INVESTMENT AND INVESTMENT FINANCE
THE SUPPLY AND DEMAND OF LONG TERM FINANCE
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The Role of Long Term Institutional Investors in Financing Infrastructure

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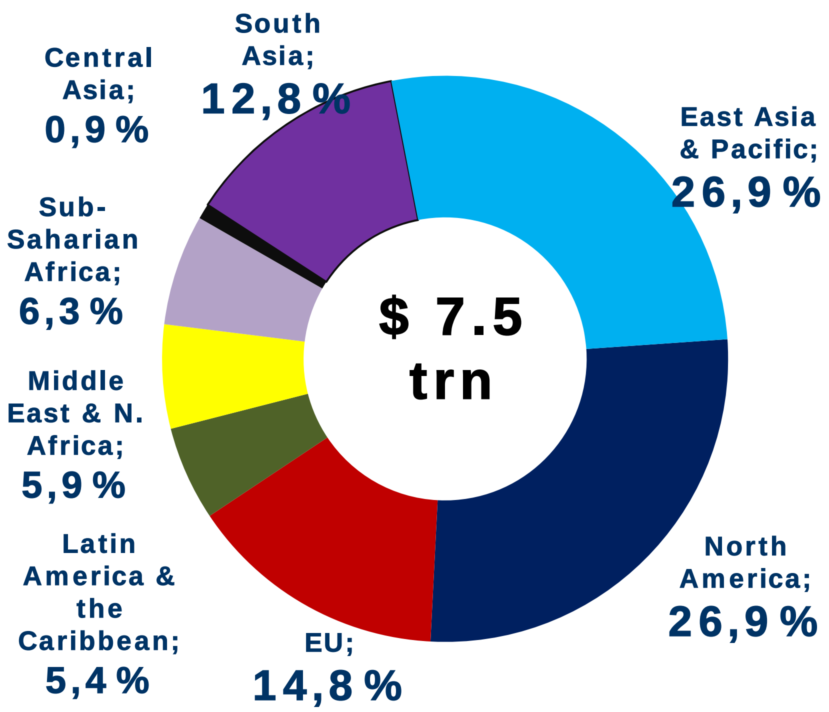
Outline 2

Growing long term investment needs

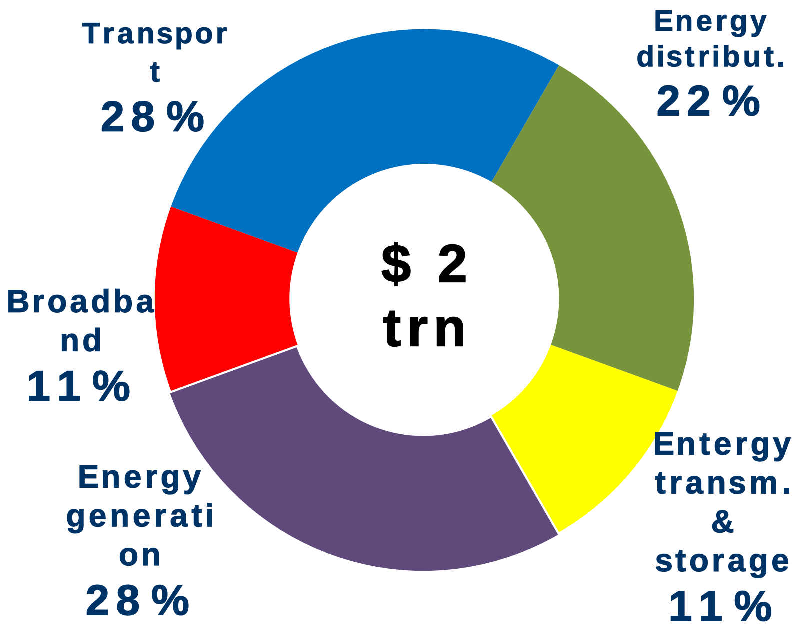
- Between 2013 and 2030, **US$ 50 trillion in capital investment** will be required for roads, water, energy, airports, telecommunications, and rail in OECD countries alone

Global Demand for Infrastructure
(by 2017)



Source: Adapted from Financing Infrastructure HSBC Research, May 2012:

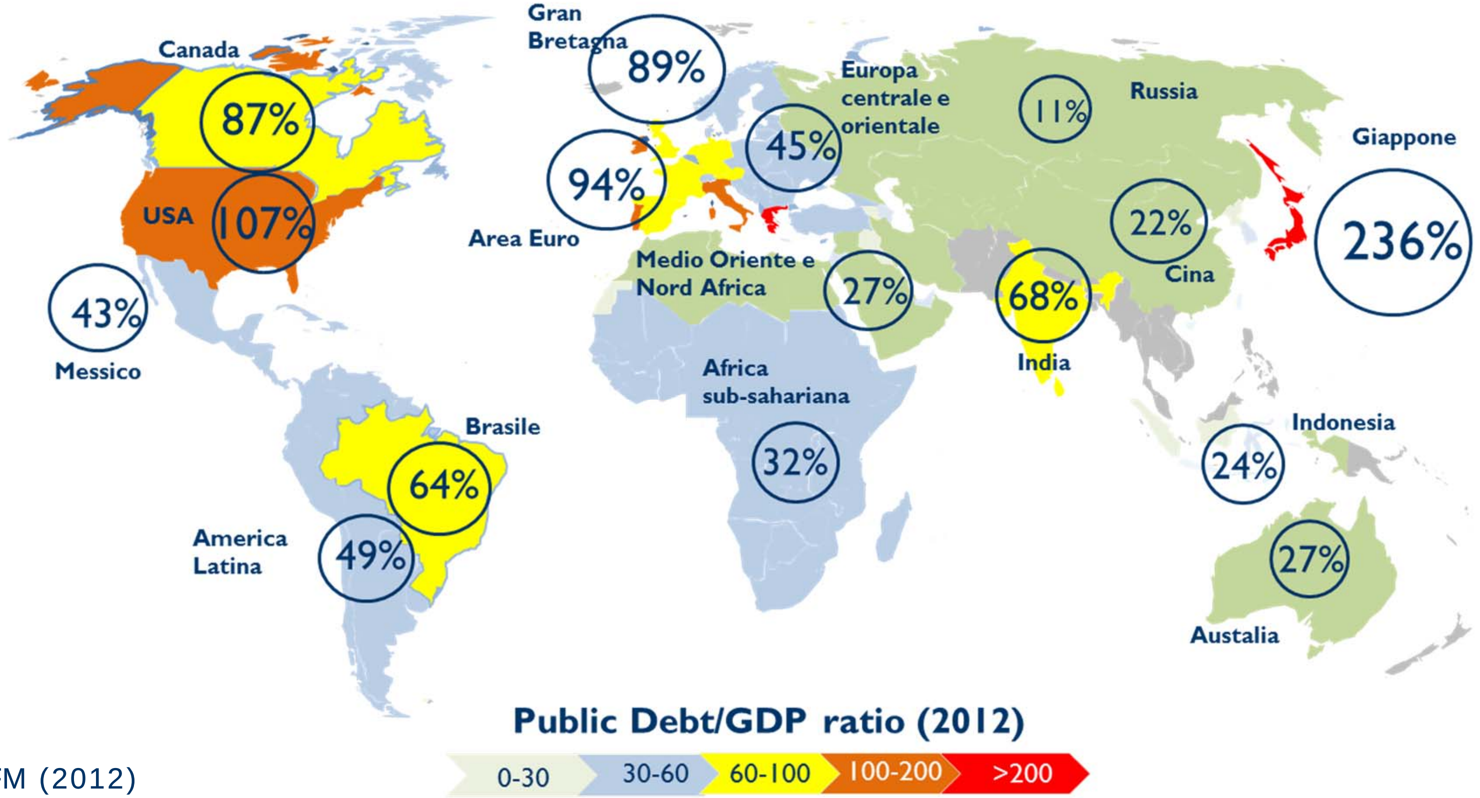
EU Investment Needs
(by 2020)



Source: European Commission

…with higher public budget constraints

- In Europe investments in infrastructure were once financed directly or indirectly from public budgets (equity) and from the banks (lending)
- Now with the **binding public budget constraints** due to Fiscal Compact, increasing recourse must be drawn from **private capital market**
- At the same time, the **European banking system** is in critical condition and has dramatically slowed down **medium and long term lending**



Source: IFM (2012)

The Crisis of Banks and Project Financing in Europe

- Before the crisis, the **European banking system financed over 90%** of the debt component of Project Finance (and more than two-thirds worldwide)
- **Institutional investors** (mainly pension funds and insurance companies) covered **around 40%** of medium and long-term bank lending for infrastructure, acquiring bank bonds and securitised loans for these projects in their portfolios.
- Monoline insurance companies guaranteed risk related to any (temporary) instability in the cash flows generated by the works being financed
- With the crisis, **this model has stopped working**
- Monoline insurance companies have all but disappeared; the new regulations act as a disincentive for life insurance and pension funds to invest in infrastructure assets
- The European banks, which are already having to cope with the crisis and the new more stringent ratios, face (in the peripheral countries) higher funding costs, and have lost confidence in each other, thus making it difficult to syndicate loans, especially medium and long-term exposures
- Together with the decline in public subsidies and the increase in lending costs, **this has blocked many infrastructure investments**
- According to BIS estimates, at the end of 2011, lending for **project financing fell by around 39%** for the weakest European banks and around 18% for the rest

Strong Reduction in Project Finance Lending

Change in lending by type of lender and loan					
	Change in new lending between Q3 2011 and Q4 2011, by type of lender; %			2011 lending volume	
Loan type	*Weaker EU banks*	*Other EU lenders*	*All lenders worldwilde*	*In billions of dollars*	*Denominated in dollars (%)*
All loans	**-16.6**	**-6.0**	**0.4**	**4,181**	**62**
Dollar-denominated	**-16.2**	**2.4**	**4.4**	**2,503**	**100**
Leveraged	**-43.0**	**-43.4**	**-18.3**	**1,085**	**80**
Project Finance	**-39.0**	**-21.4**	**-7.0**	**319**	**40**
Trade finance	**-23.5**	**-9.8**	**-4.6**	**65**	**88**
Aircraft/shift leasing	**-40.5**	**-12.9**	**7.3**	**49**	**85**
Colour coding	*[<-30]*	*[-30 to -15]*	*[-15 to 0]*		

Source: Dealogic, BIS calculations

What could / *should* Europe do?

- A European policy for promoting investment for the EU's growth and competitiveness must act on some new fronts:

1. The establishment of a **regulatory framework** less penalizing LTI in infrastructures and more attractive to private investors (Basel III-CRD IV, Solvency II, IAS, etc.)

2. The development of **new sources of public funds** for LTI

3. The creation of **innovative financial and risk mitigation instruments** (building on the experience of the EU the Project Bond Initiative and of the Marguerite, InfraMed, GIF, SMEG, RSFF, and EEEF Funds)

4. The introduction of **tax incentives** for private investment in infrastructure

5. An **unconventional measure by the ECB** to counter the liquidity crunch affecting LTI (with the introduction of a Very Long Term Re-financing Facility - ***VLTROs***).

6. The introduction of some form of **Golden Rule**, now to be limited to national co-financing of infrastructure projects financed by the EU or by the EIB.

7. And finally, the financing of large EU investment by issuing **Eurobond for Growth**

In the implementation of all these initiatives **Public EU and National Development and Investment Banks may play a crucial role as "policy oriented" European long term investors**

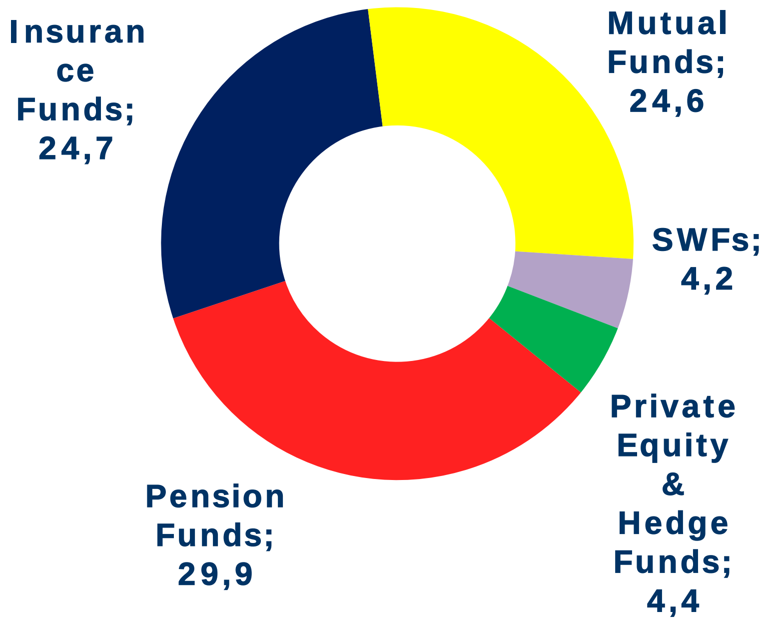
The Role of European Development Banks

- Are we then witnessing a **structural change** in the European economic and financial system with institutional investors partially replacing banks or with companies directly accessing the capital markets?
- A structural change of this magnitude, which would push **Europe closer to the Anglo-Saxon model**, has a long way to go. More likely, the European system will evolve into a hybrid model, in which the banking sector will continue to play an important, but not exclusive role in financing the real economy
- While waiting for a return of stability in the European banking system, the role of **long-term institutional investors** will become increasingly important
- As regards so-called public development and/or investment banks (EIB, KfW, CDC, CDP, etc.), the **change is already on the way**
- **New financial instruments** have been designed; **additional resources** have been mobilized to support the economy during the crisis (by **financing infrastructure and SMEs**)
- New European and domestic **long-term equity funds** have been launched to invest in infrastructure projects and strengthen company capitalization
- But it is obvious that by themselves they cannot meet the funding needs for the huge volume of investment envisaged in the Europe 2020 agenda

The Long Term Institutional Investors

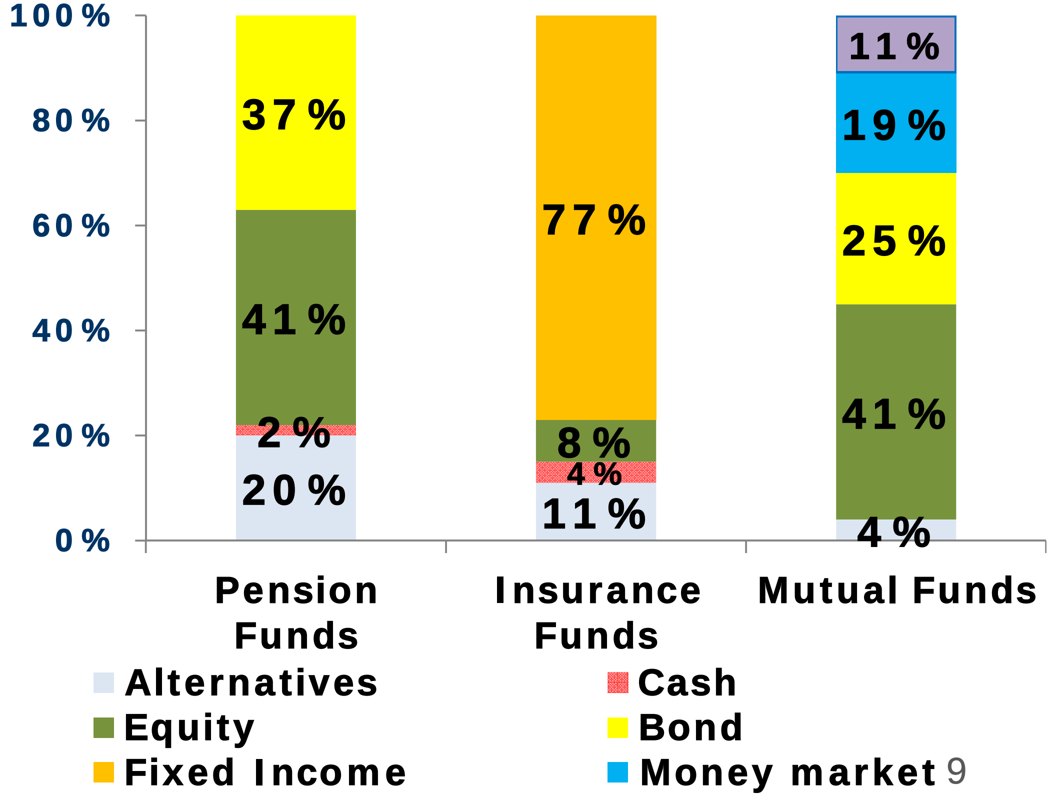
- Other long-term institutional investors, such as insurance companies and pension funds, can become major investors in infrastructure as an asset class (but regulatory adjustments are required)
- Total Assets of Long Term Institutional Investors are estimated at **$ 87.8 trn**

Total Asset under Management

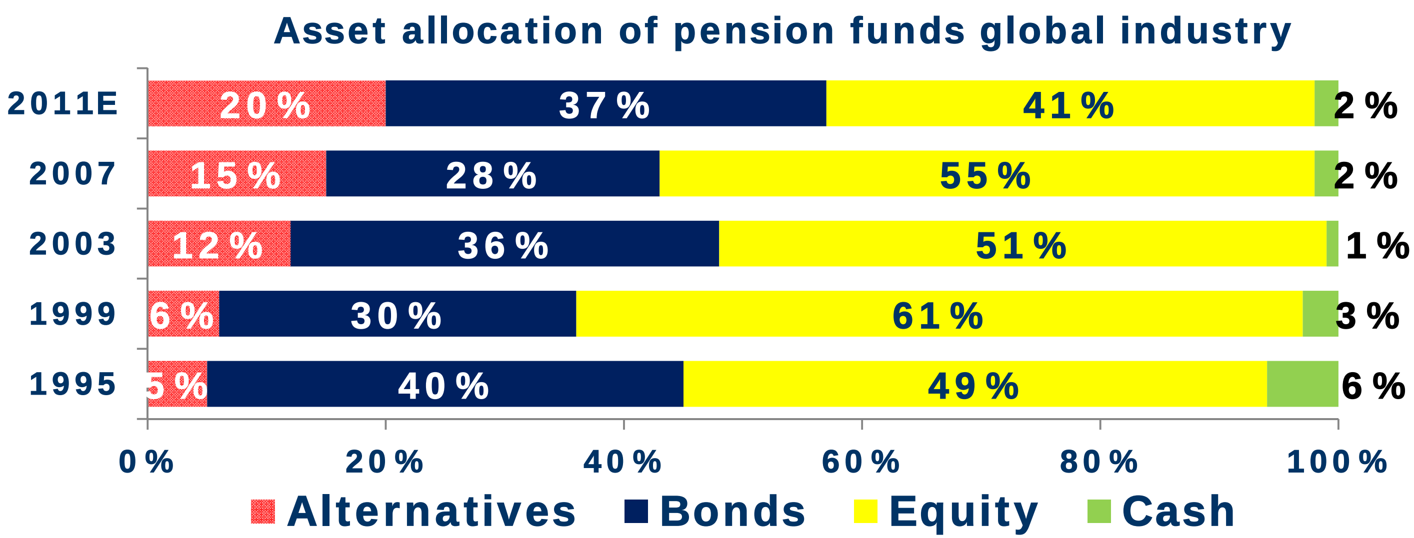


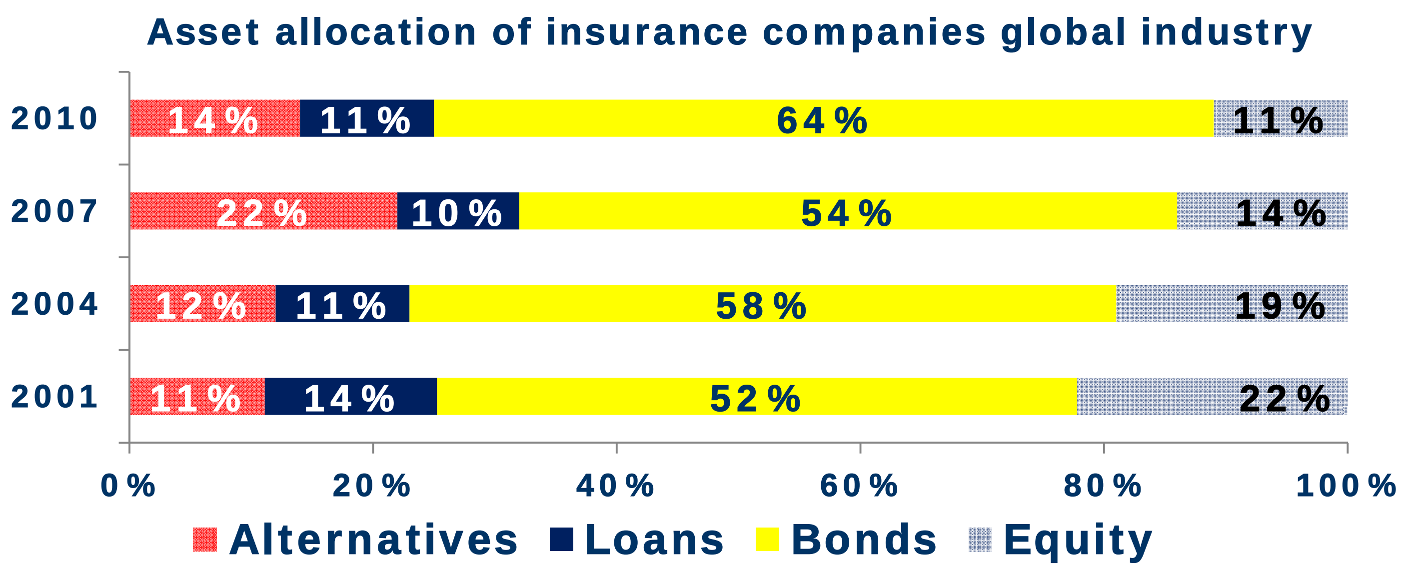
Source: OECD

Asset Allocation



Pension Funds and Insurance Companies

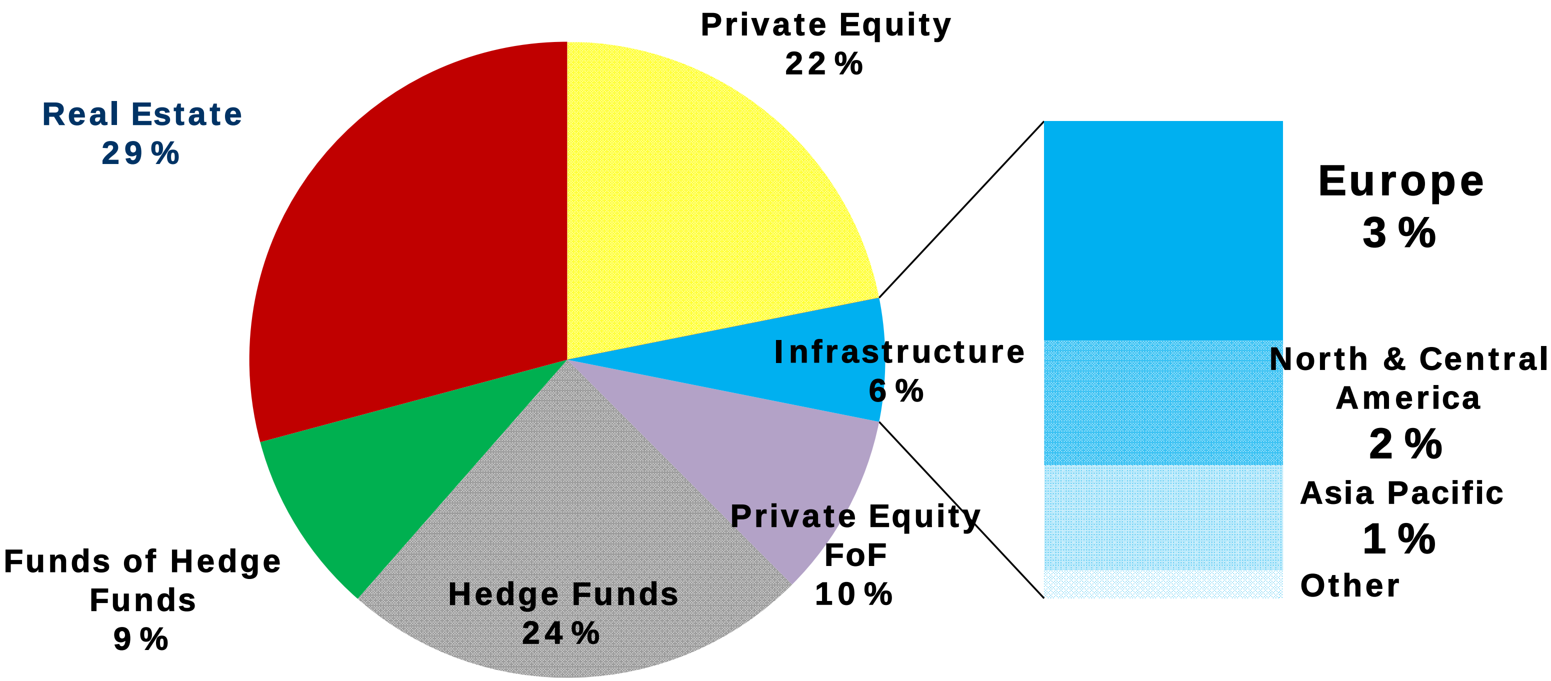




Source: PF: Tower Watson Pension Assets, Study 2012; IC: OECD,2012

Long-term investors' allocation to infrastructure

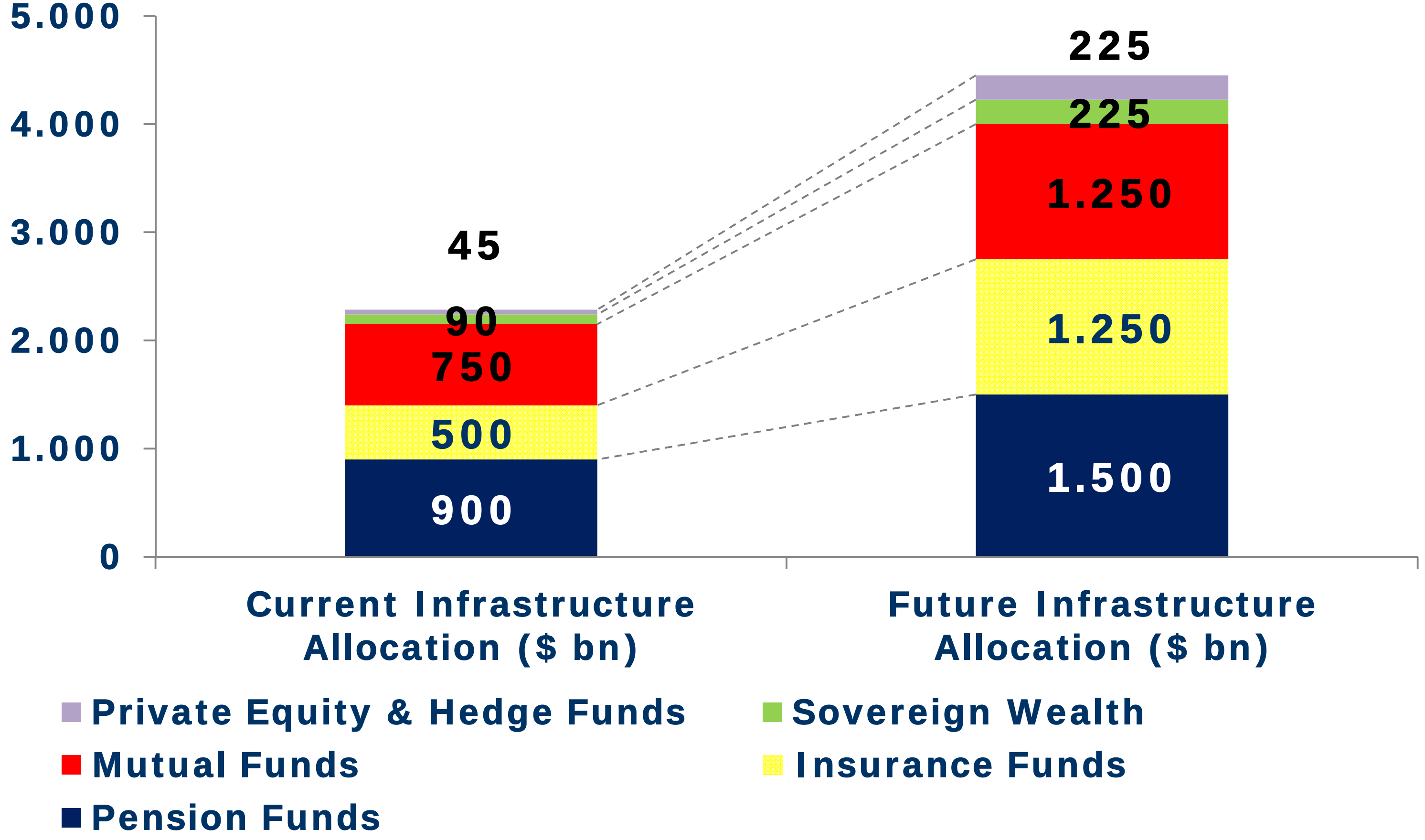
- Infrastructure investment allocation is about the 6% of "*alternatives*" assets (infrastructure investment in Europe is about 3%)
- The large majority of infrastructure investment that has been made is in the form of unlisted equity (90% of total)
- Globally, **about $ 2.3 trn** allocated to Infrastructure Investment



Source: Tower Watson Global Alternatives Survey , 2012

Potential LTIs financing of infrastructure investment

- Potentially, Long Term Institutional Investors investment can **grow up to about $ 4.5 trn** (5% of total AUM, according to a recent Study by HSBC). The goal is reasonable and the increase of resources for infrastructure quite outstanding in size



Concluding Remarks

- **Long Term Investment** plays a fundamental role in sustaining growth, fostering competitiveness and ensuring the conditions necessary for financial stability and the consolidation of the public finances

- In the current economic environment, resources for funding LTI can no longer come primarily from government budgets or from banks

- We need to create the **conditions for promoting the entry of private capital**

- More specifically, long term institutional investors can play an increasingly important role

- However, substantial changes in public and **regulatory policies and new financial instruments are needed**, both at the European and national levels, to encourage, or at least not penalise, LTI

Concluding Remarks

- At European level, the Commission is preparing a **Green Paper** to identify rules, conditions and instruments that could foster the flow of private capital into LTIs

- Internationally, the **Russian president of the G20** is going to propose that the issue of LTIs financing be given priority status on the agenda for 2013

- **The persistence of the crisis** obliges all of us to acknowledge that, in a modern market economy, **financial stability, growth and social cohesion are inextricably intertwined**, and that investment is a key factor not just for growth and competitiveness, but also for the stability of financial institutions and for rebalancing the public finances

- It would have been better to understand this earlier. But, as always, **better late than never**

Mission

A joint stock company under public control,
stake owned by the State and by a broad group of private banking Foundations

MISSION: SUPPORTING ITALY'S GROWTH

MEF — **70%**

65 PRIVATE FOUNDATIONS — **30%**

cdp

Leader in financing **Local authorities** and **PA**

Catalyst in developing the country's **infrastructure**

Key player in supporting **economic development**

Lines of business

	DEBT	EQUITY
PUBLIC AUTHORITIES	✓ Lending	✓ FIA – Fondo investimenti per l'abitare ✓ FIV – Fondo investimenti per la valorizzazione
INFRASTRUCTURE	✓ Corporate financing ✓ Project financing	✓ F2i – Fondo italiano per le infrastrutture ✓ Marguerite Fund ✓ Inframed Fund
ECONOMIC DEVELOPMENT	✓ SMEs Plafond ✓ Export Banca ✓ Kyoto Fund	✓ FSI - Fondo Strategico Italiano ✓ FII – Fondo Italiano di Investimento ✓ EEEF – European Energy Efficiency Fund

Main equity investments and funds

LISTED COMPANIES
(CDP SHARE; BOOK VALUE)

- **ENI Spa** *(26.4%; € 17.2 bln)*
- **Terna Spa** *(29.9%; € 1.3 bln)*
- **Snam Spa** *(30% - 1 share)*

UNLISTED COMPANIES
(CDP SHARE)

- **TAG - via CDP GAS** *(89%)*
- **FINTECNA** *(100%)*
- **SACE** *(100%)*
- **SIMEST** *(76%)*

PRIVATE EQUITY
(CDP COMMITMENT)

- **FSI – Fondo Strategico Italiano (€ 4 bln)**
- **FII - Fondo Italiano d'Investimento (€ 250 mln)**
- **F2i – Fondo Italiano per le Infrastrutture (€ 151 mln)**
- **Marguerite Fund (€ 100 mln)**
- **InfraMed Fund (€ 150 mln)**
- **Fondo Investimenti per l'Abitare (€ 1 bln)**
- **Fondo Investimenti per la Valorizzazione (€ 250 mln)**
- **European Energy Efficiency Fund (€ 60 mln)**

Corporate | Infrastructure | Other

2012 CDP Preliminary Figures and Main Facts

ASSETS

Total assets: over **€300 bln.** customer and bank loans: +2%, amid a larger market stagnation

LIABILITIES

Almost **24 million clients, about 10% of national household savings. Stock** over **€230 bln. Net funding** around **€10 bln**

SME LOANS

€18 bln in 2 years for about **60.000 SMEs**

EXPORT FINANCE

€4-bln fund supporting **exports** and **international expansion** for companies

AQUISITIONS

30% **SNAM**, 100% **SACE**, 100% **FINTECNA**, 76% **SIMEST**

NET INCOME

Over **€2 bln** forecast in the business plan for 2012, up from €1.6 bln of net income in 2011.