A forum in Hong Kong was told the Belt and Road Initiative needs to come up with new funding mechanisms to bridge the huge infrastructure gap across the region. The one-day forum, on Oct 15, was organized by the Hong Kong Institute of Bankers and the Asia-Pacific Structured Finance Association. ROY LIU / CHINA DAILY ASIA WEEKLY

Securitization to push BRI

Financial technique for channeling credit flow can generate more capital for Belt and Road, forum hears

By DAVID HO in Hong Kong
For China Daily Asia Weekly

China's signature Belt and Road Initiative is five years old, but there is still much to be done about financing infrastructure and other projects under the far-reaching plan. A critical component in freeing up capital for BRI projects could be securitization, say experts.

Securitization is a financial technique that makes it possible to transform a pool of illiquid assets into tradable securities. In other words, through securitization, assets like mortgages held by banks can be turned into shares for investors to buy. The process would allow countries to tap enormous pools of funds held by individual investors.

"Securitization provides a valuable conduit for channeling credit flow between suitable borrowers and lenders. It is becoming more relevant and important in China," said Susie Cheung, a co-convener of the Asia-Pacific Structured Finance Association (APSA).

"Those of us in Hong Kong should carry on with it, as it is a very effective weapon and useful technique to provide relevant capital."

Cheung's views were shared by other speakers at a forum on infrastructure financing for the BRI. The one-day event was held at the Hong Kong Convention and Exhibition Centre on Oct 15, and organized by the Hong Kong Institute of Bankers and APSA.

James Pedley, a foreign legal consultant with law firm Clifford Chance, agreed that Hong Kong's legal muscle could play a key role in expanding the use of securitization.

"At all stages of an infrastructure project's life cycle, you would need the legal certainty that you would get what you want," said Pedley.

Cheung also called for the establishment of a BRI securitization platform and to develop bankable projects under the initiative as a "BRI infrastructure asset class". Both initiatives could help increase the attractiveness of securitized assets to potential investors.

Peter Burnett, managing director and regional head of Corporate Finance, Greater China and North Asia, with Standard Chartered Bank (Hong Kong), commended the "positive impact" a new tradable asset class could have.

New funding initiatives

And the time could not be better to launch new funding initiatives to fill a rather large infrastructure gap. Infrastructure is vital to fulfill the potential of the BRI.

Michael Camerlengo, Hong Kong-based partner and director of KPMG's Infrastructure Advisory practice, said the infrastructure gap across the region is more significant than initially thought.

"Much of the growth needed is in our own backyard. The gap between current expenditure levels and what is needed based on economic growth actually comes to about $1.4 trillion per annum, and it is growing," said Camerlengo.

He believes the BRI can bridge the gap, but significant funds will be needed over the long term.

"Private capital should make up a large volume of infrastructure expenditure, but it only makes up 20 percent of total capital at the moment. It is currently a minority source in the region and in the Belt and Road as well," said Camerlengo.

More can be done to encourage the flow of private capital into infrastructure.

Camerlengo noted how government incentives can help, looking to examples in his native Australia.

"The Australian government offered the state governments a 15 percent bonus payment on each infrastructure project sold. The asset recycling initiative resulted in 12 major public assets sold, and incentivized A$23 billion ($16.4 billion) in infrastructure investment," said Camerlengo.

He said that institutional investors often look to reviews from credit rating agencies to make their decision. To address the risks that these agencies look out for, it is important to "create business models and project structures that are effective from the outset" .

Among factors he suggests including in the planning stage is an in-depth risk allocation exercise.

Camerlengo was not the only one to discuss risk, which can range from environmental risk to management issues.

Wilfred Lau, a director at engineering and design company Arup Group, spoke at length about the technical risks involved in major infrastructure projects.

"There are four pillars in technical risk reduction. The first is the need for an infrastructure master plan. This will automatically reveal the state of any given project in the future and provide greater certainty to investors," said Lau.

Camerlengo believes the planning stage is the most crucial.

"Planning is very important. It is the single biggest factor stopping more projects from being realized. Most never go beyond an Excel worksheet because of insufficient planning," he said.

And that goes toward future-proofing these projects as well.

"We need to think ahead about what happens if there are demographic changes or structural changes," said Eric Wu, head of Asia Infrastructure Debt at investment management firm BlackRock, about the stability of returns on infrastructure projects.

The second pillar suggested by Arup Group's Lau is a generally acceptable procurement framework for BRI projects.

"There should be standard international contracts. And it should be a quality-based selection rather than fee-based ," said Lau.

In his presentation, Camerlengo concurred with Lau's point. "Contract structures should be easy to follow for all players. The tender process should be free from bias," said Camerlengo.

Ecosystem

The third pillar is an enabled ecosystem for projects. This deals directly with risks.

"Besides the talent involved, the project owners and investors should create an ecosystem to mitigate risks in projects. There is a need to understand risk allocation between different parties at different stages," said Lau.

He advocated the use of digital platforms to share info, report and track progress between all parties. Lau also believes that modular construction, segmental construction, and 3D printing, can be utilized to save time and ensure the quality of a project.

This also calls for a clear dispute resolution process. "This should be negotiated at the start, so all parties are aware of it and can take action if needed," said Lau.

With legal risks at both international and domestic levels, Clifford Chance's Pedley said Hong Kong is "very much in the center of the Belt and Road with the right talent for dispute resolution".

The final pillar would be a structured risk management approach through the lifetime of projects.

"People involved in financing would see risk very differently from an engineer, and vice versa. If they can all come together, then risks can be mitigated better," said Lau.

With better management of risks, securitization can be carried out to bring in more capital for BRI projects.

During a roundtable dialogue to close off the event, Standard Chartered's Burnett said: "Most importantly, the Belt and Road builds financial capacity."

"Securitization will mobilize a new and much bigger pool of institutional capital, and frees up capital on a banker's balance sheet," he added.

Pius Chong, a co-convener of APSA, said the BRI is all about connectivity and socioeconomic engagement to make an impact globally.

"There is a lot to do, and Hong Kong is well placed to play a role in the financing of the BRI. Greater ingenuity will see the BRI supply bankable infrastructure projects.

"The thing is to make them sustainable and beneficial to the people in those countries involved," Chong said.