Lost Decades?

The fortunes of PPIs (private participation in infrastructure) move in line with the health of global finances: Last year, financial and real assets amounting to nearly $29 trillion have been wiped out globally. (MGI Capital Report, 2009). Cross-border flows too have declined by over 80% reversing the fast pace of financial globalization that began in 2002. Compared to $10.5 trillion in 2007, cross-border financial flows plummeted to $1.9 trillion in 2008. A major casualty of financial turmoil usually is private infrastructure and this crisis is no exception. Overall project finance volumes came crashing down by 58% in the 12 months from September 2008. If it was not for the dominance of Indian deals, accounting for a quarter of total global volumes, project finance would have been back to 2004 levels.

It was only recently that investors had begun to return to PPIs after the 1997 Asian financial crisis. According to the World Bank's PPI database, it took nearly a decade to come close to the global private interest in infrastructure achieved in 1997 and yet, the peak of 351 projects closed in 1997 is not surpassed since then. The 1997 crisis impacted PPIs at three different levels: The projects that were in the pipeline remained so for a long time; many projects that were under construction slowed down with significant cost implications; whereas those under operations were put up for re-negotiations on a large scale.

A fundamental difference between the 1997 financial crisis and today is the importance policy makers and politicians alike attach to infrastructure investments. In 1997, PPIs were seen as the only politically acceptable instrument for investing in infrastructure, and hence, at least in Asia, the 1997 crisis led to shrinking fiscal space available for new investments. The governments stepped in much later to reverse the decline in infrastructure investments when PPIs paused. This time, infrastructure, public, private, any infrastructure is seen as the savior of the economy. Private sector's role in infrastructure is supported in almost all countries, be that USA or China, but the actual cash for projects is coming largely from the public purse.

This trend is indeed a worrisome development since the history of PPIs is curiously discontinuous. Different forms of private infrastructure investments were so common in the pre World War I era. For six decades, however, PPIs disappeared until their reemergence in the late 1980s. Are there similarities between the problems being faced by investors then and now? What should be appropriate public policy response to ensure that PPIs continue to remain as alternative model for infrastructure investments?

Posted by Rita Nangia on December 12, 2009