages

- For EMDE governments, incorporating and reporting on ESG considerations throughout the infrastructure project lifecycle not only sends an important signal to the market – which has increasingly embraced ESG as a key factor in investment decision-making – but, at the asset-level, makes infrastructure programmes and projects more resilient and sustainable over the long-term.
- Sustainable infrastructure that is informed by ESG factors is more capable of withstanding external shocks – such as the effects of climate change and other hazards – optimising value for money for both end-users and investors over the asset lifecycle.
- EMDEs must deepen ESG and climate-related reporting standards and ensure that their approach to sustainability is aligned to the broader market; likewise, institutional investors must adopt and adhere to sustainability frameworks to ensure that ESG factors are rigorously analysed to facilitate more informed due diligence processes and investment decisions.

Reflecting increased investor appetite and the potential for outsized risk-adjusted returns, sustainable investment assets – encompassing ESG considerations – have grown considerably over the past few years, reaching more than USD 30 trillion in 2018 according to the Global Sustainable Investment Alliance.⁴⁰ The share of institutional investments in sustainable assets is roughly 23 percent of AUM, where sustainable investing is defined as an investment approach that considers ESG factors in portfolio selection and management. Infrastructure assets have the potential of increasing the supply of ESG investments available to institutional investors.

FAST-Infra: Building the Market for Sustainable Infrastructure Assets

The “Finance to Accelerate the Sustainable Transition-Infrastructure” (FAST-Infra) initiative aims to close the trillion-dollar sustainable infrastructure investment gap, with urgency, by transforming sustainable infrastructure into a mainstream, liquid asset class. FAST-Infra was conceived in early 2020 by HSBC, Climate Policy Initiative (CPI), IFC, OECD, and the GIF under the auspices of President Macron’s One Planet Lab. Over 50 global entities, representing governments at all levels, the financial sector, investors, DFIs, insurers, rating agencies, and NGOs are actively participating in developing the FAST-Infra initiative. In response to market demand for coherency on ESG aspects of infrastructure, FAST-Infra is working towards establishing a consistent, globally applicable labelling system for sustainable infrastructure assets – a Sustainable Infrastructure label (SI label). An SI label will allow the market to easily signal the sustainability of an infrastructure asset. Investors can trust that their money is going to projects that meet environmental, social, resiliency, and governance criteria and contribute to the SDGs. An SI label will also encourage governments and project developers to embed high environmental, social, resiliency, and governance standards into new infrastructure at the design and pre-construction phases on the grounds that only assets incorporating such standards will obtain the label. The SI label will also attract private finance at the construction stage and institutional investors post-construction. Overall, an SI label envisions the creation of a standardised and scalable framework to identify sustainable infrastructure investment opportunities, thereby facilitating the mobilisation of financial markets to meet the challenges of sustainable infrastructure financing in EMDEs, to help unlock pipelines of projects, and to facilitate the emergence of sustainable infrastructure as an asset class. Alongside the SI label work, FAST-Infra is developing financial mechanisms to mobilise private investment at scale for the financing of labelled projects.

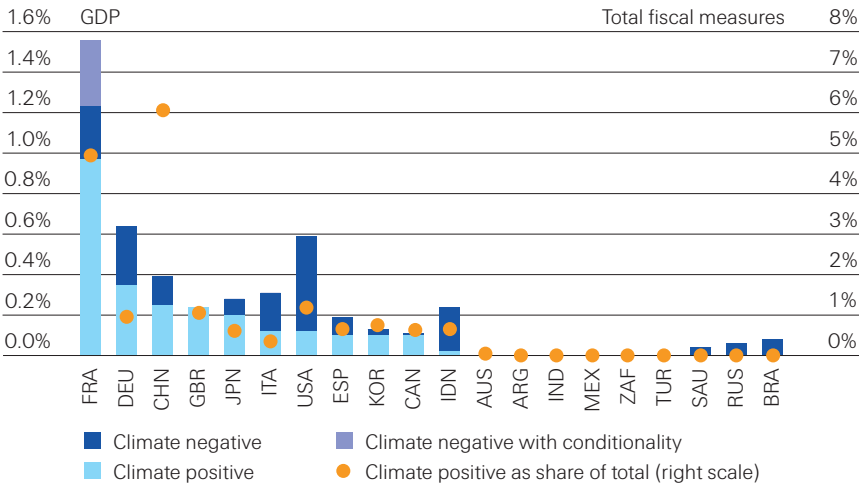
⁴⁰ 2018 *Global Sustainable Investment Review*, Global Sustainable Investment Alliance (GSIA), 2018.

Action Area 5: Enhance Integration and Disclosure of ESG Alignment

While ESG considerations have grown in importance, institutional investors today are presented with the additional challenge of incorporating climate risks into their infrastructure investment decisions. Against the backdrop of an evolving climate crisis, managing environmental factors such as climate resilience and mitigation has become a core component in ESG – that is, taking into consideration the long-term environmental risks and opportunities associated with investments in EMDE infrastructure. For EMDEs looking to bring infrastructure projects to market, incorporating ESG factors at the earliest stages of project preparation has become critical – not only to mobilise needed capital from ESG-oriented investors, but also to create more resilient, sustainable infrastructure projects capable of withstanding future climate-related events. Indeed, sustainable infrastructure can optimise value for money for both taxpayers and investors over the asset lifecycle and can also generate income (particularly for low-income households).⁴¹ Furthermore, sustainable infrastructure has the ability to mitigate greenhouse gas emissions and contribute to the transition to a low-carbon economy.

Fiscal policy globally has rightly been focused on addressing the economic crisis induced by the pandemic. As we emerge from the health crisis, attention needs to turn towards climate-related risks. Investment needs for mitigation and adaptation to climate change remain substantial and crucial, and even more so now that the COVID-19 crisis has highlighted the need for transition to more resilient pathways. The greenness of fiscal responses globally has varied (see Figure 4 for the G20 responses). As policies shift from crisis management to recovery, there is a huge opportunity for public spending into ESG-compliant infrastructure to act as a catalyst for private capital flow into such projects.

Figure 4: Climate Relevance of Fiscal Measures in the G20 Related to the COVID-19 Crisis



Note: Measures are categorised into positive and negative policy “archetypes,” based on the climate relevance of specific activities. A similar methodology is applied to that of the IMF in the Greenness of Stimulus Index.

Source: *Fiscal Monitor*, IMF, October 2020.

⁴¹ Martin Dietrich Brauch, *Contracts for Sustainable Infrastructure: Ensuring the economic, social and environmental co-benefits of infrastructure investment projects*, IISD Report, 2017.

Action Area 5: Enhance Integration and Disclosure of ESG Alignment

To demonstrate both the ESG and financial value of investments in infrastructure, EMDEs must enhance and deepen ESG and climate-related reporting standards, as well as monitoring frameworks that are benchmarked to the SDGs, Paris Agreement, and other sustainable development considerations.⁴² More forward-leaning investors have already created and adopted explicit sustainability frameworks integrating time-tested standard practices to ensure that ESG factors are rigorously analysed during investment due diligence, which in turn enables them to make well-informed decisions. One of the most widely adopted frameworks, the UN Principles for Responsible Investment (PRI),⁴³ outlines six core principles on how to integrate ESG considerations into investment decision-making, including how each principle can be applied to direct and indirect infrastructure investments. The principles, to which signatories have committed, range from incorporating ESG issues into the investment analysis (e.g. consider the ESG track record of the asset), to appropriately disclosing ESG issues encountered.^{44, 45} The UN PRI, among other initiatives in the market, provide a roadmap and clear regulations on how to direct private investment in ways that can generate positive ESG outcomes while still generating the risk-adjusted financial returns that investors seek. For institutional investors interested in directing capital into needed infrastructure, ensuring ESG compliance through robust regulations is crucial. Without strict regulatory implementation, institutional investors risk entering a “climate Minsky moment.”

The Aligned Set of Sustainability Indicators: Creating a Standardised Approach Towards ESG Integration and SDG Alignment

The Public-Private Investment Advisory Facility (PPIAF) of the World Bank is co-leading an initiative with the support of the GIF, EBRD, and the Inter-American Development Bank (IDB) to establish an “Aligned Set of Sustainability Indicators” (ASSI). The ultimate goal of the ASSI is to improve the mobilisation of private capital towards the delivery of sustainable, high-quality, and resilient infrastructure projects in EMDEs with an emphasis on LDCs. The initiative focuses on the ESG aspects of sustainability and ensures alignment with the SDGs. It represents a collaboration between leading international sustainability standard setters (SuRe by Global Infrastructure Basel, Envision by the Institute for Sustainable Infrastructure (ISI), IS-Scheme by the Infrastructure Sustainability Council of Australia (ISCA), CEEQUAL by BRE, and GRESB’s rating system) to develop a harmonised set of sustainability indicators. These should be incorporated into infrastructure projects as early as possible in the lifecycle to deliver sustainable outcomes. Once finalised, the ASSI is intended to be made available as a public good.

⁴² *Better Finance Better World: Consultation Draft of the Blended Finance Taskforce*, Blended Finance Taskforce.

⁴³ *Primer on Responsible Investment in Infrastructure*, UN PRI, 2018.

⁴⁴ Eighty-two percent of PRI’s direct infrastructure investor signatories have a dedicated responsible investment policy for infrastructure. For example, Swiss Re now invests close to 100 percent of its assets in environmental, social, and governance benchmarks.

⁴⁵ *Responsible Investments – Shaping the Future of Investing*, Swiss Re, 2017, and the follow up *Responsible Investments – The Next Steps in Our Journey*, Swiss Re, 2018.

Swiss Re's Approach for Incorporating ESG Criteria into Investment Decisions

In terms of investor methodology, Swiss Re's approach to ESG integration when investing in infrastructure assets is focused on three principles:

1. Enhancement – Enhance the investment process by consistently integrating ESG aspects. This includes the execution of an ESG Letter that formalises the commitment to ESG integration on the part of the external manager. Potential transactions are then screened by considering the three ESG dimensions: environmental, social, and governance, each entailing specific topic areas – e.g., climate and environmental protection and resource efficiency for the “E.”
2. Inclusion – Focus on themes. Within the infrastructure mandate, the inclusion principle ensures a strong focus on renewable energy and social infrastructure.
3. Exclusion – Exclude certain sectors based on the Internal Sustainable Risk Framework. An example is the avoidance of investments relating to thermal coal.

Conclusion

Infrastructure serves as the backbone of societies across the globe – connecting communities to jobs, markets, and crucial services. A significant economic multiplier, infrastructure not only addresses present-day economic conditions and service needs, it also promotes long-term resilience against the effects of climate change and other future global shocks, including public health crises and economic recessions. While the case for infrastructure investment is a well-trodden path, the infrastructure investment gap has nonetheless continued to widen. Particularly in EMDEs, strained public budgets have rendered governments unable to meet the growing need for infrastructure investment – which has been further exacerbated by the economic aftershocks brought on by COVID-19.

As EMDEs begin to stabilise and recover from the COVID-19 shock, mobilising private investment into high-quality, sustainable infrastructure will be critical in promoting long-term, sustainable economic development. It is therefore essential to act now to unlock some of the USD 80 trillion of institutional capital. Accessing this pool of capital, however, can only happen if the right mechanisms are in place. For EMDE governments, this requires dedicating resources to build robust pipelines of bankable, high-quality infrastructure programmes and projects, adopting measures to improve standardisation of contracts and other transaction documents to facilitate the investment process, and creating aggregation platforms capable of promoting infrastructure as a viable asset class. Attracting institutional capital also hinges on MDBs and DFIs – which often play an important intermediary role between governments and the private sector – to leverage credit enhancements and other risk mitigation instruments to improve the overall risk-return profile of emerging market infrastructure. Finally, it requires that EMDE governments and institutional investors alike integrate ESG screening, disclosure, and reporting standards that align with the SDGs, Paris Agreement, and other global commitments. Table 3 provides an overview of the action areas put forward in this paper with the corresponding demand- and supply-side challenges they address.

Bridging the sustainable infrastructure investment gap is a collective effort. It requires that EMDE governments, MDBs, DFIs, and institutional investors unite around a shared objective: identifying innovative pathways and deploying the right set of tools to promote sustainable, quality infrastructure investment in the markets that need it most. By understanding the barriers that have traditionally hampered infrastructure investment, as well as action-oriented solutions to overcome these obstacles, institutional investor capital can play a powerful role in bridging the infrastructure investment gap.

Table 3:
Overview of Challenges and Action Areas to Mobilise Institutional Capital into EMDE Infrastructure

| | Current Challenges | Action Areas to Facilitate Investment |
|--------------------|---|---|
| Demand Side | <ol style="list-style-type: none"> 1) Lack of bankable projects 2) Elevated transaction costs 3) Fear over investment quality stemming from macroeconomic and political uncertainty 4) Small ticket sizes relative to transaction costs 5) Limited transparency regarding ESG compliance | <ol style="list-style-type: none"> 1) Expand infrastructure pipeline development through high-quality project preparation 2) Promote standardisation of new/greenfield projects 3) Increase use of credit enhancement products 4) Create aggregation platforms 5) Enhance integration and disclosure around ESG alignment |
| Supply Side | <ol style="list-style-type: none"> 1) Low capacity to prepare infrastructure projects that are attractive to private investment 2) Constrained public funds and capacity 3) Sub-investment-grade sovereign ratings 4) Constrained capacity to bundle infrastructure assets to increase overall ticket size 5) Lack of resilient, sustainable infrastructure projects capable of withstanding future climate-related events | |

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GIF Description:

The Global Infrastructure Facility (GIF) is a G20 initiative with the overarching goals of increasing private investment in infrastructure across emerging markets and developing economies and improving services in ways that contribute to poverty reduction and equitable growth aligned with the SDGs. The GIF provides funding and hands-on technical support to client governments and multilateral development bank partners to build pipelines of bankable sustainable infrastructure investments and has designed a suite of blended finance solutions to facilitate private investment. The GIF enables collective action among a wide range of partners – including donors, development finance institutions, country governments, together with inputs of private sector investors and financiers – to leverage both resources and knowledge to find solutions to sustainable infrastructure financing challenges.
www.globalinfrastructure.org

Swiss Re Description:

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