Study on Investment and Finance Mechanism of New Urbanization

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Abstract. By analysis of opportunities brought to Xuzhou, a north city in Jiangsu Province by new urbanization, we make comparative research on the urbanization experience in some developed countries. According to this, some suggestions are put forward to the innovation of investment and financing mechanism of urbanization in Xuzhou.

Introduction

In March 2014, with the release of the strategic “National Plan on New Urbanization”, the problem of capital allocation of the urbanization has begun to get a lot of concern. The plan will see people-oriented urbanization as its essential value, and it is not only to raise the proportion of urban population, but to realize the urbanization of people’s whole life including mode of production, way of life, living space and development space. New urbanization construction is a long-term systematic project, it can neither be achieved nor be sustainable by only relying on land finance to meet the funds needed in the field of both construction and maintenance. So, it is urgent to establish a diversified investment and financing system of urbanization.

The Opportunities Brought About by the New Urbanization to Xuzhou

With the Release of Jiangsu Plan on New Urbanization, Xuzhou, as a “Central City” will be Stressed

In May 2014, Jiangsu New Urbanization and Urban-Rural Integration Planning was released, which put forward clearly that Jiangsu will continue to promote the development of new urbanization and urban-rural integration, to cultivate the region of coastal towns, towns along east Longhai areas, and the Grand Canal, and continue to build Nanjing, SuXiChang (Suzhou, Wuxi, Changzhou), and Xuzhou as three metropolitan areas. Xuzhou, as one of the three metropolitan areas as well as the city along the east Longhai and the canal, becomes one of the few “cross cities” of Jiangsu province, which further highlights its status as the regional central city. The New Urbanization and Urban-Rural Integration Planning and the subsequent policies will serve as a booster for Xuzhou and the counties (cities) around it to speed up their new urbanization and promote their industrialization.

During the process of new urbanization, Jiangsu stressed that among its big and medium sized cities, small towns and urban agglomeration there should be scientific arrangement, reasonable division of labor and intensive development. Thus central cities focus on enhancing their comprehensive function. while small and medium-sized cities promote their industry carrying capacity and give play to the role of radiating and exemplary; small towns meet the basic needs of production and living of the residents around, and resolve the problems like supplying service to agriculture, rural areas and farmers, developing commerce and trade circulation, and improving basic public service ability, and the like. As there are regional differences within the province, the goals of development of South Jiangsu, Middle and North Jiangsu are not the same. In accordance with the
construction of metropolitan area, North Jiangsu should speed up its new industrialization and urbanization process, implement the strategy for the development of coastal areas, promote cluster development of the coastal towns as well as the towns along East Longhai, and promote Xuzhou’s comprehensive function as a central city of metropolitan areas.

High Quality of the Existing Urbanization Provides Much Development Space for the New Urbanization

According to “China’s Urbanization Quality Report” issued by Institute of Urban Environment of Chinese Academy of Social Sciences in March 2013, Xuzhou’s urbanization quality level ranked 75th of more than 286 cities. It is not only a recognition of Xuzhou’ achievements in urbanization construction, but also a sign of a healthy development momentum of the urbanization construction in Xuzhou. Over the years, Xuzhou has attached great importance to its urbanization construction, organized the implementation of a large number of infrastructure and functional projects, vigorously improved the public service, and created a way of urbanization with its own characteristics. In early 2010, according to different factors such as natural conditions, location characteristics, industry foundation, and resources endowment, 114 villages and towns and two sub-district offices of Xuzhou were divided into different types as for their development modes. A number of distinctive towns and districts have been preliminarily formed: Kiln Bay town, an antique ancient town which has been existing from Ming and Qing dynasties; Hanwang town, an ecological livable town which is also famous for its historical culture; Liguo town, a big town of steel and iron introduction which is situated on the shore of Weishan Lake; Datun town and Guanhu town which are of strategic importance for the massive economic development; Huankou town and Liji town are important towns for border commerce and trade.

New Urbanization will Provide Long-Lasting Impetus to Xuzhou Economic Development and will Serve as an Important Platform and Carrier for the Transformation and Upgrading of Industrial Structure.

New urbanization requires coordinated development of new industrialization, informationization, and agricultural modernization. It emphasizes the optimization of integrated layout as well as the harmonious development of big and medium sized cities and small towns. According to some economists, China's urbanization rate will grow by 1% each year, and will drive the market demand by 7 trillion yuan. If calculated by 1.05% increase per capita, there will be 7.35 trillion yuan market demand a year. New urbanization will bring a variety of investment opportunities to the development of Xuzhou in the future.

First, the transfer of agricultural population to urban residents will bring huge domestic demand. Second, further development taken by the agricultural labor force migration to the third industry and services will improve the capability and speed of structure transformation. Third, new urbanization contains huge investment demand including the instruction of urban infrastructure, public service facilities, and housing construction. Forth, through prompting institutional reform and eliminating policy barriers huge dividend from system can be realized.

Investment and Financing Mode of Urbanization: the Experience from Developed Countries

In western developed countries, financial tools and products supporting the development of urbanization is rich and varied. Overall, financial institutions play very important role in municipal construction financing either in the financial system led by capital market which is represented by Britain and the United States, or in the financial system led by banks which is represented by Japan and Germany. Among the financing modes, credit and loan, under the basic principles of commercial finance, relies more on medium and long-term financial support from policies. At the same time, market-oriented financing means is very enriched and developed including municipal
bonds, infrastructure investment funds, asset securitization, etc. With the development of capital markets, direct financing will play more and more important role in it.

In America, based on the developed capital market, there are diversified investors and varied financing means for urban infrastructure construction. In the field of pure public goods, the general corporate bonds, stocks and loans from bank can not meet the need of capital of public service sectors and the public projects effectively, then the government would play a leading role by means like municipal bonds and government procurement. Municipal bonds in America are classified into general obligation bonds and revenue bonds. Revenue bonds will be used in the field of health care, higher education, transportation (highways, toll roads, ports and airports) as well as public utilities (water supply, sewage treatment, electricity, and gas); for some construction projects whose later income will not be enough to repay the debt, such as the construction of exhibition centers and street lamp systems, local governments will issue general obligation bonds, and pay back the debt with specific sales tax, fuel tax, or a combination of the two. Asset securitization and infrastructure investment funds are also used for urban construction financing.

In Japan, financing for urban construction mainly relies on long-term credit and local public bonds in policy-based financial institutions and markets. In 1951, the Japanese government established the "Development Bank" to provide long-term low-interest loans to domestic energy, transportation and other infrastructure sectors. Most of the bank's money came from the government’s fiscal investment and financing plan, meanwhile they get money by issuing bonds in international bond market which are guaranteed by the central government of Japan. Policy finance has not only promoted the rapid growth of the infrastructure sector, but also had a very good guiding effect on private capital. A large number of private financial institutions began to provide loans to the departments to which policy Banks had invested, so that demand for capital of large-scaled infrastructure construction could be met effectively. Local bonds in Japan includes local public bond and Local public-enterprise bond, and local public bond is the main body of local bonds. local public bonds are issued by the local government directly, and is mainly used in road construction, regional development, facilities for compulsory education, public housing construction, purchase of public land, and other public utilities. Local public enterprise bonds which are issued by some special local public enterprises and guaranteed by local government, are mainly used for the construction of sewer, tap water and transport, etc. Compared with the system of municipal bonds of United States and other western countries, local bonds in Japan is not a real market-based financing system, it has a strong financial nature of private coordination.

In South Korea, the government makes good use of private capital for infrastructure construction by setting up national investment fund and formulating policies and regulations. Congress passed the law of promoting private capital to infrastructure construction, then introduced the countermeasures to expand infrastructure, and banks got interest subsidy from government. It is South Korea's central bank who is responsible for foreign borrowings from other countries, and then lends them to domestic corporations through development banks and commercial banks. According to relevant policies, these banks will lend the money from both abroad and home to infrastructure companies with low interest rates (7% ~ 8%).

Innovation of Investment and Financing Mechanism of New Urbanization Construction

Introducing Mode of PPP to Innovate Infrastructure Financing Mode

Infrastructure construction is a critical part of new urbanization. Infrastructure construction has the characteristics of concentrated investment time and long-lasting benefit time. As government’s limit annual financial revenues can't meet the needs of huge sum of investment, other channels need to be found. For the construction projects whose investors and beneficiaries are different, principles of “He who makes investment gets benefit” should be followed. Investment of future generations can be used by the way of government borrowing. People of contemporary and future generations have the
responsibility and obligation to repay the debt according to the above principles so as to share reasonably the construction cost. PPP mode has its unique advantages in this respects.

PPP, the abbreviation for “public-private partnerships”, refers to the mode by which public sectors provide public products or services through cooperating with private sectors. According to the National Council on Public Private Partnership of America: PPP is a contractual arrangement between a public agency and a private sector entity. Through this agreement, the technology and assets of both sectors (public and private) are shared in the delivery of service or facility to the public. In addition to the sharing of resources, each party should also share the potential risks and rewards. The nature of PPP is that public sectors no longer buy assets anymore. Instead, they buy service under certain conditions of cooperation, and service facilities will be supplied by the private sectors. Through this mode, governments and private sectors can learn each others’ strengths and set up a relationship of mutual cooperation to realize their common goals and interests, share resources and risks, distribute income and take social responsibilities. Under the traditional financing mode, national and local government is the main body of public projects, and tax revenue is the main source of construction fund. Government hopes to achieve the development of infrastructure construction and to bring economic benefits to the whole society through investment, but is under the stress of fiscal expenditure pressures; while private sectors hope to get their returns on investment and social effects through investment. Based on this background and the demand for a win-win situation, public-private partnership comes into being. PPP is widely used in western countries in the process of infrastructure management and is thought to be an effective mode that will be able to bring varieties of public service to the government.

From the point of operation process, PPP includes establishing project, setting up a project company, bidding and project financing, project construction, project management, project transfer, etc. Government and private sectors set up a project company together—a Special Purpose Company (SPC). Taking the project as main body, funds are collected according to the expected earnings of the project as well as assets and government support measures (such as tax incentives, loan guarantees, and the priority right to use the land alongside, etc.). The most important source of project capital is from the contribution of SPC and loans got from commercial banks by SPC. Government departments give charter rights to SPC with which SPC can make project development on behalf of the government. When the project is completed, SPC has the rights of management within a certain period of time during which SPC can recycle funds and earn profit through direct returns of the project and benefits from government support. Rights of management will be handed over to the government when it expires. PPP project operation mode is shown as followed:

![Figure 1. PPP Project Operation Mode.](image)

PPP has great development potential in China, and is an important form of financing channel of new urbanization construction. In March 2014, in a PPP training program held by the Ministry of Finance, deputy finance minister Wang Baoan pointed that, PPP is the internal requirement to establish a modern financial system, the important measures to improve the government’s public service and support to new urbanization construction. In 2013, PPP projects in China had a total investment of $127.8 billion, and there is still a large gap compared with the emerging markets of the
same type. Newly added investment of PPP in 2013 was only $700 million, while the total amount of Quasi-municipal bond of the same year was as high as 951.2 billion yuan. If PPP successfully replaces Quasi-municipal bond as the leading financing mode, it will have a tremendous development space, which is also a financing mode that the Ministry of Finance is pushing hard. Distribution of size and fields of newly added PPP Investment in recent years is shown in Fig 2. and Fig 3.

Figure 2. Distribution of Size and Fields of Newly Added PPP Investment (dollars in millions).

![Figure 3](image)

Figure 3. Chinese PPP Scale Compared with Some Major Emerging Countries.

One of the core functions of PPP is to change public goods supply mechanism. Through PPP mode, government can be extricated from part of its debt, which can reduce some pressure, and should change step by step from a single annual “management of budget revenue and expenditure” to the financial planning of long and medium term as well as “asset and liability management”. The key of PPP is to introduce private sectors to bear most of the work for public goods and services like project financing, construction, operation, etc. Compared with the mode of public goods and services provided by government directly, PPP will help local debt governance. It is the private sectors who undertake most of the project financing, in exchange of franchise for public goods and services for a long time, and the government will move part of the debt to private sectors, thus PPP mode can relieve the incremental debt of government. The private sectors are more efficient than the financing platform companies in project operation and maintenance. Although government departments have to take part in financing work for new projects which increases leverage, the increased net benefits gained due to the efficiency of project operation help digest the stock of government debt. PPP dispersed part of the
risks. At the beginning of the project, PPP have realized risks distribution, that is the government will bear some risks which will reduce the risk of private capital, reduce the difficulties, and help achieve project financing. If the project losses, government and the private sectors will share the losses. PPP is suitable for wide range of applications, especially for large, one-off projects, such as water supply, construction of roads, hospitals and schools. Beijing subway line 4 and the national stadium are models of successful application of the PPP mode.

**To Develop Diversified Financing Channels, and Introduce Private Capital**

Introduction of private capital and innovation of financing methods can be realized by municipal bonds, project financing, trust plan, equity financing and through the government financing platform.

(1) Issuance of municipal bonds. Municipal bond is issued by local government investment and financing agencies, used in the construction of local infrastructure and social public welfare projects. Its advantage is to make the best use of scattered money in society.

(2) Project financing. Project financing is a new type of financing mode nowadays. The private sectors (private economy) engage in public infrastructure projects providing public services to the society, and recover the private sectors’ investment cost and reasonable profits with the project future earnings or disposal value of assets, so as to achieve the goal of government to finance public infrastructure projects. Project financing mainly includes BOT, TOT, ABS, BT, PPP as mentioned above.

**To Establish a Multi-Leveled, Broad Covered and Sustainable Rural Financial System**

Rural credit involves the financial demand of multi-field, multi-level and multi-type: both the general farmers’ microfinance demand and the large-scale capital requirement of the leading enterprises in a certain industry are needed. Therefore, it is necessary to segment the agricultural credit market, develop various forms of financial organization, foster diversified subjects of rural finance, and to establish a multi-leveled, broad covered and sustainable rural financial system. First, the existing rural financial market is to be further improved and standardized. Second, to build community oriented financial service system, and increase production and consumption credit of urban residents. Third, to establish a multi-leveled agricultural insurance system and provide suitable insurance products to the suburban land-lost farmers. Fourth, to increase the ratio of financial supporting from postal savings, and strengthen the feedback.

**References**


