

ALTERNATIVES

by Richard Morrow, Joe Marsh | Oct 13, 2020

How Indonesia's new SWF aims to raise infra funds

The country's planned new sovereign wealth fund is intended to act as a conduit for infrastructure investment, via several investors as well as different investment paths.



Indonesia's incipient sovereign wealth fund should offer the country a means to attract more infrastructure investment, potentially via other institutional investors and multilateral institutions.

Tushar Mohatar, head of Malaysia equity research at Nomura, noted in a report on Monday (October 12) that after the Indonesian government passed an Omnibus Law, the country is set to launch the SWF in the coming few weeks.

Sources familiar with the plans for the SWF, which will be called Lembaga Pengelola Investasi (LPI), say that it is set to start with Idr75 trillion (\$5 billion) in initial capital. Of this, \$2 billion will consist of cash injected by the government, with another \$3 billion-worth of assets being

transferred from other state organisations. It will then seek foreign investments for an additional \$15 billion.

Indonesia's SWF initiative is led by an enormous push by the government to raise money from foreign investment partners for the country's huge infrastructure needs, said Jahangir Aka, London-based head of official institutions at Neuberger Berman.

"They have a time line for this development; they don't have a choice; this has to get done," he told *AsianInvestor*. "They have a domestic agenda – it's about moving a huge amount of capital into huge projects, such as a new capital city."

The Ministry of Finance, which is setting up the fund, did not respond to emailed questions from *AsianInvestor*.

There has already been foreign investor interest. In January, **Bloomberg reported that** the United Arab Emirates would invest \$22.8 billion in the country via Indonesia's new fund, particularly into the infrastructure and energy industries. That may well happen via Adia, its own SWF.

Nomura's research put that figure lower, at \$6.8 billion for refineries investments. It added that Japan's Softbank may commit up to \$40 billion to develop a new capital city for Indonesia, while the US's IDFC is interested in investing \$5.5 billion across several sectors.

Interest from other countries in Indonesia's sovereign wealth fund

Country	Investment, USD bn	Objective
Japan (Softbank)	40.0	New capital city development
United Arab Emirates	6.8	Refineries
United States (IDFC)	5.5	Pharmaceutical, defense, security, energy

Source: Nomura research

Other potential partners include the likes of Asian Infrastructure Investment Bank and Asian Development Bank. AIIB declined to comment on the potential to team up with the new SWF but noted that in September it made a \$150 million loan to Satelit Nusantara Tiga, a public-private partnership satellite designed to offer broadband internet to 45 million people.

INFRA INVESTING CONDUIT

The intent of the new Indonesian SWF is simple: to act as a conduit and catalyst for some of the infrastructure investment that the country sorely needs.

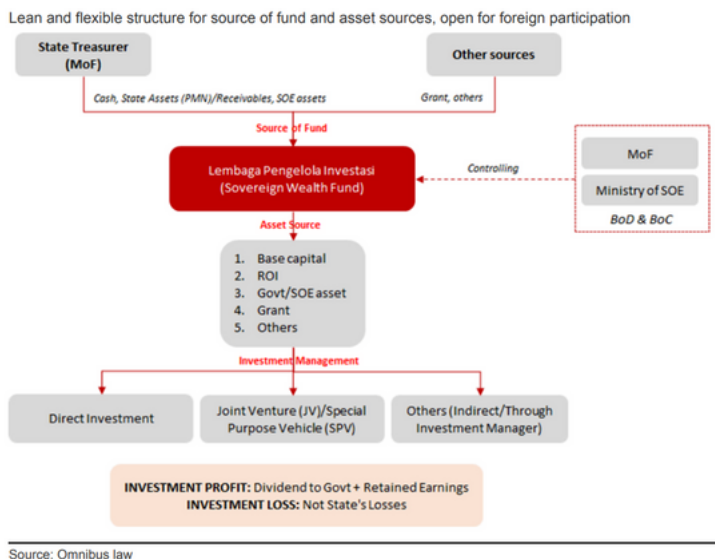
It looks set to do so via direct investments, joint-ventures and investing indirectly, potentially through external infrastructure managers.

"If all goes to plan, which we believe it should, the SWF may be a game-changer for future infra funding," Mohatar said in the report.

He added that the government wants the SWF to achieve three main goals. The first of these is "to accelerate new infra projects, with lean structures to encourage foreign participation (i.e. joint ventures/JVs, special purpose vehicles/SPVs, direct investment)".

Second, Jakarta likely wants the SWF to create a recycling process of state-owned enterprise (SOE) assets, which it can invest into toll roads being divested by other state companies. And lastly, the SWF could invest in areas that otherwise SOEs might need to do, helping ease some pressure on their balance sheets.

How Indonesia's sovereign wealth fund will be structured



Given these plans and the foreign investor flows, Gary Smith, managing director of think tank Sovereign Focus, said the SWF nomenclature might be slightly misleading.

"To me, this looks like a PE (private equity) fund, and the government acts as the general partner (and maybe also a limited partner)," he told *AsianInvestor*. "The aim is to speed-up infrastructure investment in a country with enormous infrastructure investment needs."

Diego Lopez, founder and managing director of boutique advisory firm Global SWF, added that the creation of state investment funds that act as conduits for foreign investment is "increasingly common among 'sovereign development funds' or 'strategic investment funds' that seek not only financial returns but also to catalyse investment into the country and contribute to the development of the domestic economy".

Developing nations often start governments fund to help develop strategic domestic assets, added Neuberger Berman's Aka. Mumtalakat, the SWF of Bahrain, took a similar route. These assets ultimately create big cashflows and as the fund grows, it reaches a natural saturation point when it reaches a certain size and would curtail the private sector if it got any bigger.

"Whether that is 10% or 50% of the national economy, the fund can then use experience they have gained from managing those domestic assets to invest overseas," Aka said.

The Indonesian fund looks to be taking an approach similar to Abu Dhabi's Mubadala, whereby it aims to set up partnerships with different corporates or institutions, he added. "If they want to invest in energy, for instance, they might team up with [oil and gas producers] Exxon or BP. It's not just about bringing in capital, but capital with expertise."

Smith agreed that enticing outside investors to fill the fund's coffers could prove positive, particularly if they have a firm voice in its operations.

"If the structure of the fund succeeds in this regard, and the investors use their clout to ensure that projects are justified on an economic basis (and not driven by local politics), then why not?"

Lopez sounded a note of caution, however, about the disparate nature of the three foreign investor partners looking to support Indonesia's SWF. "Vehicles like Adia, IDFC and Softbank are very different in nature and could create conflicts in managing the fund," he said.

STEPS TO SUCCESS

In addition to gaining foreign investors, Lopez suggested the Indonesian government and SWF executives ensure they have a few steps in place upon its establishment.

"Prior to pursuing any investment, the SWF should ensure that proper governance mechanisms are in place, with a SWF law that clearly defines the deposit and withdrawal rules, the institutional framework and the investment strategy including the asset classes and geographies the fund is allowed to invest in," he told *AsianInvestor*.

Lopez added that the new SWF should ensure it has its processes in place before seeking to put money to work.

"Our main advice is not to rush into the operating phase - and ensure that a number of workstreams are designed and implemented before any investment takes place," he said.

The workstreams include legitimacy and governance; mission and investment strategy; organisational structure; development mandate and fundraising policies.

Indonesia, whose 267.7 million population live on an archipelago of 17,000 islands, certainly does not lack for infrastructure needs.

Global Infrastructure Hub, a not-for-profit organisation that aligns with G20 priorities, estimates **the country will need to invest \$1.7 trillion** in infrastructure projects by 2040, of which it is looks set to fund \$1.6 trillion, based on current investment trends.

The country's government **reportedly wants to invest \$430 billion** in infrastructure by 2024, 20% more than the \$359.2 billion it invested between 2015 and 2019. Much of this investment is set to take place in the transportation space; nearly three-quarters of the projects currently being planned and constructed, according to Fitch Solutions.

"Indonesia is not lacking projects with attractive returns, but it is lacking funding options, especially in view of its strapped state fiscal position, stretched SOE balance sheets and long bureaucratic processes for private participation," noted Nomura's Mohatar.

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