Meet the CMD

‘There’s a mad rush to fund renewable energy projects’

The total spending on infrastructure projects has gone up 21 per cent for the six months ending September, says YM Deosthalee, L&T Finance Holdings

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While there are hardly any big-ticket projects in sectors such as ports and power, there is a lot of lending activity in renewable energy, transmission projects and road projects (to some extent), according to YM Deosthalee, Chairman and Managing Director of L&T Finance Holdings. He believes that government spending is key to revival in economic activity. Excerpts:

In the last 6-8 months, the Centre has been announcing various policy reforms in the infrastructure space. How are things at the ground level?

At the ground level, there is some visible pick-up, but it is not broad-based. Let us first look at some macro numbers. Oil demand for the month of October has grown 17 per cent over last year, which is the highest growth in the last 11 years. This is a reflection of growth in the transport and industrial sectors.

The other indicator is bitumen sales, which grew 54 per cent, indicating that there is some pick-up in road construction, where bitumen is mainly used. Power consumption, which was lagging behind, has also started to pick up pace in line with the improved production of coal. It was growing at sub-5 per cent earlier but has now started to grow at 10 per cent.

If we look at the order book for infrastructure players — road construction and transmission business — there is some revival there too. The construction order books of road developers are growing steadily with two-years-plus revenue visibility. This has happened on the back of increased tendering and awarding activity.

If one goes by the statistics of projects awarded in 2015, we see a lot of traction in roads, power distribution, water supply, pipelines and irrigation projects. Some of this is driven by the States while some are driven by the Centre. For instance, water supply and irrigation are largely driven by the States.

Lastly, if one were to look at the total spending on infrastructure projects, it has gone up 21 per cent for the six months ending September. Putting numbers to this growth, contracts worth ₹1.65 lakh crore have been awarded. And more importantly, tenders worth ₹2.68 lakh crore were floated, an increase of over 50 per cent.

So, if we look at the value of tenders, more projects are likely to be awarded in the next six months. Hence, if we look at all these figures, it indicates that things are indeed improving at the ground level.

So, has there been an increase in lending opportunities as well?

Despite some signs of revival, lending opportunities are still limited and have a long way to go before picking up. For instance, most of the projects that have been awarded have been on EPC (engineering, procurement, construction) basis and therefore, the scope for financing is limited as these will be executed by the NHAI, Indian Railways or State Governments.

Nevertheless we can see financing activity in three areas.

First is the renewable energy space. There is a mad rush to finance projects in this space. Every other lender wants to fund renewable energy projects. But this is a specialised sector that requires the requisite appraisal skills and understanding of risks. Fortunately for us, L&T Infra Finance has created competencies in this space three years ago and we continue to be a major player when compared with other NBFCs and banks.

Lenders are keen to expand in this segment as the Centre is giving top priority to this segment and also this is one area where there are significant opportunities to lend.

The second lending opportunity is in power transmission projects. This is because distribution and transmission lagged behind the tremendous growth in generation capacity over the last few years.

Lastly, there is some activity in road projects, but there is typically a lag between bidding and project implementation. Many of the road projects that have been awarded are yet to reach financial closure. Once that happens there can be increased activity in road projects.

But there are hardly any big-ticket projects in sectors such as ports, airports and power for now.

What is the scope for refinancing of projects? Are Infrastructure Debt Funds (IDFs), which were conceived to provide an additional funding route for infra projects, on track?

Most of the recent lending activity is on account of refinancing of existing projects. There are lenders who have funded infrastructure projects in the initial phase. Once these projects become operational, their risk profile changes and a lender can refinance the project at much better terms.

Entities that have promoted IDFs like ours have a lot of potential in refinancing infrastructure projects. Typically, IDFs are AAA rated and also tax-free entities. Hence, the cost of borrowing is low, allowing them to lend at more competitive rates when compared to other infrastructure sector lenders.

Earlier, NBFC-IDFs were only allowed to invest in infrastructure projects that were developed through public private partnership (PPP) with a project authority and a tripartite agreement. This largely limited the scope of IDF funding to sectors, such as roads and ports. The RBI has now allowed funding of projects in the PPP segment without a tripartite agreement. This enables IDFs to fund renewable energy projects in addition to the sectors covered earlier. This increases the potential to refinance projects, particularly for entities like ours, which has funded all types of infrastructure projects in the past through L&T Infra Finance. These projects, in addition to projects financed by other lenders, can be refinanced through the IDF.

YM Deosthalee joined L&T in 1974 and in 1995 was appointed Wholetime Director of L&T. He held the title of Chief Financial Officer till 2011. He assumed the office of CMD of L&T Finance Holdings in 2011

Only de-leveraging of private sector developers can kick-start big-bang projects. But many highly leveraged companies are selling their core assets, which will only hurt earnings. What is the way forward?

These companies were caught in a difficult situation because of project delays due to problems in land acquisition, environmental clearances and inability to raise equity. This, coupled with the slowdown in the economy, has affected cash flows of private sector developers.

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So, first, the overall activity in the economy needs to pick up to improve the cash flows of these companies. Second, while these companies need to de-leverage, they must be careful not to sell their core assets out of desperation, because this will only hurt their earnings in the long run.

Infrastructure projects have long gestation periods. Hence, restructuring these projects under the 5:25 route can help, to some extent. A combination of re-adjustment of repayment schedules of projects, pick-up in economic activity and selective asset sale can help in reviving these companies.

So, what can revive economic activity?

The most important driver for investment activity is government spending, which is already happening. The results of this will be visible in the second half of this year. Given the erratic monsoons and the limited spending capacity of the private sector, it is critical for the government to generate demand through productive spending.

That said, the private sector does have some capacity to bid for new projects as well, provided the risks are well apportioned.

Along with this there is scope for foreign direct investment in the infrastructure sector.

Since the government seems to be working towards improving the PPP framework and proactively seeking FDI in infrastructure development, we should see economic activity reviving in the next one year.