

Thought you may find the attached article -- regarding China ACM's large and rapidly growing addressable market -- of interest.



Challenges for the foreign investor in infrastructure

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Despite huge state spending, the mainland's infrastructure market remains fraught with difficulty for foreign investors.

White elephant projects built simply to generate jobs, excess capacity that remains idle while investors await returns and delays in getting deals done are often the realities of the sector. "The danger with China's approach to infrastructure investment is that it may be viewed as an end in itself rather than as a means towards growth," Michael Spencer, Asia-Pacific chief economist at Deutsche Bank, said.

Spencer was one of several speakers at the recent Infrastructure Investment World Asia conference in Hong Kong, which drew dozens of executives, analysts, economists and investors.

"When you initiate infrastructure projects mainly because you're trying to maintain employment, you won't necessarily build the right infrastructure," he said. "In many Chinese cities, you see massive and opulent city halls. Promoting future growth doesn't seem like the main objective there."

Beijing's approach to infrastructure seemed often to be "build it and they will come", he added. "It is probably true that if you wait long enough, the capacity will be used up," he said.

"But by putting in place infrastructure like toll roads or airports long before there is a commercially sustaining demand, the government is displaying a willingness to tolerate depreciation costs over the next 10 to 20 years that is probably greater than private investors can bear."

John Stuart, chief executive of Macquarie Infrastructure Management (Asia), said building excess capacity on the mainland made sense because it was likely to be used up since the country was enjoying high economic growth. "But for investors, there are challenges with

immediate returns and cash flow," he said.

An executive with a leading US bank said foreign investors found infrastructure deals on the mainland often took longer to close than might initially seem the case. "This is not a good thing for foreign investors, as they have to commit manpower before they know if they have a deal," the executive said.

Many private infrastructure investment teams in Asia were new and lacked track records, said Joseph Chang, vice-president of SCM Strategic Capital Management Asia, a Swiss provider of management and consulting services for investments in infrastructure, private equity and real estate. "That's why many funds are not eager to invest in infrastructure in Asia," Chang said.

However, Spencer said: "The advantage China has over India is when China decides to spend US\$600 billion on infrastructure over the next several years, there's a warehouse of ready projects and the government's decision-making processes are faster."

In late 2008, to counter the global financial crisis, Beijing launched a 4 trillion yuan (HK\$4.57 trillion) stimulus to be spent by the end of this year. Nearly half the amount is devoted to infrastructure such as airports and the railways.

The budget of the mainland's Ministry of Railways over the next 10 years was US\$730 billion, Jeremy Goodwin, president of China Advanced Construction Materials Group (China ACM), said.

But as of January 2009, foreign investment in all infrastructure sectors of the country was no more than 4 per cent, according to McKinsey.

In the water market, the government accounted for 78 per cent of investment, while domestic private investment accounted for 16 per cent and foreign investment only 6 per cent, Christoph Graf von Waldersee, managing director of Asia Water Development Corp, said. "This is a dramatic imbalance."

Goodwin said: "It's very difficult for a new player to break into China's high-speed railway because of stringent local standards. The Ministry of Railways is reluctant to outsource because of its high quality requirements."

Goodwin's company is the only private supplier of concrete to the mainland's high-speed railways. China ACM, a private mainland firm listed on the Nasdaq, has also supplied concrete to prominent Beijing landmarks such as the CCTV tower, the Bird's Nest Olympic Stadium and the Water Cube Olympic swimming complex.

One reason China ACM had been able to win contracts for major projects was the background and connections of the company's founding chairman, Han Xianfu, Goodwin said. Han was a party secretary of a Beijing state-owned municipal construction company

and a former chairman of the Beijing Concrete Association.

The advantages of China ACM's founder were his local knowledge, experience, track record and references, Goodwin said. "In China's high-speed railway, you need to have good relations with the contractors."

International institutions like the Asian Development Bank are helping foreign investors break into the mainland's infrastructure market. The bank was in discussions with the government to let public-private partnerships take over some infrastructure projects like roads and water treatment funded by local government investment vehicles, Michael Lindfield, lead professional in urban development at the ABD, said.

Beijing had recently clamped down on the local government investment vehicles, because they have incurred trillions of yuan of debts from funding infrastructure projects, Lindfield said. "This is an opportunity for the private sector. It's something we support."

Right now, Goodwin said: "Chinese officials make out that money is not an issue in the short term."

About US\$20 trillion is needed to be spent on all infrastructure sectors on the mainland in the next 20 years, he said. "I don't think the Chinese government will invest all that ... China's infrastructure needs to be funded by the private sector as well, because the figures are dizzying."

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