Rethinking the PPP Funding challenge

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Is PPP debt the next emerging asset class? I was struck by this thought following a recent trip to Latin America where I talked to a number of key people involved in public sector financing.

Latin America is increasingly turning to Public Private Partnership (PPP) structures – to fund big infrastructure, energy and health projects. According to the World Bank, 17 countries across Latin America have fully functioning PPP units, and PPP accounts for about 40% of the region's yearly infrastructure commitments.

In many cases, the investment is huge. Take Colombia, the country is engaged in its fourth generation toll road programme (known as 4G for short), which comprises 179 projects. This has already involved some innovative bond issuance.

Peru has big projects in energy and transportation and recently updated the legal and institutional framework for PPP to help create higher quality projects. Argentina's pipeline includes USD 169 billion of road programmes and USD 34 billion in the energy sector.

Boosting regional financial markets

A World Bank report last year made a telling point. Achieving Latin America's PPP potential would require a number of things – including 'boosting project finance capacity and increasing the depth and sophistication of regional financial markets'.

The second half of that, of course, is very much what we at Euroclear seek to do. Both Peru and Argentina, for instance, are on Euroclear's iLink platform, connecting their domestic markets to our ICSD.

Infrastructure is an illiquid market. One way of changing that is to raise funding through the Eurobond market. But to qualify for funding from the regional development banks these deals have to be domestic projects. Regional or multi-development bank involvement is critical as it provides guarantees for other investors.

However, Euroclear's iLink platform helps promote international market in domestic securities. And that opens up a number of possibilities.

One of the challenges is the size of likely issues. Much of the PPP work is put together at the particular ministry level. Individual issues of USD 100 million or USD 150 million are not going to be attractive to big international investors, however keen they may be on taking the country risk.

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But if the funding for several ministries could be brought together or issued as fungible instruments, with ministry of finance support, the scale of the issuance should guarantee the sort of liquidity that would encourage international participation – provided that can come through an ICSD linkage.

To all intents and purposes, these issues would look like quasi-government bonds, with the obvious appeal of a yield pick-up. But size is crucial. It increases the range of options for buyers – such as using the bonds as collateral. And it makes it easier for issuers to issue follow-on tranches.

Aligning with G20 initiative

Moves to create more liquid PPP funding instruments and make them easily accessible to an international investor base would align with a wider initiative from the G20. This seeks to improve the flow and quality of private and public infrastructure projects by establishing a Global Infrastructure Hub, which is intended to share knowledge and help promote projects to a global investor base.

All the above arguments can be applied to other developing nations keen to travel the PPP route in their infrastructure funding. Turkey, for instance, has some USD 300 billion of projects in the pipeline, including a new airport and a tunnel under the Bosphorus. Indonesia is talking of projects worth USD 500 billion.

Those figures give some idea of the potential scale of what could become a new USD 1 trillion-plus asset class for the investing community. That, in turn, could have a dramatic and beneficial effect on funding costs for the developing nations involved, a prize that is surely worth the effort.