

Decoding the National Investment and Infrastructure Fund: An Exploratory Study

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ABSTRACT

Sovereign wealth funds (SWFs) are government owned and managed investment vehicles used to further some pre-determined macroeconomic and/or development objective. The National Investment and Infrastructure Fund (NIIF) incorporated by India is a quasi-sovereign wealth fund, partly funded by the government and partly by other national and international financial institutions including sovereign wealth funds of other countries. The objective of NIIF is to create a pool of money large enough to finance major infrastructure projects in the country and bridge the deficit in infrastructure financing in India. This article is an exploratory study which attempts to bring together information pertaining to NIIF from various sources and explain its concept, functioning and potential. We conclude with a critical assessment of the idea and questions for further research.

1. Introduction

We are a vibrant country of 1.3 billion people. We have the highest GDP growth rate in the world, the third largest GDP by PPP and are among the top 20 most important destinations for FDI in the world. But despite these achievements and after 70 years of independence, we are still the nation with an infrastructure investment deficit that is “simply too large to eliminate anytime soon” (S&P Global Ratings 2018). As per the Economic Survey 2018, India is expected to face a \$526 billion gap by 2040. According to an estimate given by ex-finance minister, Mr. Arun Jaitley, India needs to spend anywhere between 1 to 1.5 trillion US dollars over the next 10 years to realize its true growth potential and bridge the huge infrastructure gap. That’s 150 billion US dollars annually and almost 7% of our current annual GDP. As of now, infrastructure investment constitutes only 5% of our gross domestic product. Of course, an increase of 2% does not seem to be an unachievable goal in itself, but when you’re talking about the largest democracy of the world trapped in a vicious cycle of poverty, hunger and inequality, it is hard to imagine where this 2% would come from. The stressed assets problem being faced by the banking sector has only aggravated this problem. Nevertheless, a crucial and rather innovative step in this direction has been the setting up of the ambitious National Investment and Infrastructure Fund, as announced in the budget of 2015. This article seeks to develop an understanding of the novel idea of NIIF, its structure, functions and developments so far. We conclude with a summary of findings and critical assessment of the fund.

2. Research Methodology

This study is an exploratory work which assimilates and synthesizes secondary data and information relating to sovereign wealth funds, as available in the public domain. We go through government reports, press releases, newspaper reports and all data available on the NIIF website to provide a holistic view of the fund to the readers.

1. What is the National Investment and Infrastructure Fund?

The National Investment and Infrastructure Fund is an entity formulated by the government to attract investment in infrastructure. It is 49% funded by the government with a sum of \$3 billion (Rs. 20,000 crores) and the rest is expected to be raised from other private institutional players such as sovereign wealth funds, mutual funds, pension funds etc. The entire collection is to be invested in infrastructure finance companies such as Indian Railway Finance Corporation Limited (IRFC) and National Housing Bank Limited (NHB), which lend money to the ultimate developers. The motivation behind NIIF is multifold. Emphasis is being placed on increasing the share of equity participation in infrastructure projects, which is largely missing from the Indian scenario. Government estimates show that with an initial equity corpus of \$6 billion (Rs. 40,000 crores: 20 from the government and 20 from private players), NIIF might be able to raise debt worth \$60 billion (Rs. 4 lakh crores) on a long-term basis. If that is the case, it is clearly a big win for the Indian growth story. However, boosting investment in infrastructure is not the only goal of NIIF. NIIF is also expected to foster smart public private partnership models to accelerate the process of growth and development and bring synergies in operations. Relieving the Indian banking sector from the immense pressures that infrastructure financing brings is another major but less talked about goal. The stressed assets ratio for infrastructure lending is one of the highest reported among all sectors (18.7%). RBI reports indicate that if the total corpus of loans extended to Indian industries is Rs. 100 crores, Rs. 35 crores go to infrastructure, out of which, Rs. 6.5 crores become non-performing. With NPAs and GNPA's piling on the Indian banks' balance sheets for a long time now, shifting the responsibility of infrastructure finance to NIIF will have a positive impact on the banking sector.

3. Structure of NIIF

NIIF has been registered as a trust under the provisions of the Indian Trust Act, 1882 and as a Category II Alternate Investment Fund (AIF) under the SEBI (Alternative Investments Funds) Regulations, 2012. Category II AIFs include those AIFs which are not extended any specific government concessions or benefits (unlike Category I) but are eligible for pass-through

status; meaning that the income generated by them is taxed in in the hands of the final recipient, and not the trust itself.

In order to provide maximum flexibility and choice to investors, the total corpus of NIIF has been divided into three main sub-funds: the master fund, the strategic fund and the 'fund of funds'. The master fund is designed to focus on developing core infrastructure such as roads, ports, airports etc.; the strategic fund is aimed at growth and development stage investments of economic and commercial importance and the 'fund of funds', as the name suggests, seeks to invest in other funds which are primarily focused on investments related to infrastructure, green energy, social infrastructure, manufacturing and services. This "fund of funds" structure of NIIF, together with the provision for co-investing with the Gol makes NIIF an attractive opportunity for investors overseas.

The day to day management of the fund has been entrusted with Mr. Sujoy Bose, who has been appointed as the MD and CEO of NIIF. He is supported by a small investment team at arm's length with the government; this team would take important fund raising and investment related decisions.

NIIF Trustee Limited, a 100% government owned company has been assigned as the trustee of NIIF. To oversee the activities of the NIIF and NIIF Trustee Limited, government has also appointed a governing council comprising the representatives of government and experts from the field of finance and economics.

4. Money in and Money out

Ever since it was formulated in 2015, NIIF has been actively scanning the domestic and foreign markets to spot potential investors. As far as international investment is concerned, MoUs have been signed with sovereign wealth funds (Abu Dhabi Investment Authority, Temasek and Qatar Investment Authority) (sovereign wealth fund of Abu Dhabi), development institutions (Asian Infrastructure and Investment Bank, CDC Group PLC from UK and Russia's Rusnano), infrastructure developers (DP World- Dubai and ROADIS) and banks (HDFC and SBI). While UAE and QIA are mainly focused on long term infrastructure development, DP world wants to invest in developing the logistics sector. Accordingly, NIIF and DP World have together created Hindustan Infralog Private Limited to invest \$3 billion in developing ports and logistics. Similarly, Rusnano plans to establish a high technology private equity fund worth \$2 billion (Rs. 12000) in partnership with NIIF for joint implementation of technology and defense related projects. UK on the other hand is interested in taking a stake in India's growing renewables and energy market through the establishment of the Green Growth Equity Fund worth \$300 million (approximately), contributed equally by both India and UK. With HDFC Capital, NIIF has established the HDFC Capital Real Estate Fund 2 to invest in mid-income and affordable housing projects.

As far as the investments of NIIF are concerned, the key criterion for selection of projects is commercial viability, with an inclination towards projects which foster infrastructure and technological development in the country. NIIF has full autonomy in project selection. The portfolio of NIIF is expected to comprise a full range of greenfield and brownfield projects, along with asset reconstruction companies and stalled projects with gestation periods as long as twenty years. Generating a risk adjusted rate of return for its clients is of utmost importance.

Numerous possibilities for future growth and expansion are also under consideration. The government is exploring the idea of creating a fund under NIIF specifically to address the capital requirements of domestic steel companies. A proposal to form an airport development fund and a port development fund under NIIF, keeping in mind the preference of foreign investors for sector specific investments is also in the pipeline. Talks are also in progress with countries such as the United States of America, Hong Kong, Japan and sovereign wealth funds of Australia and Canada for future collaborations.

5. Critical Review and Final Words

NIIF is one of the most novel ideas India has come up with in the past decade. Financial Times (London) awarded it as the "Most Innovative Structure in Asia Pacific" under Finance and clearly, the possibilities are endless. While NIIF does indeed present a ray of hope for India's ailing infrastructure sector, especially at a time when the government is trying to "make in India", it poses certain challenges too. As discussed earlier, it is known with measured certainty, that NIIF will indeed take some burden of infrastructure financing off banks. But it is still unclear how it will deal with stressed assets of its own. No entity can survive for longer periods of time without generating constant returns or attracting consistent infusion of new capital. With every Rs. 6 out of Rs. 35 lent going unrecovered, what is the insurance for foreign and domestic institutional investors here?

The difference between government's expected and actual allocation for 2016-17 is also a point of contention. According to Budget papers, while the government had initially earmarked a sum of Rs. 4000 crores for investment in the NIIF, it drastically lowered the actual investment down to Rs. 1000 crores, without any explanation whatsoever. Does this reflect government's lack of confidence in the NIIF? If so, what is the message that we are sending to potential partners, and, more importantly, who is going to rescue India's ailing infrastructure sector after all?

We hope that this article will encourage the academic community to look closely not just at NIIF but also at other similar funds all over the world. A comparison of NIIF with similar quasi-sovereign entities of the world can give important insights into the potential and problems associated with these funds, thus enabling our policymakers make better decisions for the welfare of all stakeholders.

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