

ASEM conference: Investment and its Financing
What causes private investment to remain
relatively low in Asia?

Experiences from Europe for better channelling savings to investments

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Channelling savings to investment is a major challenge

Channelling savings to investment is important for growth:

- Produces information about investments and allocates capital
- Monitors investments and exerts corporate governance
- Facilitates the trading, diversification, and management of risk
- Mobilizes and pools savings
- Eases the exchange of goods and services

Finance is the transmission channel:

- If it functions well, the financial system helps increase productivity, e.g. through the selection and monitoring of investment.
- Young and innovative enterprises demand a flexible financial structure
- There is no evidence that market-based systems are superior to bank-based financial systems: legal issues ruling investor protection and transparency are paramount.



Why savings often do not flow downhill?

1. Because of the lack of domestic investment projects (or the lack of structures to identify and prepare them)
2. Because of inadequate infrastructural networks
3. Because of inadequate financial intermediation systems
4. Where the share of investment is relatively low: because of risk-aversion
5. Corporate tax regimes
6. State monopolies in some sectors
7. Barriers to entry



Why savings, even if they flow downhill, sometimes go to the wrong place?

1. Short-term (speculative?) capital flows to emerging market economies
2. Savings flow to bubble-prone sectors (in primis real estate)
3. Volatility and financial instability risks



The need to find a sound institutional setting and financial intermediation that would help markets allocate savings efficiently

The European experience:

1. To channel regional savings to regional investment: integrated financial markets
2. Infrastructure/project-based investment (e.g. EIB) and PPPs: a structured framework, to avoid politicisation
3. Early identification and some mechanism to reduce intra-EU imbalances



The European experience with integrating financial markets

Advantages of having better regionally integrated capital markets:

- to avoid the hurdles in cross-border investment flows and facilitate cross-border mergers and acquisitions (economies of scale and scope)
- coordinating financial legal frameworks, legal protection of stockholders and creditors increases the efficiency of corporate governance and performance, which can influence returns
- Single market (banking and financial industry)

The European experience with integrating financial markets

- Comparing European and Asian financial markets: European bond markets are more integrated.
- East Asian countries can gain by mobilising more of their capital between them to rebalance the savings-investment gaps.
- How much of the exported capital from East Asia should circulate within the region is hard to quantify. But if the level increased substantially, the returns would be large.

http://ec.europa.eu/economy_finance/publications/economic_paper/2010/pdf/ecp423_en.pdf

The European experience with infrastructure/project-based investment: the European Investment Bank

- EIB makes long-term finance available under favourable conditions.
- EIB bonds are of the highest credit quality. The EIB is rated triple-A by Moody's, Standard and Poor's, and Fitch.
- Factors backing the EIB's credit standing and triple-A rating include:
 - Joint European sovereign ownership and support
 - Outstanding asset quality
 - Conservative risk management
- EIB loans are a complementary source of financing: up to 50% of total project cost.



Advantages of this type of infrastructure/project bank

Transparent source of financing / co-financing and monitoring of projects (de-linked from political pressure) => governance issue

A new triple-A rated issuer

Assists the region according to its own development and policy goals

Mobilises resources and adapts projects to local needs (requires also technical assistance structure)

Spurs long-term projects and helps job creation



The European experience with public-private partnerships

Ability of governments to finance huge infrastructure is becoming increasingly limited

How do public-private partnerships enhance investment?

- Risk-sharing between public and private sectors
- Long-term relationship between parties
- Public service and ultimate regulatory responsibility in public sector's hands

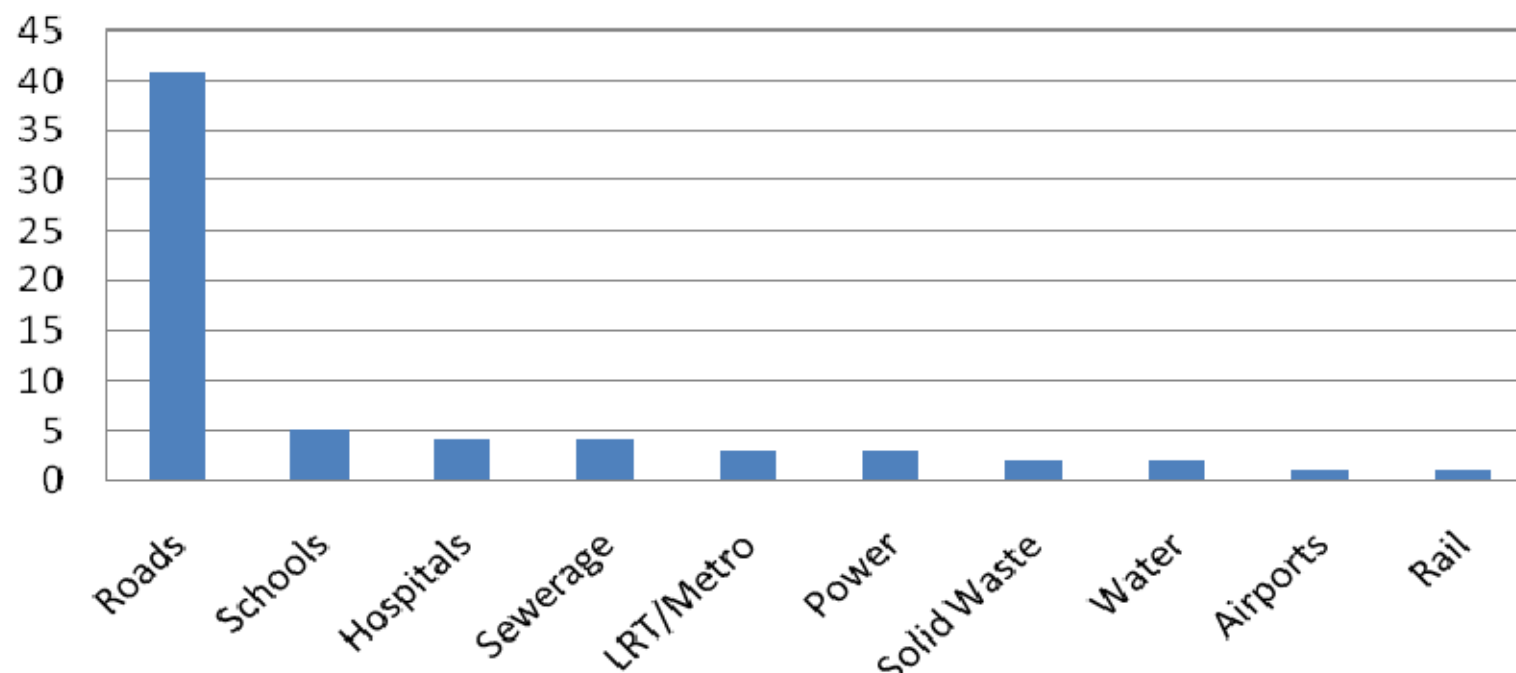
Somes success stories:

- EPEC, the European PPP expertise centre: Third PPP Forum 13/12/2010 <http://www.eib.org/epec/>
- ASEM conference on PPP in infrastructure, organised in Seoul in 2009, PPP experts' forum 13/12/2010 in Brussels



EIB public-private partnerships

Completed PPP Projects by Sector



Early identification of imbalances is important

Some European thoughts:

- Monitoring **macro-economic imbalances** such as large current account deficits or bubbles in housing markets (which are harmful for growth and stability)
- Devising an **alert** mechanism based on indicators and thresholds
- Issuing policy **recommendations** and sanctions.

European Semester:

1. integrated macro- and structural surveillance of fiscal policies, key structural reforms that address growth bottlenecks, macro-imbalances, and financial systems.
2. and ex-ante policy advice: Commission and Council prepare guidance, opinions and recommendations at a time when important budgetary decisions are still in a preparatory phase at the national level.



Better channelling savings to investments...

Mechanisms or institutions are needed, to address the mismatch between savings and investments

Regional financial integration can raise the depth and liquidity of bond markets and keep the savings in the region

If appropriate solutions are put in place, no need to resort to capital controls; strong surveillance and a set of macro-prudential measures will suffice

Role of financial safety nets

Capital should flow downhill and have a positive impact on growth

