Asia-Pacific Green Deal for Business Roundtable: Building smart, low carbon, climate-resilient infrastructure in developing countries

Report of Meeting held 1 November 2023, Vientiane, Lao PDR

ESCAP
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1. Introduction

THE IMPORTANCE OF INFRASTRUCTURE FOR SUSTAINABILITY

The impacts of climate change are becoming more apparent on cities and communities across the Asia-Pacific. As such, the necessity of resilient infrastructure for ensuring sustainable development is now well-recognized. Infrastructure designed to withstand the effects of natural disasters and to cope with the changing climate plays a crucial role in safeguarding the well-being of citizens and facilitating the continuous operation of essential services. Properly designed infrastructure not only enhances economic opportunities, leading to job creation and poverty reduction but also, when imbued with resilience, diminishes the risks of damage and losses resulting from climate-related events and other disasters. Therefore, investing in resilient infrastructure is a vital component of climate change adaptation strategies.

Constructing infrastructure in less affluent countries, especially in the Least Developed Countries (LDCs) and Landlocked Developing Countries (LLDCs), poses myriad challenges. Chief among these challenges is the scarcity of funding, given the limited resources, low levels of foreign investment, and the high-risk profile of LDCs and LLDCs. Other obstacles include weak institutions, geographical barriers, competing priorities, lack of technical expertise, and issues related to corruption, all of which impede infrastructure development in these nations.

To overcome these challenges, a concerted effort is needed, involving collaboration between governments, international organizations, and private sector entities.

The detail of this report is drawn from the discussions at a meeting organized by ESCAP and the ESCAP Sustainable Business Network, held on 1 November 2023 in Vientiane, Lao PDR. The meeting brought together a range of stakeholders from both the public and private sectors to talk about the challenges and good practices for building sustainable and resilient infrastructure, and utilization of private sector expertise in this realm.
2. Private sector approaches to sustainable infrastructure development

Many private companies, especially large companies dealing in infrastructure development or adjacent areas, have significant pressures on them to become more sustainable. This arises from their close dealings with governments that are also pursuing sustainability goals, but also from their consumers, and out of concern for their public image. Currently, the Science Based Targets Initiative (SBTi) is known to be one of the most demanding and respected programs that companies can commit to if they wish to demonstrate their sustainability credentials. MTR Corporation, for example, which is a public transportation provider (rail transit) based in the Hong Kong Special Administrative Region of China, has an overall target of carbon neutrality by 2050, and further Science Based Targets for 2030. In holding the current chair of the ESBN task force on Green Infrastructure, MTR seeks to promote and exchange best practices in the region, as well as advocate for publicly committed carbon reduction targets for Asia-Pacific infrastructure businesses. Publicly committed targets are important for keeping companies accountable and avoiding greenwashing.

In the domain of large infrastructure, sustainability is now well and truly in the public consciousness, and decision-makers at all levels are striving to implement better sustainability practices. Technologies for greening infrastructure are being developed and implemented at very high rates however, infrastructure tends to be long-lived, and as such, the payoff in carbon reductions from building better projects will not arrive until some time in the future. Nevertheless, building better now can save on carbon emissions and save costs in the future through greater resilience to a changing climate and natural disasters.

Private companies that build infrastructure such as transit, commercial developments, and energy are incorporating more detailed factors into their lifecycle analysis for projects. Sustainability needs to be a consideration from the design and planning, the construction, the operation, and then also finally the demolition and decommissioning of infrastructure. Companies such as Swire Properties are embedding ESG decision-making processes at high levels of the company to ensure the fulfillment of business strategies that prioritise environmental sustainability, as well as profit and economic sustainability.

Given that developing countries are
particularly finance-constrained, prioritizing projects is of key importance. This is an area where governments can seek private sector involvement, as both entrepreneurs and established companies alike can contribute to a multi-stakeholder dialogue that establishes where the most critical infrastructure gaps are. For many developing countries, agriculture is an important part of their economy and a contributor to export earnings, and as such investment in agribusiness and rural infrastructure remains important even while seeking to modernize the economy.

Nevertheless, developing countries are still making large gains in sustainability, and are not necessarily short of entrepreneurs who are motivated to make green investments and employ green business strategies. In economies with large informal sectors, small entrepreneurs will be critical in developing more sustainable approaches to business, and they can take advantage of opportunities offered by banks and other financiers for smaller, pilot programs that focus on green loans. As in more developed economies, stock exchanges (such as the Chittagong Stock Exchange in Bangladesh) are playing a role in facilitating information transparency and promoting ESG approaches, which can see more sustainable companies get better access to finance from sustainability-focused investors.
3. Financing better infrastructure via private capital and multilateral development banks

International institutions and governments alike are observing that the sustainable infrastructure financing gap is too large to be covered through government spending alone. For this reason, governments are partnering with companies and banks to set up climate-smart public-private partnerships. While this is not in itself a new development, the importance of including climate- and disaster-related risks is increasingly becoming an area of focus.

Both multilateral development banks such as the World Bank and the Asian Development Bank, and private sector capital providers are capable of deploying blended finance. Blended finance recognizes that private capital requires a market rate of return – however, by taking advantage of catalytic funding from public or philanthropic capital that can accept a lower rate of return, private capital can enter into projects that may achieve an overall below-market payoff. This means that governments and development banks can leverage private capital – for each dollar of public investment, multiple dollars of private investment can be unlocked.

International development banks like the World Bank and the Asian Development Bank have a wealth of practical experience that is regularly deployed to advise developing nations on building successful PPPs. This experience comes from the legal and policy side, relating to PPP institutions, as well as the more technical side that can advise on specific projects, whether they be regarding water, energy, transport, or waste management.

Mature PPP markets take a long time to develop. In addition to establishing an appropriate legal environment, project preparation, and project pipelines, the formation of consortiums willing to invest, and confidence in a government’s commitment are all factors that build over an extended period.

Risk allocation is an area of PPPs that receives much attention and with good reason. At times, governments with relatively little PPP experience try to shift too much risk to the private sector. This can be problematic, however, for several reasons. Firstly, the best investors will not bid on projects that are perceived as having unbalanced risk allocation. Secondly, an inappropriate balance of risk can lead to disputes occurring early in the project period and demands for early renegotiation of the contract. Still, governments should be
aware that not all climate-related risks need to be borne by the public sector. With appropriate contract provisions and insurance markets available, the private sector is capable of managing climate risk.

Solicited proposals, drawn from an established process for building a project pipeline, remain the best practice for PPPs. While there is some perception that unsolicited proposals can allow governments to get PPPs implemented faster, it is underappreciated how much these can create reputational risk. High-quality investors have been known to prefer competitive tenders for solicited proposals, as this is a signal of a committed government and shows that there is a lower risk of disputes over a contract midway through a project’s life, or following a change of government.

Greenwashing is receiving more and more attention from private financiers of infrastructure. Funds that specialize in green capital are highly sensitive to accusations of greenwashing, however, negotiating this space is difficult when there is no agreed definition, standard, or guidelines that apply across the region. As such, to bring more funds into the sustainability space, there is good reason for governments to seek to cooperate on transparency, reporting standards, and data requirements for green investments.
4. Challenges of development: the experience of Asia-Pacific Countries

The world’s developing countries, landlocked countries, and other countries in special situations such as the small island developing states (SIDS) face great risks due to a changing climate. Rising sea levels, changing weather patterns, and increased exposure to floods, cyclones, and other disasters all weigh heavily on the growth prospects of developing economies. Forecasting climate risk is particularly difficult in developing countries, as the data gaps are more severe than in wealthier economies.

To achieve their development goals, a number of less wealthy countries have turned to PPPs with varying degrees of success. Countries such as Cambodia have a relatively longer history of pursuing PPPs and have established institutions, frameworks, and government experience in working with the private sector. Partnerships with the private sector are often viewed as a natural way of pursuing the government’s sustainability strategies, whereby it can direct private investment towards sustainable energy, disaster mitigation, waste management, or other sectors it deems a priority.

The Philippines is one country that has achieved some success with PPPs, however, most of the funding has come from domestic banks rather than international sources. The framework for PPPs in the Philippines is typically strongly output-based: that is, the goals for the project are set and relatively little control is exercised over the intermediate parts of the process. This means that integrating sustainability requirements can be challenging. Introducing standards for green procurement, or sustainability metrics for construction will constitute a more intrusive role of government in PPP projects, and might be unfavorably received by investors. Going forward, however, there may be some changes to this established practice to exercise more control over climate and sustainability-related aspects of projects. An enduring problem faced by developing countries is the reliance on partners such as the ADB or consultants for expertise in deal structuring and project preparation. While governments make many efforts to retain talent and suitably train their PPP staff, it continues to be difficult for the government to compete with other entities providing more attractive employment opportunities.

One interesting example of PPP implementation is provided by the Kyrgyz Republic. In this country, PPPs tend not to be large and complex projects but rather smaller projects, such as the development of sporting facilities or healthcare centers. In the
experience of the Kyrgyz Republic, focusing on smaller projects enables faster project completion, faster generation and recycling of investor funds, and lower risk. A unique circumstance of this country that lends itself to this model is the existence of a large number of unused or underutilized government assets.

The PPP model enables the government to better utilize these assets and provide services to the population without outright relinquishing control over them.
5. Recommendations

1. Sustainability-focused infrastructure companies should be publicly committing to sustainability targets, such as the Science Based Targets Initiative (SBTi). Companies that publicly commit can use their influence and reputation to advocate for public targets in business forums and through business chambers. In this way, a culture of sustainability can be further encouraged throughout the region and spread to other companies that are at an earlier stage of their sustainability journey or have weaker internal targets.

2. Risk allocation in PPPs is generally a difficult area of negotiation, however, risks related to climate change and disaster resilience don’t need to be entirely left on government books. By carefully considering climate-related risks and working to establish appropriate terms with insurers, private companies can position themselves to accept these risks and governments should negotiate accordingly. Nevertheless, the appropriate allocation of risks between the government and the private sector is in everyone’s interest, as an unbalanced allocation can lead to contract disputes early in a PPP’s life.

3. Solicited proposals remain best practice for choosing PPPs. In developing countries in particular, investors may consider that unsolicited proposals increase the risk of contracts being altered or disputed during changes of government or other dramatic circumstances.

4. Private finance can be further mobilized by taking advantage of blended finance, improving data transparency, and developing green standards. Sustainability funds are motivated to align investment with government policies on sustainability, as this builds their credibility. Investors motivated to invest in green projects can be mobilized to contribute where government capital is already playing a seed role. To alleviate concerns about greenwashing, guidelines, and standards allow investors to allocate their money with confidence.

5. It takes a long time for PPP markets to come to maturity. If circumstances allow, there may be potential for developing markets to develop smaller PPPs that encompass fewer risks, less complex contracts, and lower finance requirements. In this manner, governments can simultaneously build expertise in managing PPP projects while also building the reputation required to generate investor interest in larger and more complex projects. In addition, the multilateral development banks have extensive training programs and advisors available to help governments leverage private expertise for sustainable infrastructure development.
6. The private sector could drive costs down to achieve higher returns on investment in infrastructure. However, in terms of a project’s sustainability outcomes, this relentless focus on lower costs may come at the expense of the environment or resilience to disaster. While contracts that focus solely on output tend to be less complex and more easily managed, governments may need to assert some degree of control over the intermediate processes of building infrastructure in order to achieve the kind of sustainability results they desire.
ABOUT THIS MEETING

On 1 November 2023, a cross-section of infrastructure, economics, and policy professionals from the Asia-Pacific region gathered in Vientiane, Lao PDR, to discuss how the private sector can work to facilitate better infrastructure in developing countries. With a focus on climate resilient and green infrastructure, and on the particular experiences of countries that may be landlocked or least developed countries (LDCs), participants shared their viewpoints across topics such as financing infrastructure, developing expertise within government PPP units, and private sector involvement in development.

The meeting was held by the ESCAP Sustainable Business Network, in partnership with ESCAP and the Investment Promotion Department of the Ministry of Planning and Investment, Lao People’s Democratic Republic.
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