Infrastructure Financing Challenges in LLDCs and SIDS in Asia and the Pacific

UN ESCAP Infrastructure Financing for Sustainable Development

Expert Meeting
Bangkok, 7-8 March 2019

Ulukbek Usubaliev, Economic Affairs Officer, ESCAP

Fauziah Zen, Senior Economist, ERIA

Outline

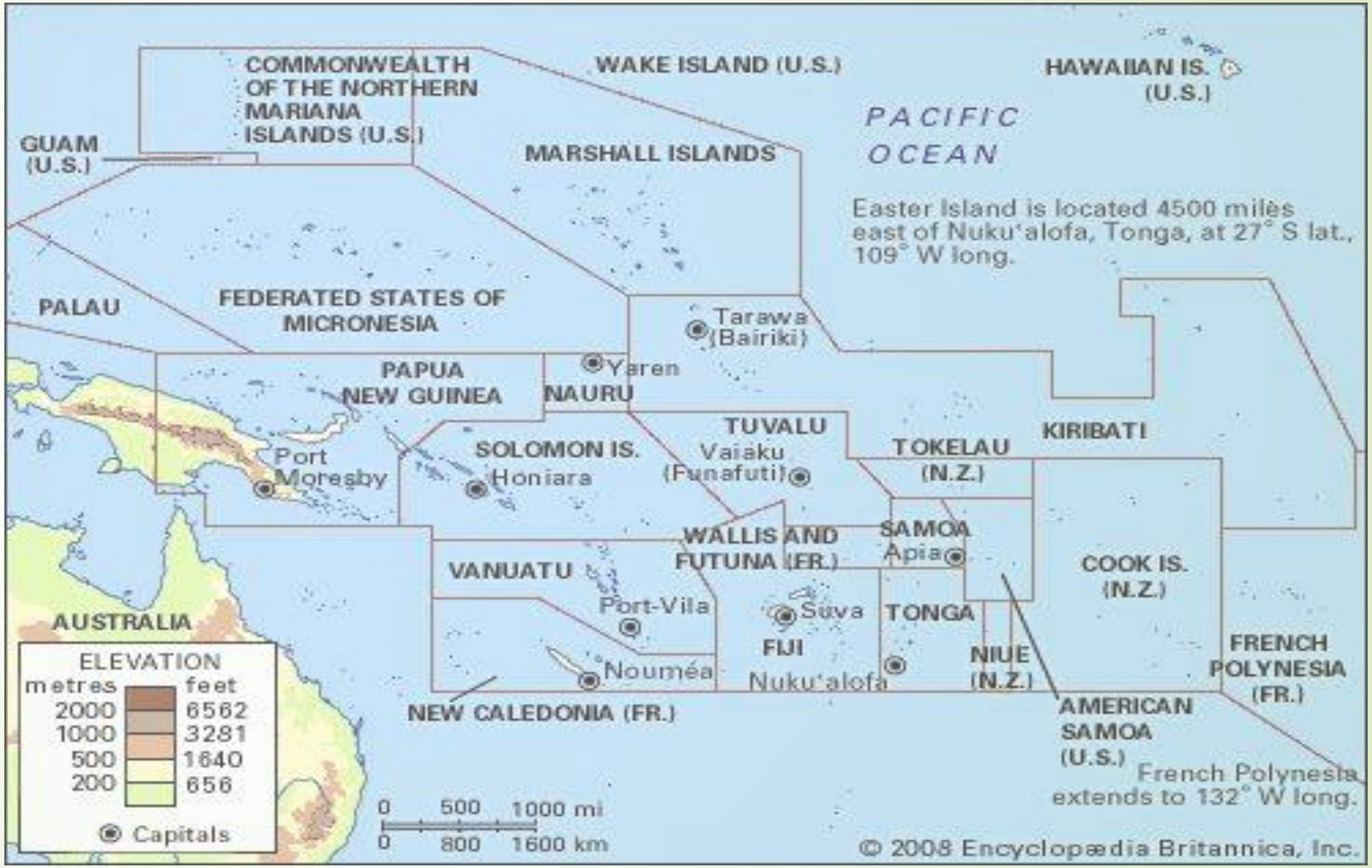
1. Introduction
2. Characteristics of LLDCs and SIDS
3. Infrastructure financing challenges and opportunities in SIDS
4. Infrastructure financing challenges and opportunities in LLDCs
5. Conclusions

Introduction

	LLDCs	SIDS
Coastal area	Do not have	Yes, low lying coastal land
Infrastructure	Inadequate	Inadequate
Natural disaster	Relatively vulnerable	Highly vulnerable
Market	Small, dependent on neighboring countries and external markets, hard to meet economies of scale, uneven distribution of population, rich (some former Soviet LLDCs) and limited natural resources	Small, isolated, dependent on external markets, hard to meet economies of scale, uneven distribution of population, limited natural resources, long distance international trade.
Financial system	Underdeveloped capital market	Underdeveloped capital market
Education and health status	Low for Least Developed Landlocked Countries, relatively high for former Soviet LLDCs	Low
Major Trade Partners	Former Soviet LLDCs: Russia, China, and European Union. LLDCs: India and China	Australia, Japan, China
ODA	China, Japan, MLA	Australia, Japan, China, and MLA

Characteristics of SIDS

- 58 SIDS in the world, of which 38 are United Nations Member States
- The Pacific SIDS: Fiji, Kiribati, Marshall Islands, Micronesia (Federated States of), Nauru, Palau, Papua New Guinea, Samoa, Solomon Islands, Timor Leste, Tonga, Tuvalu, and Vanuatu.
- The islands economies:
  - world biodiversity
  - vulnerable
  - diverse
  - limited development option



General Economic Indicators

Country	Population	Area (km²)	Population Density (per km²)	Number of Islands	GDP (million $)	GDP/cap (PPP $)
Fiji	918 757	18 270	50	330	5 061.20	9 555
Kiribati	120 428	810	146	33	196.15	2 175
Marshall Islands	53 211	180	294	34	199.40	4 193
Micronesia (Federated States of)	106 983	700	151	607	336.43	3 622
Nauru	11 260	20	539	1	113.88	14 158
Palau	22 206	460	48	340	291.54	14 536
Papua New Guinea	8 586 525	452 860	18	600	21 088.76	4 197
Samoa	198 909	2 830	70	9	856.63	6 611
Solomon Islands	635 254	27 990	22	998	1 303.45	2 422
Timor Leste	1 352 360	14 870	89	3	2 954.62	7 213
Tonga	110 041	720	146	169	426.06	5 957
Tuvalu	11 363	30	434	9	39.73	3 925
Vanuatu	288 017	12 190	23	83	862.88	3 208

Source: Population and density data are from United Nations Population Division (2018), others from the World Bank (2017)

Infrastructure Characteristics

- High cost in investment and maintenance: imported capital goods, difficult access, environmentally vulnerable.
- Low maintenance budget: "build-neglect-rebuild" behavior, short project life-cycle.
- Increasing infrastructure spending on government budget, but the gaps still high.
- Infrastructure: aid + public funds
- Private sector participation:
  - The mechanism is unclear and not easily accessible to the public.
  - There are only two nations having PPP Act: Fiji (2006) and PNG (2008).
  - Incomplete regulatory frameworks.
  - Lack of incentives.
  - High restrictions.

Selected Public Finance Indicators in Pacific SIDS, % of GDP

Country	State Budget	Official Aid (ODA+OOF + Private)	Debt	FDI	Special Revenue
Fiji (2017 estimate)	32.4	3.13	48.1	-8.0	..
Kiribati (2016)	115	28.22	42	..	66 (fishing license)
Marshall Islands (2016 estimate)	58.4	29.53	42.5	..	8.3 (compact fund) 6.3 (fishing license)
Micronesia (FS) (2016)	61.2	237.35	25.3	..	19.6 (fishing license)
Nauru (2016 preliminary)	91.6	97.65	64.9	..	27.4 (remittances) 12.9 (tourism)
Palau (2016/2017)	34.9	11.41	26.3	..	39.9 (tourism)
Papua New Guinea (2017 estimate)	20.3	2.00	37.5	..	..
Samoa (2015/2016)	36.5	12.33	52.6	..	..
Solomon Islands (2018 estimate)	46.9	15.74	12.1	31.1	..
Timor Leste (2016 estimate)	64.5	7.51	2.8	..	19.6 (petroleum rev)
Tonga (2017 estimate)	44.9	21.54	48	2.7	..
Tuvalu (2017 estimate)	126	69.54	37	..	50 (fishing license)
Vanuatu (2016)	36.9	16.38	48.8	..	25.5 (tourism)

Source:
- *IMF (2019a; 2019b; 2019c; 2018a; 2018b; 2018c; 2018d; 2018e; 2018f; 2018g; 2017a; 2017b; 2017c).*
- *OECD Statistics: https://stats.oecd.org/Index.aspx?DataSetCode=Table2A# accessed 17 February 2019*

Challenges in infrastructure financing

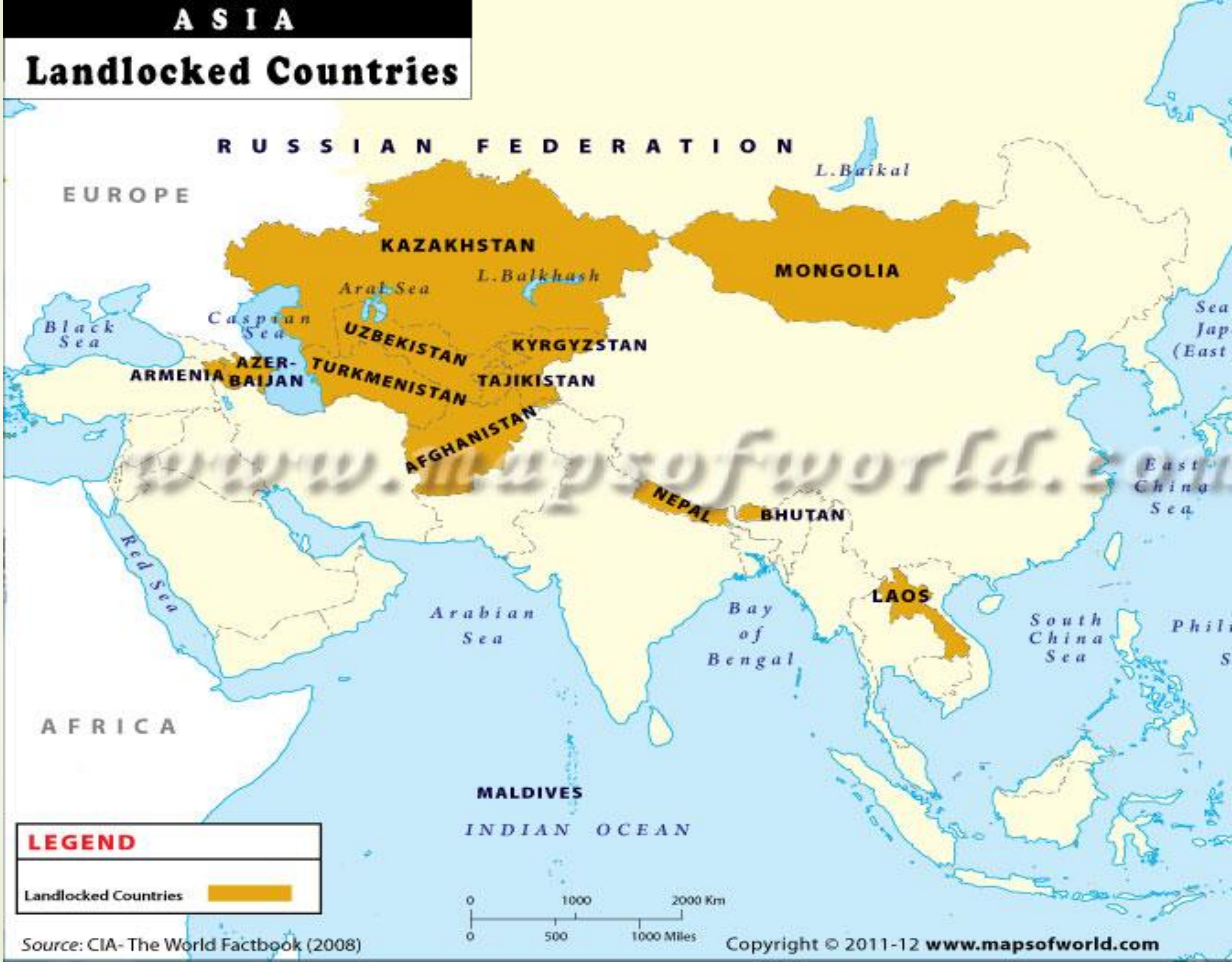
- Market-related
  - Small market and future potentials, isolation, and climate change threats.
  - Structural challenges:
    - Thin market, low purchasing power, high costs of capital, maintenance and replacement.
    - Natural disaster risks
  - Operational challenges:
    - incomplete infrastructure market
    - Incomplete legal framework
- Public sector
  - Lack of leadership, risk management, fiscal support provision, technical aspects, and good pipeline.
  - Low tax revenue and enforcement, low government effectiveness and regulatory quality.

Opportunities for infrastructure financing

- To expand the market: establishing cooperation with neighboring countries or taking part in regional/Global Value Chain (GVC).
- Tourism and GVC:
  - Expand cooperation in tourism sector
  - Provide adequate tourism infrastructure
  - Sustainable framework
  - Explore opportunities to participate in GVC through big neighbors/sponsors: Australia, Japan, China, Indonesia (outsourcings, suppliers, tourism cooperation, etc.)
- Develop adequate infrastructure to attract businesses and increase contribution from tourism sector.
- To increase fiscal capacity
- Climate-change financing: solid planning and leading actions from the authority.

Characteristics of LLDCs

- The LLDCs are a group of 12 countries found in Asia.
- **Mongolia and seven former Soviet LLDCs**: Armenia, Azerbaijan, Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan.
- **Least Developed Landlocked Countries** are Afghanistan, Bhutan, Lao PDR, and Nepal.
- Population: 159.7 million
- Total GDP: $ 393.6 billion including $ 317.4 billion – former Soviet LLDCs



Infrastructure Financing Challenges in LLDCs

The main sources of infrastructure financing in LLDCs

Public sector
65%

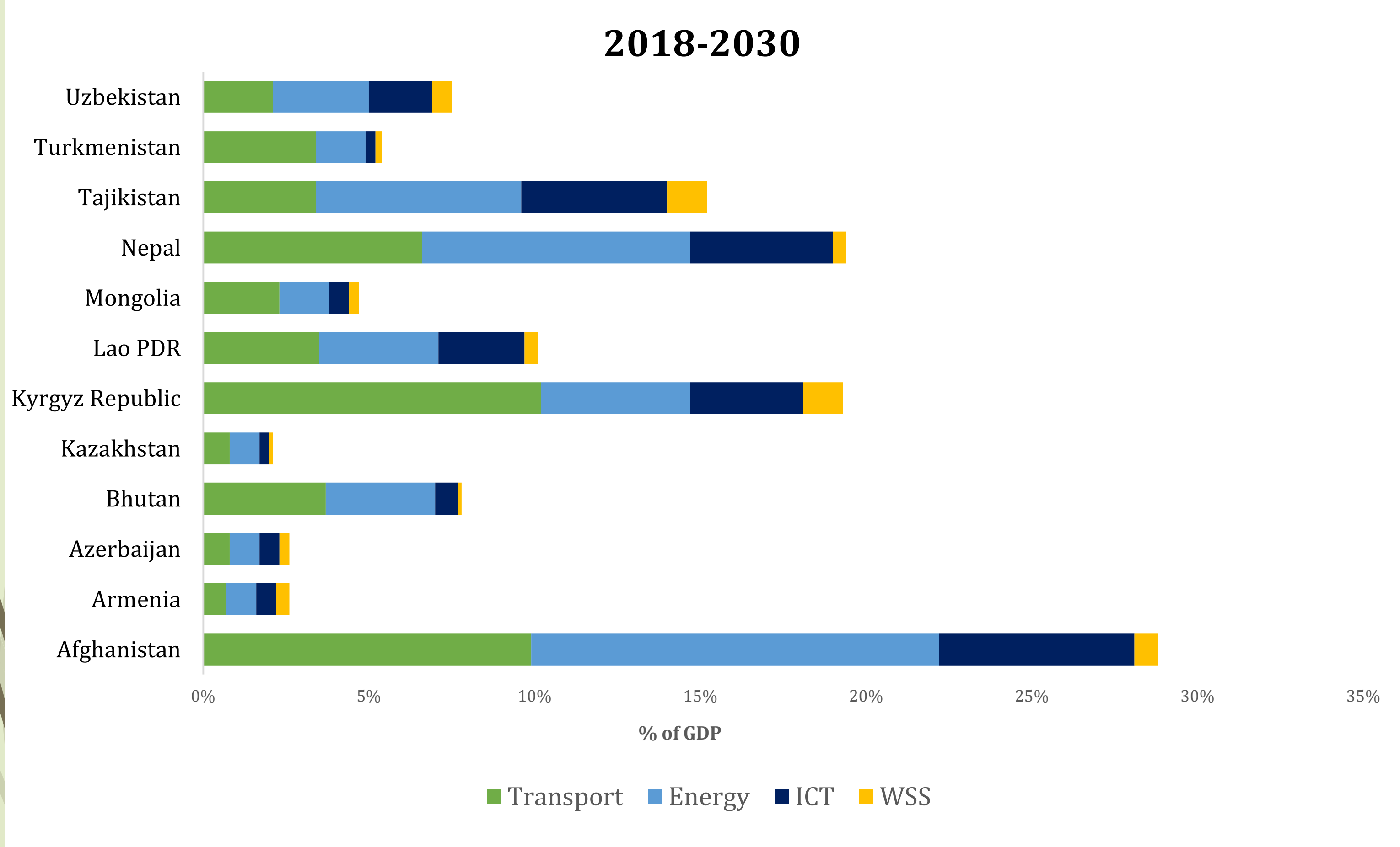
Private sector
15%

ODA
10%

MDBs
10%

Infrastructure Financing Challenges in LLDCs

Infrastructure Financing Needs in the Asian LLDCs



Infrastructure financing requirements to cover all components of infrastructure from 2018 to 2030 in the LLDCs would be totally $180 billion or $15 billion a year in 2010 dollars. This represents 7.6 per cent of the total GDP per annum.

Closing infrastructure gap in CSN, keeping up with growing demand for new infrastructure and maintaining existing infrastructure, will require 10.5 per cent of GDP annually in average.

Source: Economies 2018 Economies **2018**, 6(3), 43; https://doi.org/10.3390/economies6030043

Infrastructure Financing Challenges in LLDCs

Geographical and climate conditions

- Inhospitable continental climate
- Unfavorable topography. Many LLDCs are very mountainous
- Low population densities and
- High exposure to natural disasters: earthquakes, landfalls, flood.

Public financing

- Fiscal balance and current account balance deficits or “Twin deficits”
- Public debt issues
- Inefficient tax administration and low efficiency in public spending

Private financing

- Investment climate in infrastructure markets
- Financial sectors: narrow and underdeveloped, maturity and currency mismatches
- PPPs: limited experience, lack of legal framework, skills, technical capacity and bankable projects

Infrastructure Financing Opportunities in LLDCs

Public financing

- Domestic mobilization through tax reforms
- Transport user charges

Private financing

- FDI incentives: fiscal and financial. Case study: Astana International Financial Centre
- PPP opportunities
- Domestic pension and insurance funds. Case study: Bhutan – pension fund investment in a power plant
- Access to finance

Infrastructure Financing Opportunities in LLDCs

International financing

- Regional Initiatives: BRI, ASEAN, CAREC, TRACECA, etc.
- MDBs and ODA
- International Development Finance: Climate finance, Islamic principles of financing, global pension and insurance funds,etc.

Conclusions on LLDCs and SIDS

- LLDCs are more advanced in overall opportunities than SIDS.
- Being landlocked has impact on infrastructure financing at various extent for each particularly LLDC along with other factors and heavily depends on fundamental specifics of a country.
- Landlockedness and remoteness are rather **additional c**hallenges, but they are not the main factors hindering investment flows and infrastructure financing
- The combination of factors such as governance issues, unfavourable investment climate, corruption, a lack of economies of scale, higher transportation costs, poor infrastructure development are common features for LLDCs and SIDS.
- Geographical and climate conditions

Conclusions on LLDCs and SIDS

- Most Asian LLDCs do not depend on the access to the seaports since their largest trade partners and foreign investors are mostly neighbouring countries. LLDCs of Central Asia depend more on land access to reach their major trading partners.
- Despite being landlocked, former Soviet LLDCs are more advanced in overall development including infrastructure as well as more attractive for foreign investments than many coastal countries globally.
- In case of infrastructure financing opportunities, all LLDCs in Asia do not use the full potential of existing global infrastructure financing options and, consequently, have substantial space to mobilize additional resources for infrastructure financing.
- LLDCs are advised to consider all the relevant potential sources of infrastructure financing and technical assistance from international community.

Conclusions on LLDCs and SIDS

- The disaster threats + small economic size = complicated business climate, especially for large and long-term investments.
- To reduce unfavorable conditions:
  - Improve islands resilience
  - Improve and strengthen legal system to reduce uncertainty
  - Implement capacity building for key government officers
  - Explore potentials for regional cooperation, especially with neighboring countries,
  - Establish a solid, competence, and accountable risk management authority
  - Integrate infrastructure development into national or regional disaster management framework
  - Improve fiscal policy to generate higher fiscal capacity and create fiscal space to develop infrastructure.
- Improve the roles of the donors and development partners of the SIDS

Thank you!