

Investing in the nation's future



Major investments are being made in building new infrastructure, and upgrading existing ones, and billions of dollars have started flowing in as new power plants, ports and airports, roads and expressways are being laid out across India. **Aju Joseph** and **N.B. Rao** take a look at the buoyant scenario in the infrastructure sector



For India's growth story to continue unfolding over the next few years, one of the crucial sectors is infrastructure. The Government of India has estimated that at least \$350 billion are needed by the infrastructure sector – including power, surface transport, aviation and ports – over the next five years.

When huge sums are invested in

these core sectors, there will be a spill-over effect, benefitting the entire economy. Economic growth will be catapulted to the 10 per cent-plus category – from the current eight to nine per cent levels – once investments begin happening in the infrastructure sector.

Prime Minister Manmohan Singh recently emphasised the importance of investing in the infrastructure sector. "We

have seen and expect to further see a massive increase in investment, both public and private, domestic and foreign, in our infrastructure," he told an international gathering in Delhi recently. "The institutional architecture for sustaining high levels of investment in infrastructure has been indeed put in place – public private partnerships, systematic bidding systems, viability gap funding and other financing mechanisms and standardised approval procedures. These are already fetching results and to some extent, the increased investment in infrastructure has been a driver of growth as well as demand."

The growth of infrastructure, among others, would involve large inflow of foreign direct investment (FDI), added the Prime Minister.

For a country that achieved eight per cent-plus gross domestic product (GDP) growth consecutively for the last three years, inadequate infrastructure is a blemish. After many years of decelerated growth in various segments of infrastructure, there is now a widespread consensus that efficient and effective infrastructure services is essential to realise the full potential of the growth impulses surging through the economy.

While stepping up public investment, India is actively scouting for private sector participation in infrastructure as the government finds it difficult to provide adequate scale of investment, technical efficiency, proper enforcement of user charges, and competitive market structure. On the flip side, as the recent Economic Survey points out, the complete reliance on private production, without appropriate regulation, is also unlikely to produce optimal outcomes.

"The \$350 billion investment during the 11th Five-Year Plan, beginning 2007, is a Herculean task," notes a Mumbai-based analyst with Infrastructure Leasing and Financial Services (IL&FS). "These investments are expected to be achieved through a combination of public investment, public-private partnerships (PPPs) and exclusive private investments, wherever it's feasible. Investment requirements by 2012 estimated by the Committee on Infrastructure, headed by the Prime Minister, in some of the key sectors include \$50 bil-



FOCUSSED ON INFRASTRUCTURE: Prime Minister Manmohan Singh



LIGHT AT THE END OF THE TUNNEL: The Mumbai-Pune Expressway has proved to be hugely popular

lion for modernisation and upgradation of highways, an equal amount for power sector, \$9 billion for civil aviation, \$11.4 billion for ports, and \$68 billion for the railways," adds the analyst.

While funding long-gestation infrastructure projects remains a major concern, efforts are currently on to build an investor-friendly atmosphere in the country. The government has recently established an infrastructure fund by a special purpose vehicle (SPV), India Infrastructure Finance Company (IIFCL), in a consortium with Citigroup, IDFC and Blackstone.

IIFCL recently sought the Reserve Bank of India's (RBI) approval to enhance its limit for raising overseas funds by \$1 billion. "We are in discussions with the RBI on the issue of the external commercial borrowings' (ECB) limit," says S.S. Kohli, chairman and managing director, IIFCL. "As part of the memorandum of understanding (MoU) signed with the partners, an amount of \$3 billion in debt has to be arranged for the infrastructure

fund. Thus, we have asked the RBI to consider raising our annual ECB limit by \$1 billion from the current \$500 million," he adds.

The plan is to launch a \$5 billion fund soon for financing infrastructure projects in the country. Of this, \$2 billion will be deployed as equity capital while the remaining \$3 billion will be raised through long-term debt with maturities exceeding 10 years. "We will explore opportunities domestically apart from tapping the overseas market for raising long-term debt," adds Kohli.

Another source of funds for infrastructure projects, according to many, is the burgeoning foreign exchange reserves, now topping the \$200 billion mark. "The idea that has been germinating for the last two years is that foreign exchange reserves must be put into use in order to promote investments, especially in infrastructure," says Finance Minister P Chidambaram. "We have a large requirement for resources to finance investments."

According to the Economic Survey, there were 837 projects at the end of June 2006 (each costing \$4.65 million and above) with an estimated investment of about \$84 billion spread over 16 sectors, including atomic energy, civil aviation, power, railways, road transport and highways, shipping and ports, urban development and water resources.

Economists and industry observers have opined that strong, well-recognised linkages exist between infrastructure on the one hand and economic growth and poverty alleviation on the other. "Not only will infrastructure give a fillip to economic growth, but robust economic growth, in turn, will promote investment in infrastructure," says the IL&FS official.

With an acute electricity shortage staring India in its face, the power sector figures on top of the priority list. According to R.V. Shahi, former secretary, Ministry of Power, the sector is likely to receive investments of over \$56 billion during the 11th Plan, during which

a capacity addition of 62,000 MW has been planned.

Some of the strategic inputs that are being considered include greater thrust on power generation from LNG and hydro. While the target for hydel power generation during the 10th Plan was 10,000 MW, it has been raised to 17,000 MW in the 11th Plan.

“The National Electricity Policy of 2005 is emphatic on fully exploiting non-conventional energy sources, mainly small hydro, wind and bio-mass,” says Shahi.

Coal has continued to remain the mainstay of the power sector, with 54.2 per cent of total installed power generation capacity in the country being coal-fired thermal units. The power sector is the major consumer of coal in India, absorbing 78 per cent of the country’s total coal production. As a result, India’s dependence on coal imports from Indonesia, Australia and South Africa is growing by the day.

All the ministry-proposed Ultra Mega Power Projects (UMPPs) of 4,000 MW would be fired by coal, domestic or imported. Nine sites have been identified by Central Electricity Authority (CEA) in nine states for the proposed UMPPs, including 4 pithead sites, one each in Chhattisgarh, Jharkhand, Madhya Pradesh and Orissa, and 5 coastal sites, one each in Andhra Pradesh, Gujarat, Karnataka, Maharashtra and Tamil Nadu.

The Ministry has also issued the approach and guidelines to develop Merchant Power Plants (MPPs). Unlike traditional utilities, MPPs compete for customers and absorb the full market risk. There is no guarantee regarding minimum off-take of their output.

Typically, the risk of a MPP is carried on the balance sheet of the promoter.

MPPs can provide the additional generating reserves that India needs now and will need in the future. They are a product of the restructuring of the electricity industry and fill different niches in the market – some provide steady supplies to a power grid, while others fire up only when demand is at the highest and meet peak loads. Merchant power plants operating competitively help assure that power is produced with efficiency and



POWER THRUST: The power sector absorbs 78 per cent of the country’s total coal production

supplied to locations where it is needed most. MPPs up to a capacity of 1,000 MW would be provided coal linkage, and captive coal blocks may also be provided to merchant power plants in the range of 500–1,000 MW.

The government is actively pursuing public-private partnerships (PPPs) to bridge the infrastructure deficit in the country. Several initiatives have been taken during the last few years to promote PPPs in sectors like power, ports, highways, airports, tourism and

urban infrastructure. “PPP is still a nascent concept in India, and expertise at the level of project authorities, both at the central and state levels, is limited,” says a senior government official. “To promote the PPP programme, all state governments and central ministries have been advised to set up a PPP Cell with a senior level officer deputed as a nodal officer.”

PPP projects involve long-term detailed contracts between government and private parties spelling out the rights



OPENING THE FLOODGATES OF INVESTMENT: Innovative new funding models are being set up to finance mega projects

and obligations of both the contracting parties. Given the complex issues involved, the government has decided to create standardised frameworks based on due diligence rather than evolving agreements on a project-by-project basis.

The agreements will be based on international practices and will create a framework with the right matrix of risk allocation obligations and returns. So far, 29 proposals have been received from different central Ministries for clearance, out of which 15 proposals involving a capital cost of \$1.9 billion have been approved.

State governments across India are also striving to attract funding to develop major infrastructure projects, including metros for major cities, IT parks, state highway projects, and ports and airports.

States like Maharashtra and Gujarat are hoping to attract investors to develop greenfield airports around their major cities – Mumbai, Pune and Nagpur in Maharashtra, and Ahmedabad and Vadodara in Gujarat.

Similarly, many state governments are vigorously pursuing plans for the development of mass rapid transit systems, including metros, for their major cities, following the success of the Delhi Metro.

IT parks are another major infrastructure segment that are attracting huge funding from international companies. The success of southern cities like Bangalore and Hyderabad, in setting up IT hubs has seen other state governments planning similar facilities in their capitals. Both West Bengal and Orissa are now planning software parks and complexes.

According to Dr Debesh Das, IT minister, West Bengal, the state will soon have an IT park focussed on VLSI (very large scale integration) and chip related design firms. The government plans to develop a 100-acre VLSI facility at Kharagpur, home to the Indian Institute of Technology (IIT). Besides Kolkata, the government is also promoting Kharagpur, Durgapur and Siliguri as IT hubs.

The West Bengal government is also selecting a private sector partner for its

proposed 'India Design Centre,' which is coming up at the Electronics Complex in Salt Lake.

The West Bengal Electronics Industry Development Corporation Ltd (Webel), the single window support centre for IT and other high-tech firms investing in the state, is planning to promote IT parks jointly with private sector partners in other cities including Durgapur, Halodia, Kharagpur, Siliguri and Kalyani.

According to Webel, the state – which is the fourth fastest growing one in India – aims to emerge among the top-three IT states in India by 2010. West Bengal aims to account for 15 per cent of India's IT revenue by 2010, and 20 per cent of the BPO (business process outsourcing) revenues.

Infrastructure development has emerged as the buzzword in India, as governments realise the importance of this key sector. Pouring money into the infrastructure sector boosts employment, transforms the economy, and generates millions of dollars in tax revenue, needed to improve social sector spending. 🌈