Better Prospects

Investor confidence gradually returning with various initiatives

While infrastructure financing remained subdued during the past year, stressed advances to the sector declined. Factors hindering the infrastructure sector's stability include land acquisition issues and sizeable cost overruns. Significant announcements from the government and the Reserve Bank of India (RBI) are expected to draw renewed interest from stakeholders. The outlook could improve in sectors like renewable energy, airports and ports from "negative-to-stable" to "stable" during the current financial year, on account of favourable policies coupled with timely revenue realisations. Experts share their views on the infrastructure financing scenario and the way forward…

What have been the key trends in the infrastructure financing sector in the past 12-15 months?

Manish Aggarwal

Traditionally, infrastructure financing avenues have been limited, primarily driven by debt from banks, equity from sponsors, private equity, initial public offer markets and infrastructure funds. Financing was further limited by the slowdown in the economy, policy inaction around segments within the infrastructure space, a high-interest-rate scenario, and a number of execution challenges that led to delays. With the government's focus on the resolution of key issues, public spending in infrastructure and structural reforms, we have been witnessing a renewed engagement by investors in the sector.

The past few months have witnessed an increase in credit offtake from banks and non-banking financial companies in sectors such as renewables, transmission and ports. The bond market has also witnessed increased traction, especially in the transmission and highway sectors. Capital markets are yet to see large infrastructure-led activity.

Ramesh Bawa

The government and RBI have been working very hard the past 15-18 months to support the financing requirement of the infrastructure sector. Since the exposure level in public sector banks has already reached the maximum level, financing by them has not been to the extent required. However, with the extensive efforts of the government and RBI, infrastructure projects have been able to attract investments through foreign direct investment (FDI), the public-private partnership (PPP) model, infrastructure debt funds (IDFs) and various other financial instruments/products at the global level.

Hemant Kanoria

We have finally started witnessing a distinct improvement in the economy and more specifically in the infrastructure sector, after a lull during the past few years. Infrastructure, as a key area for the development of any economy, will always take centre stage in a country's growth. However, the uncertain economic environment and muted investor sentiment had restricted the growth of infrastructure project development for the past few years. This has had a cascading effect on the demand for infrastructure loans. Concurrently, banks were experiencing stress on their asset quality, which made them cautious in sanctioning fresh loans. We are still seeing that many banks and financial institutions have not been able to comprehend the complexities of the sector and the risks within it, and are grappling with unresolved issues.

Vikas Sharda

Infrastructure credit growth experienced a slowdown during 2011-16 and fell to its lowest at 4 per cent in 2015-16. This is attributable to rising non-performing assets including restructured standard advances to the infrastructure sector during the same period. This trend, however, saw a reversal in the year ended March 2016 when the overall quantum of stressed advances saw a decline. This is due to the combination of a few critical measures taken by the government, such as the establishment of a debt recovery tribunal, premium recast for highway projects, a one-time fund infusion for languishing projects by the National Highways Authority of India, a 100 per cent exit option for developers within two years of the commercial operation date, and takeover of 75 per cent debt of distribution companies by state governments. Besides, RBI has also enabled banks to undertake the restructuring of advances to reduce stress. These measures are likely to benefit the overall infrastructure sector.

What are the new funding sources that are

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Manish Aggarwal, Head, Corporate Finance, Infrastructure, and Head, Energy and Natural Resources, KPMG in India

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Ramesh Bawa, Managing Director and Chief Executive Officer, IL&FS Financial Services Limited

currently being explored?

Manish Aggarwal

The government has been working on opening more avenues for access to capital, which is being actively pursued by some subsegments within infrastructure. Green bonds and climate bonds have hit the market and will act as catalysts for accessing this source of capital. They are being complemented by masala bonds which provide a very interesting play given that currency risks are borne by the investors. Strategic investments, which remained dormant for a while, have seen some activity too. This is aided by the emergence of the sovereign/pension funds asset class. Infrastructure investment trusts (InvITs) are being actively considered by many large public and private players. Overall, we have seen the emergence of many new sources of financing in recent times. This augurs well for infrastructure players, given the large capital requirements. However, we are yet to see an interest in new capacity building, except, to some extent, in renewables.

Ramesh Bawa

The government is exploring various financing options for infrastructure projects. Apart from higher budgetary allocation for 2016-17, funding by multilateral institutions and easing of FDI norms is expected to boost project financing. Investors are also benefiting from the government and RBI initiatives with changes in norms such as flexibility in refinancing infrastructure projects under the 5/25 scheme, cash reserve ratio/statutory liquidity ratio exemptions to banking and financial institutions with respect to infrastructure bond issuances and the liberalisation of the external commercial borrowing policy.

Hemant Kanoria

The present government ushered in a host of positive moves including the setting up of the National Infrastructure Investment Fund (NIIF), the 5/25 mechanism for refinancing, etc. While the government and the public sector will continue to play an important role in meeting the sector's funding requirements, given the humongous scale of India's infrastructure needs, the private sector will have to step in as well. India needs better roads, more ports, uninterrupted power supply and the development of rural infrastructure. There is an urgent need to resuscitate the PPP model. We need to appreciate that the PPP model in India has been a huge success. However, certain mistakes have been made by both the government and the private sector. We believe that this model will thrive once again and meet the funding requirements of the sector, if the contours of the PPP model are properly worked out.

Vikas Sharda

The Life Insurance Corporation of India (LIC) has plans to set up a dedicated fund for the credit enhancement of bonds for infrastructure projects. While this move is seen as a stimulant to the otherwise lacklustre corporate bond market in India, it would be important for LIC to have an efficient in-house credit appraisal system for infrastructure projects. The InvIT is another vehicle for refinancing infrastructure projects that are almost operational and is an alternative to capital with equity or quasi-equity instruments. The exemption of special purpose vehicles from paying the dividend distribution tax has been a welcome step, as many developers are thinking of raising funds under this route. Another source is the NIIF which aims to attract investment for infrastructure development in commercially viable projects from both domestic and international sources. It is understood that the establishment of the fund is in progress.

What is the current stance of infrastructure financiers? Which are the sectors drawing investor interest?

Manish Aggarwal

Key subsegments which are attracting investors and offering multiple capital access avenues are renewables, highways, transmission and stressed thermal assets. Having said this, within each of these subsegments, actual investment is driven by scale, portfolio quality, the sponsors involved and risk-adjusted returns. Each of these subsegments can consider a number of avenues – platform play, long-term infrastructure funds, sovereign/pension funds, InvITs, and special situation/buy-out funds for stressed assets.

Ramesh Bawa

The road and water sectors saw a steady increase in the number of projects awarded over

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Hemant Kanoria, Chairman and Managing Director, Srei Infrastructure Finance Limited

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Vikas Sharda, Director, Capital Projects and Infrastructure, PricewaterhouseCoopers

the past year and this is expected to rise further going forward. The railway sector has also seen a surge in orders. Activities for building new airports and ports have also gained momentum. However, the power distribution and equipment segments have seen some decline in awards.

Hemant Kanoria

The present government is displaying a sense of purpose and urgency in its functioning. A series of reforms and practical guidelines spanning multiple sectors has once again got the global investor community interested in the "India Growth Story". On the infrastructure front, the government has announced a number of sectoral schemes, stepped up public investments and restarted many stalled projects. With the government setting an ambitious target of building 30 km of road length per day and achieving 100 GW of solar power capacity by the end of 2017, these sectors in particular are drawing investor attention.

Vikas Sharda

Given past experience, private lenders, especially private equity firms, are quite sceptical of investing in infrastructure. To reduce risk and help promote private investment, the hybrid annuity model has been adopted in the highway sector. Due to reduced risks under this model, renewed interest by private players is being seen. Another sector which has committed procurement from the government and relatively low risk is renewable energy. This is a sector where there is a lot of portfolio churning by developers subsequent to the operationalisation of solar and wind energy projects. The airport sector is also expected to witness bidding activity, especially airports announced at Bhogapuram, Dagadarthi and Oravakallu in Andhra Pradesh, Dholera in Gujarat and Bhiwadi in Rajasthan. The industry expects the new regional connectivity scheme to drive aircraft movement in the short-distance segment, thereby enhancing the relevance of smaller airports. Other sectors which have seen development as a result of initiatives such as Make in India are the port and logistics sectors. This is being further propelled by various industrial corridors that are on the anvil. The government's Sagarmala programme for increased coastline utilisation could drive greater port investments in the medium to long term.

What is the sector outlook for the next one-two years?

Manish Aggarwal

I am very positive as far as the outlook regarding various financing options is concerned. I see the market evolving and new instruments of financing taking shape. A new asset class is emerging, and with the continued thrust on policy, structural reforms and the expectation of high economic growth rates, we will see greater investments taking place.

Ramesh Bawa

Sectors such as renewable energy, roads and ports are expected to see a surge in activity. With enhanced support from the government as well as RBI, the implementation of infrastructure projects is bound to pick up momentum. Toll-based road projects and the coal-based power segment may also see a pick-up in activity. Independent power producers are expected to add about 10,000 MW of capacity before the end of 2017.

Hemant Kanoria

The Indian government has roped in governments of other countries to jointly implement key flagship infrastructure projects. In addition, the Indian government has conceptualised new investment vehicles which can channelise funds from India and abroad into India's infrastructure projects. These initiatives are poised to open up huge opportunities in the infrastructure sector. While the introduction of the Bankruptcy Code is a positive development, realistically, the stressed asset problem is likely to linger for some time. The government's efforts in pushing land and labour reforms by encouraging state governments to frame their own policies is a strategic masterstroke and can do wonders for industrialisation and infrastructure. To sum up, the business scenario is much better today than it was during the past three-four years. A strong foundation for long-term growth is being laid. Corrective action is being taken on several fronts sector-wise and this is paving the way for a more mature and robust PPP.

Vikas Sharda

The recent amendments to the Securities and Exchange Board of India (InvIT) Regulations, 2014 will prove to be beneficial to developers in the sector and will provide a good foundation for smaller and non-major infrastructure players to showcase their capabilities. Going forward, we expect to see consolidation with increasing merger and acquisition (M&A) activity, especially in the road and power sectors. This is expected not only from domestic developers but also international ones, who will find the Indian market attractive from a risk/reward point of view. With interest from the private sector returning and initiatives by the government such as the hybrid annuity model, bank lending to the road, port and airport sectors is likely to rise. RBI offered a measure of respite to banks suffering from bad loans seeking to ease the pressure on them and their balance sheets. It is expected that more companies under stress will opt for relief under the Scheme for Sustainable Structuring of Stressed Assets in the near future.