

Plenary Session III

Private-Public Partnership for Infrastructure Development

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Private-Public Partnerships for Infrastructure Development

1. Good afternoon. I am delighted to be part of this session on infrastructure development, a topic that is of vital importance to this region as it looks to extend and maintain its impressive record of economic growth.

Slide 1 – Growing demand for investment in infrastructure

2. It is clear that significant investment in infrastructure will be required in this region in the years ahead. The recent study, *Connecting East Asia, A new Framework for Infrastructure*, by the Asia Development Bank and its partners suggests up to \$200 billion a year will be needed in the developing countries of East Asia alone. As governments face ever growing demands on their budgets it is likely that they will increasingly look to the private sector to provide some of this infrastructure investment.
3. There will, however, also be considerable global competition for this private capital and investors will favour those countries with stable and predictable regulatory and commercial frameworks that provide a supportive investment climate. Of course, many countries in this region have a good record in providing that kind of climate and, in the Asia Development Bank report, 67 per cent of global companies said that they expected to increase investment in East Asia over next two years.

Slide 2 – Shell Gas & Power

4. My comments today will focus on the particular challenges and partnerships needed to develop energy infrastructure as clearly that is the area I know best. However, I also believe that we can draw some wider lessons from energy projects for infrastructure developments in general. In particular, Shell, like other energy companies, has long experience of working in partnership with governments and the public sector. For example, our exploration and production business in Brunei is a 50:50 partnership with the Brunei government and in

Malaysia we have been part of the liquefied natural gas industry for more than twenty years as part of a joint venture led by Petronas.

5. Let me start by telling you a little about Shell's Gas and Power business. We are the world's second largest IOC natural gas producer and have interests in pipelines, liquefied natural gas or LNG, shipping, gas fired power generation, coal gasification, gas to liquids conversion and product application, and marketing and trading. We have a presence in each of the three key gas markets: Asia Pacific, Europe, and North America. The countries of this region in particular have played a key role in our gas business for over thirty years and, I am confident, will continue to be at the heart of our business - both as customers and suppliers.

Slide 3 – Growing Energy demand

6. We have the advantage of operating in a market where demand for our product is rising rapidly. The International Energy Agency predicts a 60 per cent increase in global energy demand in the period to 2030 and the fastest pace of growth in this region. Developing Asia is likely to account for 42 per cent of world growth in energy demand but there will also be ongoing increases in demand in established economies such as here in South Korea. Within that overall growth in demand, global natural gas usage is forecast to rise by up to three per cent per annum while LNG demand is likely to grow at a rate of around ten per cent per year.

Slide 4 - Growing Global LNG Demand

7. I will focus on LNG for a few minutes because it is such an important part of the energy mix in this region and because it presents its own particular infrastructure challenges. LNG is gas which has been cooled to minus 162 degrees and can then be transported efficiently and safely in liquid form by ship. Japan and Korea are currently the world largest importers of LNG.
8. LNG offers significant advantages as a source of energy – not least flexibility, diversity of supply and environmental benefits. And those advantages are increasingly being recognised in markets around the world.

Slide 5 - Developing new infrastructure

9. As a result, we are now seeing a massive expansion in the number of LNG projects being developed around the globe, reflecting investor confidence that demand will continue to grow fast. Research by the bank ABN Amro shows that \$30 billion has been invested in LNG projects over the past nine years, but that a staggering \$75 billion of investment is planned for the next two years alone.

10. Over the past five years Shell joint ventures have constructed eight new liquefaction facilities representing twenty per cent of the world's LNG expansion capacity – an investment of \$9 billion We also have interests in seven new LNG trains currently under construction and have commenced supplying LNG into our recently completed regasification terminal in Hazira, India as well as agreeing contracts to supply LNG into China, commencing in 2006.

11. While these new markets are important we also see our presence continuing to grow in traditional markets such as here in Korea where our LNG ventures already supply almost half of total demand and which have recently secured major contracts to supply Kogas up to four million tonnes per annum over 20 years, beginning in 2008. These will be supplied from our Sakhalin and Malaysia joint ventures – both of which are major infrastructure developments.

12. Of course, investment in the infrastructure in energy production is only one part of the chain we also need the investment in the infrastructure in receiving countries to distribute gas and to generate and supply the power to the end consumer. There has been significant development in this sector in Korea where electricity generating capacity has increased by 90 per cent over the past ten years. There are ongoing projects to develop that further such as the Shell joint venture with Daelim to investigate power plant opportunities next to a LNG receiving terminal. This is known as the Songdo project and, if approved, could provide a new three thousand megawatt combined cycle power plant by 2010.

Slide 6 - Sakhalin

13. One of Shell's biggest energy infrastructure developments is the Sakhalin II project, which will supply LNG to Korea, Japan, and North America and be one of the world's most

strategic gas supply sources. It is one of the most challenging energy projects ever undertaken both in technical and commercial terms which could not have happened without strong Russian Government support. Equally important has been the need to ensure that its development brings benefits to the local community on Sakhalin Island which underlines the fact that no major infrastructure project can be seen in isolation from the wider context in which it is being built. That means in addition to any formal public private partnership, there needs to be a link between the private sector developer and the wider public bodies representing the needs of the local community.

14. In Sakhalin that means a clear focus on bringing economic opportunities to a very remote part of Russia. As a result about \$6 billion will be spent on Russian labour and related taxes over the life of the project. At the same time, more than \$700 million is being spent on improved infrastructure on the island ranging from bridges and roads to new telecommunications systems, ports and railways.
15. Finally, Sakhalin is a sustainable development project in every sense of the term. Testament to this, is our decision earlier this year to reroute the offshore pipelines to avoid the Western Grey Whale feeding area to minimise any adverse effect on these critically endangered animals.

Slide 7- The Complexity of the Value chain

16. Let me turn now to the funding of energy infrastructure projects. The hallmark of these projects is that they are expensive and although progress has been made in reducing unit costs, the scale of projects is increasing making them very capital intensive. Energy projects, especially LNG developments, are also very complex. As you can see here they are part of a long value chain and their success is dependent on the strength of every link in that chain - whether in project management or technology; gas field development, shipping or marketing. That means that developers of LNG projects need to have particularly strong strategic and commercial skills and ability to manage risks along the whole chain. And public-private partnerships can be an effective way of managing these demands by combining the different experience and strengths of each sector.

17. In infrastructure projects of this scale, always amounting to billions of US dollars, investors will also be looking for some assurance about returns over the long term and it is important that partners, especially public sector partners, understand the need for private companies to provide a return to their shareholders.
18. That means that ensuring the various contracting arrangements, particularly those relating to sales commitments, are structured to provide a clear and long term return. The traditional pattern in LNG has been for negotiated long term, twenty year, contracts. In a more complex global market, as we see it developing, there is likely to be more flexibility in the supply chain, indeed Korea has long sought arrangements to help manage its seasonal energy demand fluctuations. In essence, however, if we are to provide infrastructure development and investment on the scale needed the basis of the long-term traditional negotiated contracts are likely to remain at the heart of most projects.

Slide 8 – Working With Government Partners

19. As I mentioned at the beginning of the speech, energy projects are often developed in public private partnerships not least because governments, especially in developing economies wish to keep a strong control over their energy resources and supplies. While this brings challenges, many successful partnerships have been established in this region and continue to be developed as more countries look to improve their energy infrastructure to meet growing demand.
20. Many of these partnerships are in China, where the demand for new investment in infrastructure is very high and where demand for energy is growing fastest. One example of this kind of partnership approach is in the North West Shelf LNG project in Australia which will supply LNG to the Guangdong terminal in southern China. Under the terms of the supply deal the state owned China National Offshore Oil Company gained an equity stake in the Australian supply project, underlining the range of innovative partnerships that are increasingly being seen in these large energy infrastructure developments. Other recent infrastructure partnerships between Shell and Chinese Government-owned companies involving multi-billion dollar investments have been concluded in coal gasification,

petrochemical production, gas pipelines and distribution, oil and gas production and oil products marketing.

21. I think we are likely to see more of these complex partnerships in the energy sector not least, as on the one hand, governments are seeking access to advanced technology and commercial expertise, and on the other hand, national oil companies, especially in this region, are seeking to acquire interests in upstream projects and infrastructure outside their own countries.

Conclusion

22. So what broader conclusions can we draw about the key elements for successful infrastructure developments ? They are that infrastructure projects are expensive, they are complex and therefore investors will need some way of managing their risks, some assurance of a return and so a need for supportive overall political and economic frameworks.
23. Governments will take a particular interest in energy and other major infrastructure projects and will often want to a stake in them whether directly or through national companies. These public private partnerships can be very effective but there does need to be an understanding that private companies will be looking for contractual arrangements that provide an assurance to their shareholders of a return on their investment.
24. That means that relationships based on trust are key. Our experience in Asia Pacific has been that these long standing relationships between the public and private sector can be developed and can work to the benefit of both parties.
25. There is an enormous challenge ahead but the remarkable economic growth of this region in the past few decades shows how well it rises to challenges. And that means I am confident that we can succeed in building the infrastructure that will help both its developing countries reach their potential and ensure its advanced economies remain highly competitive players on the world stage.

26. Thank You.

