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Infrastructure to 2030: Growth, Innovation and Finance

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As Chairman of the Investment Banking Group of Macquarie in Europe, I was privileged to be a sponsor from the private sector on the Steering Group of this important OECD Futures Project on Infrastructure Needs.

It should excite a lot of interest because investment in infrastructure has got the stock markets very excited.

From being the Cinderella sector of the markets, infrastructure is now seen as an attractive new asset class.

Its attraction comes from infrastructures long-life, its often essential services, inflation-proofed regulation and pretty predictable cash flows.

- Low risk, steady yield and possible growth in value place it somewhere between Equity and Bonds in the portfolios of institutional investors.

Pension funds are particularly interested because the long-life of infrastructure runs in parallel with their decades-long liability horizons.

- Solid assets attract cautious capital
- The citizens providing for their pensions invest in the essential services for citizens.

This mutual interest is also reassuring for the policy makers, the politicians who are caught in a fiscal squeeze.

At elections, voters are making their priorities clear - more education, better health services, more age care, stronger security.

The electorate wants more social investment but is also increasingly reluctant to pay more taxes.

So even in good times, long-term infrastructure is being squeezed. As our Report shows, while social expenditure as a share of national investment has risen by one-third, capital formation has fallen by about one-quarter.

One conclusion of our report is beyond doubt - the growing need for infrastructure investment will run far beyond the capacity of governments alone to fund it.

That means traditional means of funding must be enhanced by private sector investment to support essential community services.

As we show, the global demand for investment over the next 25 years is measured in trillions - for transport, for energy, for water.

And who knows how much we might have to spend to harden our increasingly interdependent Critical National Infrastructures against attacks by terrorists or the impacts of possible climate change.

So where could this extra investment come from?

The report identifies one possible source:

- The \$18 trillion of pension funding in the OECD countries.

The pensions industry has been impressed by the performance of the dedicated infrastructure funds which have grown rapidly in recent years.

Some of the larger pension funds are now defining infrastructure as a separate asset class and assigning it increasing percentages of their portfolios.

Just one per cent of \$18 trillion could see about \$200 billion earmarked for infrastructure by private investors.

The next question is - could the public sector take advantage of this opportunity.

In the last year alone, tens of billions have been raised for new infrastructure funds. Combine that with easy credit and prices are pushed up as too much money chases too few infrastructure assets.

The challenge therefore is for the public sector to find new business models or create partnerships that will open up channels to the areas of infrastructure most starved of investment.

It won't be easy for the politicians. Over 100 countries have privatised assets with a total value of about \$1.4 trillion. Many of the privatisations have been successful but selling off state assets is usually controversial and not an easy option for the faint-hearted.

The compromise which is calculated to ease the political process is the PPP - the Public Private Partnership.

The PPP, and its variants, is increasingly popular internationally as a mechanism to engage private expertise and capital.

Our report illustrated the many forms PPP can take, the problems that can develop, and the lessons learned. Particularly in negotiating the transfer of risk and protecting public sector interests.

The UK with almost 900 PPP and Private Finance Initiatives started in the past ten years, and deals closed totalling almost £50 billion has analysed its extensive experience and the conclusions on the UK Treasury website are worth consulting for lessons learned.

Our Report concludes that the major role in infrastructure investment globally will still have to be played by governments investing public money.

But the same governments, if they want to attract significant private investment, must create the conditions required by investment institutions, namely more stable legal and regulatory frameworks.

The absence of political stability and sound governance is still the biggest barrier to investment in the developing countries where, of course, the need is greatest for water supply, for energy supply, for sustainable environments and transport systems.

I trust that "Infrastructure to 2030" will be reflected upon not just by the policymakers but will also be widely read across the business community.

I hope, too, the efforts of Macquarie and the other corporate sponsors of this important Report will encourage increasingly productive partnerships of the public and private sectors in providing better infrastructure services - because infrastructure underpins almost everything else.