

**ST. PETERSBURG INTERNATIONAL ECONOMIC FORUM**  
**JUNE 20–22, 2013**

**The Global Growth Agenda**  
**PUBLIC-PRIVATE BALANCE IN POWERING A NEW ERA OF GLOBAL**  
**INFRASTRUCTURE DEVELOPMENT**  
**Arena**

**JUNE 21, 2013**  
**09:45–11:00, Pavilion 4, Conference Hall 4.1**

**St. Petersburg, Russia**  
**2013**

**Moderator:**

**Gleb Bryansky**, Editor-in-Chief, Business News Agency PRIME

**Panellists:**

**Amitabh Kant**, Managing Director and CEO, Delhi Mumbai Industrial Corridor Development Corporation Ltd.

**Igor Levitin**, Adviser to the President of the Russian Federation

**Vadim Mikhailov**, Senior Vice President, Russian Railways

**Dennis Nally**, Chairman, PwC International Ltd.

**Yuri Soloviev**, First Deputy President and Chairman of the Management Board, VTB Bank

**Front row participant:**

**Sean Glodek**, Director, Russian Direct Investment Fund (RDIF)

**G. Bryansky:**

Good morning. My name is Gleb Bryansky and I am the Editor-in-Chief of the Business News Agency PRIME. Participating in today's panel will be Dennis Nally, Chairman of PwC International; Igor Levitin, Adviser to the President of the Russian Federation; Mr. Amitabh Kant, CEO of the Delhi Mumbai Industrial Corridor Development Corporation; Yuri Soloviev, First Deputy President and Chairman of the Management Board of VTB Bank, and Vadim Mikhailov, Senior Vice President of Russian Railways.

The topic of today's panel discussion is 'Public–Private Balance in a New Era of Global Infrastructure Development'. The topic of investment in infrastructure is a key theme at the Forum. The demand for investment in infrastructure over the next 20 years amounts to around USD 20 trillion, and the question that arises is how to find a sufficient number of projects to satisfy this demand.

At the Forum, delegates are discussing the question of how to find new sources of economic growth. This demand of USD 20 trillion over the next 20 years could serve as a driver of economic growth. The topic of investment in infrastructure was actively discussed at meetings of the B20, which is preparing recommendations for the G20 Summit due to take place in St. Petersburg in September. Investment in infrastructure was the first topic on the agenda yesterday as well, at a meeting between representatives of the business community and the President. It is obvious that what we are going to talk about today is very important, especially in the current economic climate.

I would like to hand over to Mr. Dennis Nally, who will present some research results – the results of a survey conducted by PwC International among the managers of infrastructure projects in Eastern Europe and Russia. Dennis, please go ahead.

**D. Nally:**

Thank you, Gleb, and good morning, everybody. It is great to be here with you. As Gleb just said, PricewaterhouseCoopers (PwC) just released our 2013 Capital Projects and Infrastructure Survey for Central and Eastern Europe (CEE) and the Commonwealth of Independent States (CIS). It is available here for your perusal.

I think it has some very interesting findings that I would like to at least get on the table, trying to summarize some of the survey's key observations.

First, and I think this is very interesting, 90% of the participants in the survey actually expect their projects to be funded by the private sector. A very high percentage are moving in the direction of public-private partnerships (PPP), which I think we are going to talk a lot about here today. Second, and I think important, 52% of those participants actually experienced cost over-runs on their projects in the last 12 months. Third, 72% actually expect project delays over the next 12 months. This calls into question how many of these projects are actually being managed, and we certainly have some observations to share in that regard.

Interestingly, though, notwithstanding the challenges in the global economic environment and, in particular, the environment with the status of governments today, 60% of individuals who are actually responsible for capital projects expect an increase in expenditures for capital projects over the next 12 months. Again, I think it points to not only the opportunities but also the need to have creative ways to deal with the funding and financing of these projects going forward.

When we broke this down by industry sector, this is certainly true in the energy, utilities, and transport sectors. Those were the top three sectors that really touched on expectations of increased funding for the next 12 months.

When you think about one of the key findings about project delays and over-runs, there is a lot of information in the survey where participants are basically saying we need to make some changes. Permit me to take you through some of those. First, at the outset, better risk management of the project itself. How do change orders get dealt with? How do they get factored in to the project? How are they evaluated? Second, enhanced governance of projects. This is particularly true when you think about the greater engagement and involvement of the private sector in the projects themselves. So, more independent oversight, more objectivity being brought into the management of the projects themselves. Last, the whole notion around what can be done to improve financial reporting on the projects and financial control of the projects, including project scheduling, better completion date forecasting, more realistic assessment of the challenges

associated with project management, and then lastly the whole notion around improving the quality of the information that goes into the reporting of the projects.

I think some very interesting observations from that standpoint. As we step back and think, though, about what are we seeing in terms of some best practices around the whole issue of managing capital projects and infrastructure projects, we see a couple of points. One, to really make private partnerships in government projects work more effectively, there needs to be a better approach to how risk optimization is dealt with. In other words, how is the sharing of risk and reward coming into the management of these projects? Clearly, the private sector wants to have clarity on that; government has issues from a policy standpoint on how that is to play out, but this is all about risk optimization and, to the extent that there is better engagement by both the government sector and the private sector in that process, we see that as a potential step forward. We are actually seeing a number of countries around the world putting together and communicating very definitive frameworks for how these arrangements should work. From a central government standpoint, putting forth the framework with complete transparency as to how these arrangements should work with the private sector is a step forward. Two, we continue to believe that there needs to be a real separation of the technical and the political responsibility of these projects. In other words, policy-makers clearly have an important role to play in terms of their overall views on the direction of projects, but quite frankly, the experts ought to be the ones to determine how best to meet these goals and have clear delineation between the government responsibilities versus the private sector. This is very important, I think, to really build the potential for better engagement going forward. Three, we are seeing the use of more independent experts in this process, not only to assess the feasibility of these projects on the front end, but also looking at the adequacy of the project plan, the milestones, the key performance indicators (KPI), periodically assessing performance against the plan, as a way to enhance governance and transparency around the actual movement of these types of initiatives. And last, we would say that even where governments today are using PPPs on a project-by-project basis, we are seeing

the need for much more private sector cooperation throughout the whole of the process. In other words, moving well beyond financing to really not only doing that and doing that well, but also in terms of how projects are identified, how they are scoped, and actually using the private sector to be really much more engaged in what we would describe as the infrastructure value chain. We see that as the next move in terms of more engagement of the private sector in these important initiatives.

I think it comes back to my first point that this is really all about how risk optimization is managed more effectively, and the engagement of the private sector in that process. We think it can play a very important role in that process.

There you have a quick overview of the study. I encourage you to take a look at it. There is a lot of good information in it, and I am sure we will have plenty of time to answer any questions. Thank you. Gleb, over to you.

**G. Bryansky:**

Dennis, thank you. Mr. Levitin, who is participating in our discussion today, was Minister of Transport for eight years from 2004. It was precisely during those years, in my view, that we saw a turning point of a kind: the Government began to create institutions for investment in infrastructure. If I am not mistaken, one of the first of these institutions was the Investment Fund.

Mr. Levitin, could you tell us about Russia's experience of public-private partnership? To what extent, in your opinion, has it been effective? What have you managed to achieve?

**I. Levitin:**

Thank you, Gleb. I would like to thank Mr. Nally for the very interesting conclusions which were drawn from his research. I have familiarized myself with them. In the majority of cases, everything is correctly noted, but there are a few points which could be opened up for discussion.

The 2005 law on concessions: I believe that was the real breakthrough document, which transformed the work of public-private partnerships. Did it cover every eventuality? Not quite: in order to make amendments, practical

experience was needed. The final version has now been submitted to the State Duma, reflecting all the discussions about how the law on concessions should be amended that have been conducted over a number of years.

We made use of experience from around the world, but not all of that experience was relevant to our circumstances. Infrastructure will always be the responsibility of the state, regardless of who is investing, the state or private investors. The state alone should set the parameters, the goals, and the tasks that need to be completed. The strategic priorities remain the responsibility of the state.

But in public–private partnership, there is also private initiative. For example, a part of maritime infrastructure was built using private initiative, but with government involvement. Several projects are currently being examined for the construction of railways, and for oilfields. However, there are also budget restrictions. These restrictions exist in all countries.

In my opinion, there are two contrasting solutions: the privatization of infrastructure, which we dared not even talk about ten years ago, or public–private partnership. This balance, which has been discussed by those working in the transport industry for the past ten years, demonstrates that privatization is lacking in two respects. Firstly, infrastructure is always a monopoly, and while it can be privately-owned, this creates unequal competition. Secondly, all the risks are assumed by private enterprise, and therefore we do not as yet have private concessions on monopoly in infrastructure. Why? Because we regulate the tariffs. For example, we have a network tariff on the railways, rather than local tariffs. And with a network tariff, it is very difficult to pick out a tariff that will give a return, but nevertheless, we are now thinking about constructing separate routes which could feature tariffs that would enable a return on funding.

In public–private partnership there are also some elements of monopolism. For example, a route could be constructed to an oilfield which has several owners. But if there is only one party involved in constructing the access route, that too amounts to monopolism, and here the state must intervene in order to ensure that the tariffs and the technology itself are transparent.

In my opinion, it is the state that must assume the bulk of the risks related to infrastructure, because that is what developing the economy is all about.

Infrastructure is about the development of the economy, and therefore I would like to reiterate what I have said: it is about the law on concessions; it is about the Investment Fund; it is about Avtodor, which is now implementing all of its projects exclusively on the basis of public–private partnerships; it is about Vnesheconombank; VTB; and the creation of separate structures which are already dealing with questions related to public–private partnership.

Thank you.

**G. Bryansky:**

Thank you. Some time ago, four countries with large economies were grouped together as the BRIC group, a term originally coined by an economist at Goldman Sachs. More recently the group has come to be known as BRICS, with the addition of South Africa. All of these countries had certain things in common, and all of them have been experiencing certain problems with investment in infrastructure, which may have similarities.

Participating in our discussion today is Mr. Amitabh Kant, CEO of the Delhi Mumbai Industrial Corridor Development Corporation.

Mr. Kant, tell us about your project: what is its current condition, and what problems have you encountered in making this project a reality?

**A. Kant:**

Let me first compliment Dennis on his wonderful report, which really signals the shift towards private participation as the key driver to growth in this very key sector.

I think the important thing is that infrastructure requirements are very large. The fiscal space available to governments is very small. The public sector is unlikely to mobilize the required resources and the private sector has to be necessarily brought in as a supplementary source of finance. This is necessary to not merely bring in resources, but to bring efficiency into the sector.

Yet to my mind, the role of the State is extremely critical. The role of the State changes from an actual doer of the infrastructure to the role of facilitator and a catalyst. Many people will talk about financing, but to my mind, there is a poverty



of well-structured, de-risked projects globally. If you are talking about USD 24 trillion worth of projects, that means the world needs about four times that amount of structured projects to be put out onto the market. That is, projects where feasibility studies have been done, where land has been taken, where all the risks have been shared to the people who are best equipped to take them, and put out into the market. That is an exceedingly difficult job for governments to do, let me tell you.

The Delhi–Mumbai Industrial Corridor is one of many projects, but this is a key Government of India project, and India has had a very large landscape of public–private partnership (PPP) projects. At the moment, there are about a thousand infrastructure projects under PPP. The Delhi–Mumbai Industrial Corridor is about linking Delhi to Mumbai through a high-speed container train and creating seven new industrial cities on the route.

We feel that cities cannot be created without a backbone. Certainly, everything in the world is not PPP-able. There is a trunk infrastructure – trains, sewage, solid waste – not all of which is capable of commercialization. Therefore the government must step in and create that trunk infrastructure. On the back of this, we feel that in new cities, about 40% of the expenditure must come in from government. The government must be able to do good engineering, procurement, and construction (EPC) contracts. On that basis, the balance, 60% of the projects, will be structured and put out for private–public partnership contracts.

Now, PPP projects, to my mind, are basically about de-risking projects. They are also, however, about a lot of homework. They are about creating the right kind of concession agreements. They are about a certain level of surety and consistency in the legal framework. Without a good legal framework, it is very difficult to bring in good international companies to bid for these projects. There is a need for transparency and Levitin spoke at length about competition. There cannot be monopolies in infrastructure. A private monopoly is worse than a government monopoly, and therefore you need to bring competition into the infrastructure sector. I think timely intervention on implementation and dispute resolution, as Dennis pointed out, are critical. However, I think the important thing to realize is

that when we talk about PPPs, it is not merely public, it is not merely private. We often miss out on the third component, namely, partnerships. The government's role, in fact, to my mind, increases. It increases in terms of structuring projects, de-risking projects, acting as a facilitator, acting as a catalyst. The government, having structured the project, must then put it out into the market in a transparent, competitive manner, get the best bids, and then ensure they go smoothly. And let me tell you, not a single PPP project across the world has gone smoothly. Since these projects span 25–30 years, they always run into some problem or other. You must have timely dispute resolution. That is the key.

Therefore, it is about government being the key driver of PPP through a partnership process. That is what we are trying to do in the Delhi–Mumbai Industrial Corridor: make a paradigm shift in India's infrastructure; create the backbone; put out projects; de-risk projects; put them out to market; and get the best players from across the world, so that we can create new, sustainable cities for the twenty-first century. The world has moved away from the nineteenth and twentieth century models of government-owned infrastructure. Thank you.

**G. Bryansky:**

How many years are you expecting this project – the development of the industrial corridor – to take?

**A. Kant:**

In 2017, a dedicated container train will run between Delhi and Mumbai. Today it takes 14 days to carry goods between Delhi and Mumbai, to the ports on the western coast of India. In 2017, all the goods will be in ports within 14 hours. From 14 days to 14 hours, it will be the radical shift through this container train. The first phase of the seven new cities will be done by 2019. Initial trunk infrastructure has already started in five of the seven cities. Thank you.

**G. Bryansky:**

Thank you. We have with us today Sean Glodek, the Director of the Russian Direct Investment Fund (RDIF). Sean took part in the B20 panel discussion on

infrastructure yesterday and, it would appear, also attended the meeting between experts from the RDIF, representatives of major global infrastructure funds, and President Putin. I therefore invite Sean to tell us about what was discussed.

**S. Glodek:**

Thank you, Gleb. Basically, what we talked about is recommendations for the Business-20 (B20) to the Group of 20 (G20). I think what has been discussed here is extremely important. There is a fundamental role for the private sector in global infrastructure investing, and government is not the solution to all of the problems. More importantly, governments are stretched financially, so any time you are talking about infrastructure projects, especially in emerging markets, you are looking to the government to do pretty much 100% of it. That is not sustainable.

What we looked at, together with major infrastructure funds, with multinational development banks, with some government agencies, with some non-profit organizations, was to really sit down and develop a set of recommendations that then can be put forward to the G20, that would be actionable in a way to help the specific problems being discussed here. There are really three recommendations that we came up with. The first one is to help long-term investment, which is something that is hurting, especially in the cross-border area. The specific rules and regulations on accounting and on tax actually prevent or penalize pension funds or banks for putting money in over a 20–30 year period. That is one point, we are going to bring a task force together with the Big Four to analyse that and then makes recommendations at the next G20 in Brisbane. The second area of recommendations is how to involve the private sector in infrastructure financing. There we have three recommendations. The first one is that you have to open local capital markets and local pools of funding to support infrastructure projects. These could be infrastructure bonds, junior financing, or senior secure subordinated debt. That requires developing a legal framework. That requires enabling local sovereign wealth funds and local pension funds to actually come in to these projects in a structured, secured way. There is a good example in Canada that we are going to base the recommendations on. The second

recommendation for private sector infrastructure financing, is setting up a project preparation fund, with USD 10 million from each G20 country. It will be a USD 200 million evergreen fund. There will be about USD 5–10 million per project. What we have found from practitioners is that is where most of the value could be created or destroyed for a project. It is actually in how you do the feasibility study, how you sit down with the local government and develop the appropriate PPP framework with the interest of the future investors in mind. This fund will be able to have access to the best consultants, the best lawyers, best practices, and front that expense for the government, and effectively stamp the project as something that could be then offered to investors in a way that it is almost a must-invest. And the third recommendation is, because we are talking about projects with 20–30-year commitments, and there is a lot of risk around them. That is not necessarily in the set-up stage but more in the holding and continuing to receive the same public sector guarantees that were meant at the very beginning. In this regard, we are going to talk with the Multilateral Investment Guarantee Agency (MIGA) at the World Bank Group, which provides the insurance for political risks, to actually expand their mandate to provide an insurance wrapper for infrastructure projects around regulatory risk, so the financing will be much cheaper. The final recommendation is that a lot of infrastructure spending is actually extremely inefficient, and consequently we looked at how to do more with less. It has been identified that there is USD 1 trillion per year in savings that could be gained in infrastructure spending by deploying fairly simple and specific directions on what to do and what not to do.

We are going to set up an infrastructure network run by the World Economic Forum, with the support of my company, the Russian Direct Investment Fund (RDIF), that would aggregate and disseminate best practices around PPP project structuring, as well as how to access capital and what the capital demands are, so that the local governments have one place to access this information and always have the best information to work with in terms of pricing, cost, and to disseminate best practices to improve efficiency.

**G. Bryansky:**

Thank you. Sean mentioned the capital markets, and in this regard it would be interesting to hear the opinion of the banks. I think Yuri Soloviev can tell us something about this. Mr. Levitin just mentioned VTB: he practically referred to it as a development institute. There are quite a lot of infrastructure projects in your portfolio. How do you manage them, and what must be done in order to optimize them?

**Y. Soloviev:**

Thank you, Gleb. I would like to build my presentation on what has already been said by the previous speakers. I really liked the report from PwC. I am struck and won over by the passion with which Amitabh talks about his project – we would do well to show the same enthusiasm.

We have indeed seen a small revolution taking place in our country over the last eight years. We have really begun to work on public–private partnership projects. I absolutely agree with what Mr. Levitin had to say with regard to monopolies, tariff policy, the role that the state ought to play, and federal law itself. During this time, we have carried out several projects which have earned international recognition. These are, to name just a couple, Pulkovo International Airport and the Western High-Speed Diameter – two very capital-intensive projects which have both reached the stage of financial closure. I would like to share some of our experiences with you.

The main problem is not the investment climate, but the lack of long-term funding and the lack of projects. Why do we get the sense that there are so few projects? Even though, it would seem, we are already talking about a trillion dollars being spent in the Russian economy over the next 20 years. We continue to talk, the 20 years continue to be pushed back, a trillion remains a trillion, but as yet very few projects have emerged.

The two projects that we implemented, by the way, were not carried out at the federal level, under federal law, but under regional law – the law on concessions in St. Petersburg. I would like to express my sincere gratitude to the Government of St. Petersburg: it was through their initiative that the biggest projects were

carried out. For any politician, minister, or government representative to take a decision on a long-term project which involves a large amount of risk – that is a risk in itself. In order to do this, therefore, a local law must be adopted which must be in line with federal law. In our country this is not happening at all at the moment.

All of these projects are capital intensive. Consequently, a large amount of money needs to be spent right at the outset. Some regional authorities say, “We are now spending USD 10 million, the project might not take off (which actually could happen), and then I will be asked what I wasted USD 10 million on.” I do not want to name the relevant authorities which might be interested, but when it is announced that a high-speed rail project will cost RUB 3 billion, people are very surprised and think something is probably not right there – and then it proves impossible to spend these funds on completing the project. It is an entirely practical matter, and relatively banal, but that is precisely the thing that forces people to make a decision.

Let us now look at the practical point of view. Let us say that for some reason the government wants to cancel a contract, or the concession holder goes into default. International practice in such cases is as follows: the government, at some level or other, must return the funds and compensate the investors for the main part of the debt. The share component of the capital will be practically burned up, but the debt will need to be repaid if an old debt exists. This meets with complete bemusement on the part of our authorities, for several reasons. This point of international infrastructure planning runs contrary to the norms of Russian budgetary legislation. It is not possible to make provision for such compensatory payments in the Russian budget over 30 years. How do international governments solve this problem? They attract banks, which give them guarantees against this kind of debt, and so on. In other words, there is a whole series of mechanisms in place, each of which hedges against the others. Unfortunately, perhaps through a lack of experience, perhaps through a lack of knowledge, we are coming up against this problem at the practical level.

At the level of technical or first analysis of a project in our country, we devote a huge amount of time to the technical side and the budgeting side. As a rule, we do not tend to think about risk.

On the subject of technical standards, it must be said that some of these standards, both for the use of materials and for the lighting of premises, were drafted way back in the Soviet period, when the technology used and the world itself were very different. We came up against this in Pulkovo, for example. That is why, whenever a new-fangled air conditioning system is brought in, it is not covered by any Russian standards, because there was no such thing before. This all takes up a lot of time, and therefore construction starts to get a bit behind schedule. We must go back and reformulate our projects – precisely what we were talking about.

I would like to make a separate point about fiscal problems. Any financing of projects like this involves a pledge of shares. There is a rule on thin capitalization, under which, following any pledge of shares in Russia, those financing the project may not deduct interest payments from their tax liability. That is a huge problem, because it makes the project more expensive, and sometimes this means that it does not make good economic sense either for the government or for the private sector. There are many small examples of this kind, we are all saying things that are entirely justified: about the redistribution of risk, economic expediency, tariffs, and so on – but these small things can really mount up, and can kill off a project.

We participate fairly frequently in consultations with various government bodies, and work with Avtodor, which has an absolutely solid foundation and a very professional team, and I am sure they will have many interesting projects. I believe the initial experiences of the Investment Fund were also very positive, because without those experiences some of the projects we started to work on would never have taken off.

I will now say a word or two about financing. Even during the crisis, we provided full financing for Pulkovo, we tranced the capital structure, floated the so-called older debt of EUR 800 million out of the EUR 1.2 billion, which amounted to the entire cost of the project, and went up in the international markets. That was in

the middle of the crisis, and people were happy to give us enough funds for a decade, and at a relatively cheap cost. And that was without guarantees at the federal level or any other level of government, which just goes to show that there is a huge amount of capital in the world which is ready to make its way here. However, the projects were mainly carried out in roubles, and the return on these projects will be in roubles: the tariffs will be in roubles and inflation will be in roubles. Long-term funds here are only held in either dollars or euros, and this is known as an external, international currency. From this, the question arises as to whether we have a swap market or the presence of rouble liabilities in those same banks that are prepared to take on such risks.

If you look at the structure of liabilities in the Russian banking system, you will find that it hardly exceeds a year, and we are talking here about 30-year projects. For the first three to four years we are spending money, then the cash flow begins to come in, which means that the liabilities actually have a duration of a lot less than 20–30 years. We are returning to the level of monetization of our economy, to the level of liquidity.

Everyone is talking about the Pension Fund, about the National Wealth Fund, and so on. There is a whole multitude of problems. I do not know whether it is worth centralizing all these problems within a single government organization, which would look beyond the industry and approach each project as precisely that, regardless of the sector in which it is being developed. I am sure, however, that Mr. Mikhailov will now correct me, and say that rail transport must be looked at separately. However, those same approaches, with amendments appropriate to the sector, can be applied to the housing sector, the energy sector, the rail sector, and the maritime transport sector, again without encroaching in any way on the Government's role in determining the level of monopolization, the level of tariff formation, and so on. We are therefore prepared to share our experience. Furthermore, we are participating in a large number of projects which are just beginning, and we would like to see more of them. I am absolutely certain that if we keep moving in this direction and maintain this momentum, we will achieve great things. Thank you.



**G. Bryansky:**

Thank you. One more question. A lot has been said recently about infrastructure obligations. You did not talk about these. I would just like you to share some of your thoughts on this issue.

**Y. Soloviev:**

We have a series of instruments which are already being called infrastructure obligations, but which are not, in the international sense of the term, infrastructure obligations. They are attached directly to the project and have a state guarantee, but the state guarantee is included automatically. We can talk about the mechanism of state guarantees: it ought to be a very interesting topic of discussion in itself. What is currently seen as a state guarantee here does not work as effectively as it ought to. Secondary liability does not operate. If a default occurs on obligations, you will only receive your money at the end, which assumes a huge discount – so-called present value – and so on. We could go on talking about this for a very long time: it is a separate question which needs to be addressed.

Obligations in project financing are a rather complicated instrument. There are not that many purely project-related obligations in the world. As a rule, certain instruments are set up (with a partial guarantee from the government), and a certain kind of risk, a certain kind of cash flow is tranching, and within these a certain kind of securitization occurs. There is definitely a place for these things, but investors must understand what they are buying. Unfortunately, our investment base is not sufficiently well developed for investors to be able to assess the risks of any particular project. Such instruments ought to exist within the structure of a capital market.

Everyone talks about pension funds, but people rarely recall that some of the biggest investors in the world, in terms of both volume and strength, are insurance companies. Practically all regulators oblige them to maintain equality between their liabilities and their assets. Life insurance has still not reached the same volumes here as it has in other countries, but when it develops, insurance companies will be first-class investors who ought to be included in these long-

term instruments. They must be bound to the inflation component, to a probability of default that is based on their liabilities, and so on. Nobody is talking about this yet, but this is a huge stratum of investors, and it is now putting out feelers in short-term, speculative operations. Thank you.

**G. Bryansky:**

Thank you. Before we move on to the next speaker, I would appreciate it if Mr. Levitin could strike while the iron is hot and comment now on some of the considerations expressed by Yuri.

**I. Levitin:**

I will start with what Dennis talked about. From 2014, a price and technology auditing of projects will be implemented in the Russian Federation. This was one of the instructions of the President of Russia in the executive orders on construction announced in May. The first few projects will undergo a pricing and technology audit by Avtodor, and then these projects will compete with each other. This is one of the elements of transparency and the use of modern technologies in construction, and of the pricing factor.

One question arises: who is going to do this? For this, we need very experienced specialists in the fields of modern construction technologies and finance. We believe that, first and foremost, this ought to be the banks, as we said earlier – in other words, specialists who will deal with these questions. The technology part will be undertaken by experts in the field of construction. This must be done by the same team, because it is very important that we receive such projects. This question has been decided.

I would also like to talk about the problem Yuri referred to. The Investment Fund was founded with the aim of financing projects. Today, nobody wants to take on the financing of projects. Russian Railways has requested funds from the federal budget, and a discussion is currently taking place. Who should distribute these funds? And if the project does not work out, who will be responsible for this sum – and it is a sizeable sum? The Investment Fund was created precisely to meet these challenges. There should be competition between projects here: the state

will allocate funds, and then these projects will compete with each other. Unfortunately, this Fund is no longer operating, and therefore even the start-up costs are a problem for large infrastructure projects. This is precisely what we need to be thinking and talking about today.

**G. Bryansky:**

What do you think, is it possible to somehow integrate the Investment Fund with those projects that were discussed at the B20, and which were mentioned by Sean? He was talking about some kind of general G20 fund for structuring and working on projects.

**I. Levitin:**

We spoke to the RDIF, but due to its status, the Fund can only work with foreign partners. They cannot work with our banks. Therefore, if a G20 fund is created, and if it is going to be involved in competition for projects, Russia will be able to take part in this too.

Will all of this money go to Russia? Of course not. I believe we will see a kind of global competition for projects, in which the RDIF can take part. But we need projects that we can start up here, by ourselves. And here it can only be the banks I talked about earlier, or the Fund, which will now be used by Russian Railways in order to develop the rail infrastructure. However, it seems to me that a mechanism for planning and launching such projects is nonetheless required.

**G. Bryansky:**

Thank you. In today's discussion, rather a lot has been said about the relationship between risk and reward. This relationship changes from country to country and from sector to sector. We have at this table a representative of what is probably the largest infrastructure monopoly in Russia, Mr. Mikhailov. What is this relationship like in the rail sector, and to what extent will it be possible for private investors to get involved in the railway sector, in your opinion?

**V. Mikhailov:**

Thank you, Gleb. There is probably no real doubt in anyone's mind about the question of investment in infrastructure as a driver of economic development, with the exception of a few researchers who believe that this is not entirely the case. From our perspective, it is the cornerstone for ensuring the country's growth and, of course, we are focusing a huge amount of attention on investment in our railway infrastructure, which has a series of serious limitations in terms of attracting private investment. This is due to a range of legal constraints, such as the limits imposed on the turnover of assets from rail transport.

In addition to this, infrastructure projects are very long-term investments, and private investors are not always prepared to invest in projects which take so long to offer returns. Here is a classic example: last July, when we floated the first inflation securities on the market, Mr. Soloviev and his bank participated in these securities. The maximum demand which we achieved on the market amounted to RUB 10 billion over ten years. In other words, nobody was prepared to invest more, for a longer period, under conditions of inflation (and we floated the securities at inflation plus 2.1%).

This acted as a definite trigger for the decision made by Mr. Putin, and after this the President gave a specific directive to the Government to use pension funds for infrastructure projects. Of course, a colossal amount of work was carried out within the Government. Many thanks must go to the Government for this work. In December, the fiscal policy of Vnesheconombank, as an institute for the management of pension funds, was altered, and on June 12, for the first time in Russia, 30-year securities were floated at a rate of inflation plus 1% – an unprecedented step for the Russian funds market, and more broadly for the development of a mechanism to enable the investment of pension funds in infrastructure projects. Pensioners receive a guaranteed income – inflation plus 1% – and Russian Railways receives unprecedented long-term funding for up to 30 years, at inflation plus 1%. As you know, on the whole all discussions about indexation over the next five years will be based on inflation, inflation plus 1%. In other words, the source for the payment of these sums will be established.

The company has done a huge amount of work to analyse the overall requirements for investment in infrastructure for the period to 2020. We brought

in experts who worked on the inter-industry balance during the Soviet period. There used to be a strategic planning system, which, unfortunately, was forgotten, and the Government has not worked on the inter-industry balance since 1995. An enormous amount of work was carried out, including with the help of the Ministry of Economic Development and the Ministry of Transport. On the basis of this, we had a clear understanding of President Putin's directive – to analyse the applications made by all the major goods consignors (the Kemerovo Protocol dated January 24, 2012). We looked at all the major goods consignors and specific routes for goods shipments. On the basis of the inter-industry balance, all applications which were not corroborated by supporting calculations were excluded, and a minimum requirement for the infrastructure to be developed by 2020 was established, amounting to around 5 trillion. On this basis, a long-term investment programme was drawn up – a colossal step forward in terms of long-term planning, working out which projects to choose, where to invest and why, and what sort of growth, in millions of tonnes, would be achieved in order to implement this project.

The entire investment programme is divided into three strands. The first section consists of projects due to be completed within the next 15 years. Here, we worked very intensively with the banks and with our colleagues. Russian Railways is one of the best borrowers on the market from the point of view of basic rates. The weighted average rate for our portfolio currently amounts to around 7%: that is substantial figure. Based on a debt to EBITDA ratio of 2.5, according to the recommendations of rating agencies, we are attracting funds from the market and investing them in these kinds of projects.

Can we consider these to be infrastructure projects in the classical sense or not? Whatever the case may be, for an infrastructure project they are tied to this funding at the administrative accounting level. Taking into account the introduction of the infrastructure obligations mechanism, we received up to 100 billion a year over the next three years. It will be possible to provide the significant sum of 300 billion in financing over the next three years. Projects which at one time had no commercial return potential for Russian Railways have now, with such a long-term duration and that kind of interest rate, become

profitable, and can now be added to those projects in the portfolio which offer a return. The third strand, which we do not see as being closed, contains the so-called non-return projects, which offer no commercial return potential for Russian Railways, or for companies, but are significant for the country as a whole on a macroeconomic level.

This year, the Government decided to allocate resources to the Mezhdurechensk to Tayshet route. This is another interesting example of public-private partnership, when the private investor constructs a line between Kyzyl and Kuragino, coal is dumped out onto the Trans-Siberian, and, naturally, in order for it to run, there is a need to expand carrying capacity. The Government decided that 40 billion would be set aside to sort out the bottlenecks on this route over the next few years, by means of contributions to the authorized capital.

The second major decision was taken at a government meeting on April 2 in Yakutsk: 260 billion for the Baikal-Amur Mainline and the Trans-Siberian. This is the minimum volume, which will allow us to transport an additional 50 million tonnes by 2020.

I will reiterate once again: for investments in infrastructure, there are legal constraints; however, new lines can be built, including by means of concessions, creating special purpose vehicles; it is possible to develop stations, that is, the part of infrastructure which can to a certain extent be financed by taking private capital into account. But, of course, the role of the state here is huge.

Based on the example set by Russian Railways, we can see that there are projects which this company funds independently, and there is substantial government support in the form of infrastructure obligations and significant direct government support for the development of infrastructure. A balanced approach such as this will help to solve some very serious tasks, and if it is implemented correctly, it will help to considerably expand the carrying capacity of Russian Railways by 2020.

**G. Bryansky:**

Thank you. In the B20 discussion, much was said about cross-border projects, so I would like once again to hand over to Sean Glodek from the RDIF. Perhaps you

would like to talk about some of the cross-border projects which could be implemented as part of the work of the B20?

**S. Glodek:**

Our focus was primarily on providing private capital across borders, because we were looking at a lot of markets. There is a disparity between where the capital is available and where the most value-adding and GDP-creating projects are located. Our cross-border focus was actually attracting investors from mature markets into developing market projects.

I would just add that it is a very good conversation, but I think a lot of the issues that we are discussing here are not necessarily new. They have been around for a while. What we have discovered, through work with the B20 right now, is that at this point after the recession, with a very low global growth, there is recognition that a lot of the growth in the future will come from emerging markets. There was a focus on how to recharge growth, and that is where a lot of the focus comes in. You use the available capital, because there is a lot of capital available, there is a lot of private capital available, but it is not getting deployed, because projects are not structured right and because governments often have difficulty committing to a set of priority projects which will then survive in regulatory regimes for 20–30 years. When investors make a decision, they do make a very long-term decision. Crossing a border into a project that where gains are only modest, if there is an adverse change, you get effectively wiped out. Understanding the long-term perspective coming from foreign investors is something that the B20 is really trying to communicate to the G20 governments. It is not about the short-term fix. I think what the Project Preparation Fund, for example, does is to provide the short-term fix of identifying and helping projects come to market. But it still leaves a fundamental role for government in the long-term to commit to projects and to not change the rules of the game, which is what investors are focused on and mostly worried about. This is not an emerging-market phenomenon. Governments change rules in developed markets as well. It is really a global phenomenon as far as infrastructure investing is concerned, that longer-term investors are really worried about governments changing the rules.

**G. Bryansky:**

Thank you. After such a wide-ranging discussion of the problems and prospects of the infrastructure sector in Russia, I would like to get an outside perspective.

Mr. Kant, over the past hour you have probably discovered a lot about Russia's infrastructure sector. Which of the concepts, recommendations, and ideas will you be taking back with you to India?

**A. Kant:**

Based on our experience, I have a couple of points. First, you must establish a project development fund which will create a shelf of projects which are de-risked and can be put into the market, and that is a difficult job. Second, the existing monopolies will not like the private sector coming in. Whether you like it or not, the mind-set of existing monopolies will not permit the private sector to come in at the cutting edge. Therefore, you need to bring in independent regulators. That is the only way to go about it in the long run. Third, there is a difference between construction risk and operation risk. It is important that we are able to get good companies to get over the construction risk and, once the construction is over, allow those companies to get out. Therefore you need take-out financing. You also need another set of people who can bring in global standards of operation and maintenance. Therefore, to my mind, take-out financing and the long term are important. You keep talking about pension funds and insurance funds. They will be very difficult to bring in unless the macro-fiscal balance is set right. Therefore, government needs to create an infrastructure debt fund. Lastly, I would like to say that in the initial stages, do not pass on too many risks to the private sector. If you pass on too many risks to the private sector, it will be very difficult; you will run into problems later. A better methodology in the initial stages would be to do annuity contracts, or what Canada calls 'availability-based payments'. In that way, the private sector will meet performance standards, they will raise about 90% of the debt from the market, and they will bring in about 10%. They will keep performing to prescribed standards and get paid only if they perform to those prescribed standards. With regard to annuity and



availability-based payments: let the market mature over a period of time, and then shift more and more market risk onto the private sector.

In summary, a private development fund, an independent regulator, take-out financing, availability-based payments, and annuity contracts are a very good way for the Russian Federation to move forward. Thank you.

**G. Bryansky:**

Thank you very much. When you speak with such passion, it really makes me want to travel to the Delhi Mumbai Corridor and see what is happening there.

Vadim, could you comment on Mr. Kant's statement to the effect that large infrastructure monopolies do not intend to let in private investors, and that an independent regulator is needed for this?

**V. Mikhailov:**

The question here is not whether natural monopolies intend to let private investors in or not. There are a series of legal constraints which do not allow private investors to get involved in public projects, and that is a fact. Either the legislation will need to be changed, or we will have to live with this fact.

A second point: there are definite elements that private capital should be directed towards, where it is more effective. These are the construction of new lines and the development of transfer hubs and transport hubs. The example of Moscow Region illustrates very clearly how this is being implemented. And here there are no problems with regard to access for private investors.

For infrastructure companies as large as Russian Railways, the actual moment of branching off would either take place as part of privatization or as part of concession. Experience around the world suggests that an ultra-liberal country such as the United Kingdom can return to state ownership of infrastructure. That probably tells us something, and it is certainly worth thinking about. Over the past 25 years, Deutsche Bank has been toying with the idea of privatization and yet for some reason cannot make up its mind to go through with it.

The question is very simple: this is a clash between private interests, which demand that cash loans be maximized over a fixed period of time, preferably a

short one, and the state's task of determining or developing transport mobility for the public and ensuring that goods are conveyed to places determined by a general development scheme.

The question is not, therefore, about whether we would like to see private capital or not. It is a question of expediency, taking into account experience around the world and the opportunities that the private investor has, based on the fact that in our country, nobody wants to invest in infrastructure for more than ten years under normal commercial conditions.

**G. Bryansky:**

Thank you. You are the head of a global company and you probably have a good cross-sectional view of what is happening in other countries. Could you comment on the problems related to investment in infrastructure? Are they characteristic of developing countries only, or do developed countries also experience these problems?

**A. Kant:**

I think it is a great question, and just stepping back, this has been a great conversation. However, when you really look at the bigger issue here, to me, this is all about the long-term competitiveness of a country. That is the real issue here. Without an adequate infrastructure, you have to seriously question how competitive a particular country will be vis-à-vis the global picture. That is why I think it is so important to get this right. I would also say that, reiterating Yuri's point, these issues have been around for a long time. You almost have to step back and say, "We do need a different model to really address the fundamental challenges here."

As I look around the globe today, very few governments, if any, have the financial wherewithal to do what we are talking about. They just do not have the funds. When I look at some of the big megatrends that we are going to see over the next 15, 20, 30, 40 years, with population changes and urbanization, the need for the creation of new cities, for opportunities to create jobs, and so on, if we rely only on the old model to deal with the development of this infrastructure, it is not

going to happen. I think it really is incumbent upon all countries, developed as well as developing, to think about the new models that are available. We describe it as a hybrid. It is not a one versus another, but rather government involvement and private involvement. It is important, however, to get the frameworks right, you have to address some of the legal issues that are out there today, in order to encourage the private sector to get engaged, to get involved, to de-risk some of these projects, and to make them financially viable for those enterprises to really be successful.

I think that new models that really facilitate getting on with the actual engagement of these projects are absolutely critical to the competitiveness of a country. I think that we are beginning to see some of that happening here in the Russian Federation. I would just encourage more of that to really accelerate, so that the competitive positioning of this country is going to be acceptable over the longer term.

**G. Bryansky:**

Thank you.

**V. Mikhailov:**

I would like to add my voice to that of Mr. Kant, when he says that the initial projects must be successful. If the first few projects are unsuccessful, we can forget about this issue for a long time. A discussion is currently under way with regard to high-speed lines, such as the Moscow–Kazan route. This project ought to be successful, and the state should play a key role here, because if this trial run is not successful, there will be no more high-speed railway lines.

We spent a lot of time deciding which projects to work on first with regard to motorways. We chose the Western High-Speed Diameter between Moscow and St. Petersburg, which goes via Odintsovo. And in the first instance we received guarantees. Just ten years ago, the word ‘guarantee’ from the Ministry of Finance or the Ministry of Economic Development was taboo. Nevertheless, the Government has now agreed to this, in order to ensure that these projects turn out to be successful. Because the success of the first few projects is critical.

Another thing: documents are currently being prepared for the G20, and I would like to thank the B20 for coming up with the recommendation that infrastructure projects should be conducted with the participation of large global funds and development institutions. We must not isolate ourselves, so that each country is only concerned with its own projects. It seems to me that we need more than just a financing fund: we also need a map of global projects, which the development funds of various countries could take part in.

What we need now is staff. It is very important for Russia to have a workforce capable of carrying out technological audits and providing maintenance work for projects. Project management is definitely a problem area. We must learn how to manage projects, and to do that we need staff. Thank you.

**G. Bryansky:**

And what is being done now in terms of training staff? What changes are currently taking place in this field?

**V. Mikhailov:**

I would like to talk about Avtodor. Before we created the company, we hired a team which underwent training. We invited specialists from our banks, and only then did we begin to engage in projects of this kind. Unfortunately, we are currently unable to train specialists ourselves in public-private partnership, because this is not one of the areas of expertise offered by our higher education establishments. This can only be done at the international level. This is another problem that needs to be discussed. The problem of people, that is.

**G. Bryansky:**

The creation of a faculty for public-private partnership is clearly something we ought to discuss with Mr. Mau. Are there any questions from the floor? Please introduce yourselves.

Then we will close our discussion, and I would like to offer each of our participants the opportunity to make some closing remarks. Mr. Mikhailov, we will start with you.

**V. Mikhailov:**

The discussion has been quite interesting. In order to start attracting more private capital, taking account of the constraints which exist in the legal sphere, it is imperative first and foremost to concentrate on legislative initiatives. From the point of view of the financial mechanism, a huge amount of work has been carried out by the Government and by the President's administration over the last two years. It seems to me that many of the ideas which were not implemented three or four years ago have now been properly developed and launched. The question, as our foreign colleagues say, of execution – project management – and the success of the first few projects will of course be key, in order to ensure that the developments of the past two years are brought to fruition rather than squandered. Everything leads to one task: ensuring GDP growth and supporting the development of the whole economy of the Russian Federation.

**G. Bryansky:**

Thank you. Mr. Levitin?

**I. Levitin:**

I would like to thank everyone. The discussion really has been interesting, although it is difficult to have a discussion such as this early in the morning. Nevertheless, in my opinion, it was far from boring. I would like to say that the life-cycle of an infrastructure project is much longer than the life-cycle of the Government that decides to carry out that project. We must ensure that these cycles do not influence the project itself. We must come together to think about how best to do this. Then the word 'partnership', in the phrase public-private partnership, will be spelt with a capital letter, and everything else with a small letter. Thank you.

**G. Bryansky:**

Thank you. Mr. Soloviev?

**Y. Soloviev:**

I would like to support the concluding comments of my distinguished colleagues at this round table. We, for our part, are certainly willing to get involved in the development of all projects, from the initial stages to financial closure. We are relying on experience from around the world, as in all of our projects; we have international partners, and are raising funds on the market in various forms. I would just like to see those 20 years of which we spoke – and that trillion – start being reduced somehow. As they said in the famous cartoon – do you remember? – “We built it, and built it, until at last it was built.” It would be good to see some results. Thank you very much!

**G. Bryansky:**

Thank you. Mr. Kant.

**A. Kant:**

If you want efficiency, if you want technology, if you want innovation in infrastructure, then the private sector is the way forward. But it has to be done through transparency, and competition.

**G. Bryansky:**

Thank you. Dennis, perhaps after this discussion you will want to bring in some changes or additional elements to the work your company has done?

**D. Nally:**

Thanks, but the report stands. The one observation I would like to close with is that this has been a fascinating conversation, which really does point to the complexity of the issues that we are really trying to deal with. I think sometimes we all have a tendency to focus on whether there is one simple solution, a silver bullet, that is out there, which can really address these issues. And I think the answer is fairly obvious – there is not. So the more we can use these innovative and creative practices that are emerging, to deal with some of these fundamental

issues and challenges, I think that is going to move the agenda forward in a positive way, so I would encourage that sort of thinking.

**G. Bryansky:**

Thank you very much, Dennis. I now have fewer doubts, I do not think the future will be so bad after all, and I think we will see economic growth coming directly from the infrastructure sector. Many thanks to you all.