BY JONATHAN DENIS-JACOB

MAKING INFRASTRUCTURE PROJECTS BANKABLE

Real estate strategies can play a major role in funding infrastructure developments by raising upfront capital or by generating operating revenues

THE biggest problem with financing infrastructure is that these projects are seldom financially viable on their own. After all, infrastructure projects are built first and foremost for the public benefits that they bring about – reduced traffic, improved air quality, economic development – while generating limited revenue. Hence, not enough funds are raised – or at least not enough private investment is readily available – to fund much-needed infrastructure.

Let's face it, investing in a new subway line or funding the construction of power grids in emerging markets is unlikely to set investors' hearts aflutter the way pumping money into a unicorn tech startup would these days.

Nonetheless, such investments are necessary and critical to economic growth, job creation and sustained urbanisation. There is no question that Asia needs more infrastructure, from transportation network to water supply and sanitation, but how will it pay for all that?

A whopping US$20 trillion is needed to fund infrastructure investment in Asia by 2030, according to estimates by the Asian Development Bank (ADB). This works out to an investment of US$1.7 trillion a year – not a paltry sum by any stretch of the imagination. Currently, the region funds only half of that amount every year, with 90 per cent of the financing coming from governments or government-linked agencies.

The yawning funding gap will throttle Asia's growth. There is an urgent need to seek alternative sources of financing to tackle the region's serious infrastructure shortfall.

Colliers International believes that investors, developers and the public sector can more effectively collaborate under win-win conditions to deliver high-quality infrastructure. However, in many cases, the private sector is unwilling to do so as investment returns are often too low, break-even periods are too long, and/or the risk is too high.

The solution is to make infrastructure projects more bankable through various value creation and revenue generation schemes that are attractive to private sector investors. Real estate strategies, in particular, can play a major role in drawing private investments – whether it is by raising upfront capital or by generating operating revenues.

Capital can be raised when a real estate asset is monetised to finance the construction of a new infrastructure. These initiatives include the sale of development air rights above train stations, depots and other infrastructure, land value capture – where the increase in land value from the infrastructure development is recovered and reinvested in the project – as well as land transfer or swaps.

Real estate can also generate long-term income streams to cover operating, financing and maintenance costs, and help to boost the infrastructure project's overall investment yield. These could come from rental revenue from commercial property portfolio as well as licensing agreement from hotel, retail or business park operators on the site, among other initiatives.

THE REAL ESTATE ROUTE

Connectivity and transportation networks are the backbone of growing cities, and they play a catalytic role in economic development. Investment in transportation is a key priority for policymakers in both developed and emerging nations, and they can tap financing from the private sector.

- **Subway:** The ADB estimates that total investments in subway construction will reach US$230 billion in Asia from 2016 to 2030. At an average construction cost ranging from US$100 million to US$500 million per kilometre, mass rapid transit (MRT) projects require multi-billion investments from governments across the region.

Monetising the "land value lift" – the rise in real estate value associated with new transport infrastructure – can help fund subway projects. In the City of Richmond near Vancouver, Canada, the US$25 million Capstan Way Station has been funded entirely via land value capture by development contributions from real estate developers.

In exchange for additional development density, developers contributed about US$6,500 per housing unit towards the construction cost of the station. With the approval of about 7,000 residential units within the area, the required funds were raised within just six years, rather than the 15 years originally anticipated.

In the Asian context, Singapore, Hong Kong, Japan and South Korea are no strangers to land value capture schemes, but these mechanisms have been difficult to implement elsewhere.

- **Airport:** As more airports transform into "airport-cities" and mixed-use environments, airport authorities are now developing comprehensive income generation initiatives beyond aeronautical revenues. Based on Colliers' airport project experience, non-aeronautical revenues now account for 25-40 per cent of total operating revenues in major international airports globally. These include rental revenue from airport-owned commercial/industrial property portfolio as well as from food and beverage (F&B) and hotel concessions.

In the case of Changi Airport in Singapore for example, over 50 per cent of revenue is from non-aeronautical sources – including real estate rental income, F&B and hotel concessions, pay parking, etc. The development of Jewel Changi airport, a mixed-used retail/lifestyle complex developed in joint venture with CapitaLand Malls Asia, is central to the airport's strategy to generate more long-term non-aviation revenue to fund operations, expansion and renovation works.

- **Seaport:** Currently, about 60 per cent of the world's fastest-growing seaborne trade passes through Asia. With global seaborne trade projected to grow at about 3.2 per cent per year until 2022, ports in the region will require substantial investments to increase their capacity and diversify their service offerings. The upcoming Tuas Mega Port in Singapore, for example, will more than double the port's capacity, posing a stiffer challenge to smaller ports in Asia.

Port operators can raise capital and generate income by partnering with the private sector to set up facilities such as warehousing and storage, logistics and distribution as well as a waterfront cruise centre or even free trade zones to attract investment and shipping cargo.

Private sector investors and developers have become increasingly mindful of their roles in advancing social and global challenges in the past decade. Infrastructure development – being an important tool in spurring growth and alleviating poverty – may be one of the issues that matter to their employees, customers and the wider communities.

It can be a viable long-term investment for the private sector if win-win conditions are in place, generating public benefits as expected by governments and communities while offering the possibility of a decent return on investment at an acceptable level of risk for private investors. Real estate strategies could make a particularly big difference in infrastructure financing across Asia if these conditions can be achieved. ■

The writer is associate director, Advisory & Consulting, Colliers International