Pension Funds Investing in Infrastructure

Elliot Bradbrook takes a look at pension funds and the increasingly important role they play as investors in the infrastructure asset class.

A conservatively managed infrastructure investment portfolio is commonly understood to provide investors with long-term predictable returns and increased portfolio diversification. It also acts as a hedge against inflation. As a result, infrastructure investment attracts institutional investors with long-term liabilities to meet, such as the various different types of pension scheme. Pension funds, therefore, are a staple of any successful infrastructure fund manager's client base, and represent a significant proportion of the total number of institutional investors actively making investments in the asset class.

The Pension Fund Universe

As shown in Fig. 1, public pension funds, private sector pension funds, and superannuation schemes make up a significant 40% of the active global infrastructure investor universe. Over 1,500 active investors are featured on the Preqin Infrastructure Online database, with public pension funds the most prevalent (18% of the total). Private sector pension funds follow closely, accounting for a further 17%. Superannuation schemes represent 5% of all active investors, most of which are based in Australia and are typically experienced players in the market.

In terms of location, Europe is one of the main hubs of infrastructure investment activity. As shown in Fig. 2, 39% of all active pension plans in the infrastructure space are based in Europe, with 18% located in the UK alone. Despite the high proportion of active pension plans based in the UK, the majority of these institutions only invest a small proportion of their total assets in infrastructure opportunities. Many UK-based pension funds have smaller levels of assets under management and therefore have limited resources to invest in illiquid long-term infrastructure assets. Other prominent European countries include Switzerland (5%), the Netherlands (5%), Denmark (2%), and Sweden (2%).

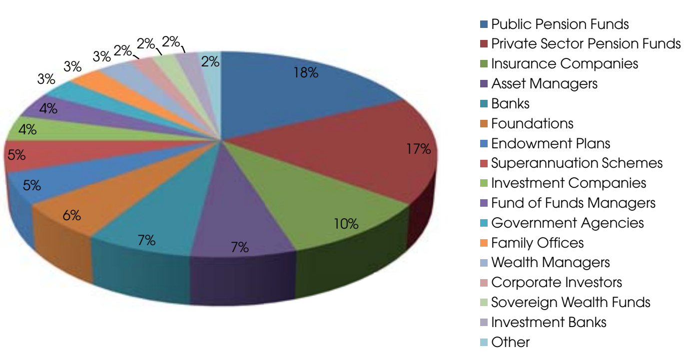
North America is also a significant base for pension plans making investments in infrastructure. Canada represents 9% of the total universe and is home to some of the largest and most experienced infrastructure investors in the world. Many of these institutions have their own infrastructure investment teams and are making significant contributions to global infrastructure development via direct investments. The US is home to 27% of the total universe, the highest proportion for any single country or region around the world. Increasingly, US investors are becoming more open to private sector investment in the infrastructure asset class, and a growing number of public/private pension funds are beginning to carve out allocations to infrastructure opportunities.

A quarter of all pension plans active in the infrastructure space are based outside Europe and North America. Australian institutions, most of which are structured as superannuation schemes, were among the pioneers of private sector investment in infrastructure assets in the 1990s and now account for a significant 13% of the universe.

Investment Characteristics

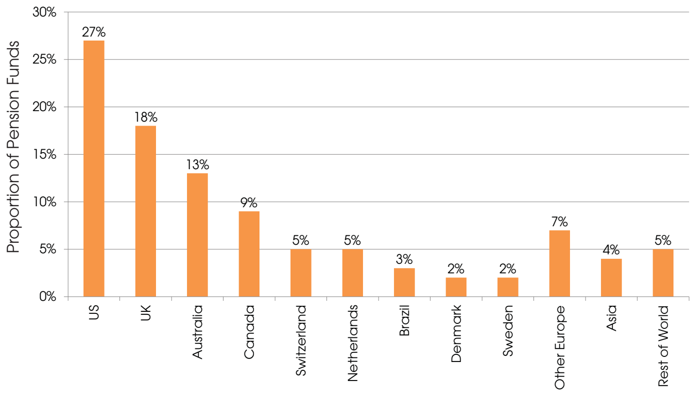
The various types of pension plans investing in infrastructure have aggregate assets under management totalling $8.4tn. Across the whole sample, these investors maintain an average current

Fig. 1: Breakdown of Infrastructure Investor Universe by Type



Source: Preqin Infrastructure Online

Fig. 2: Breakdown of Pension Funds Investing in Infrastructure by Location



Source: Preqin Infrastructure Online

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allocation to infrastructure amounting to 3.3% of total assets, and an average target allocation of 5%. These statistics differ depending on the country and region – for example, Canadian pension plans have an average current infrastructure allocation of 4.6% and an average target allocation of 7.5%, whereas UK-based institutions maintain an average current allocation of 3.6% and an average target of 5%.

Fig. 3 shows the average current and target allocations of the different types of pension plans active in the infrastructure space. Superannuation schemes typically allocate higher levels of capital to infrastructure assets – these institutions currently allocate 6% of total assets to infrastructure on average, with an average target allocation of 8%. Private sector pension plans follow, with an average current allocation of 2.8% and an average target of 5%. Public pension plans also have an average current allocation of 2.8%, but a lower average target allocation of 4.3%.

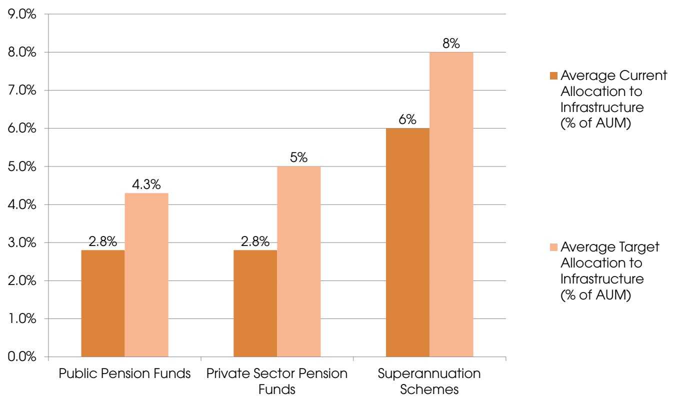
These institutions source capital for infrastructure investment from a number of different areas. Less experienced pension plans tend to invest via a general alternatives, private equity, opportunistic and/or real assets allocation, while the more experienced create separate infrastructure-specific allocations. Forty-four percent of active pension plan investors in infrastructure maintain a separate infrastructure allocation, while 19% invest via a private equity allocation, 15% via a general alternatives allocation, 13% via a real assets allocation, and a further 3% through an opportunistic investment portfolio.

The vast majority of pension plans invest in infrastructure by making commitments to third-party unlisted infrastructure funds. As shown in Fig. 4, 96% of pension plans actively investing in infrastructure look to make commitments to unlisted vehicles, while 19% make direct investments and just 9% target listed infrastructure funds. Although interest in direct investment is growing, unlisted vehicles will remain the primary route to market for pension funds in the future, meaning fund managers must continue to pay close attention to their needs and demands in order to be successful.

In terms of regional focus, Europe is again the dominant region for pension funds investing in infrastructure. A significant 53% of the various types of pension plans active in the infrastructure market favour investment in Europe, while 47% will invest in North America and 33% will invest in Asia and Rest of World. Aside from a focus on any specific region, many pension plans pursue a multi-continental investment policy in order to increase the diversification of assets held within their portfolio. Forty-three percent maintain a global investment mandate and consider investment in a range of different regions around the world.

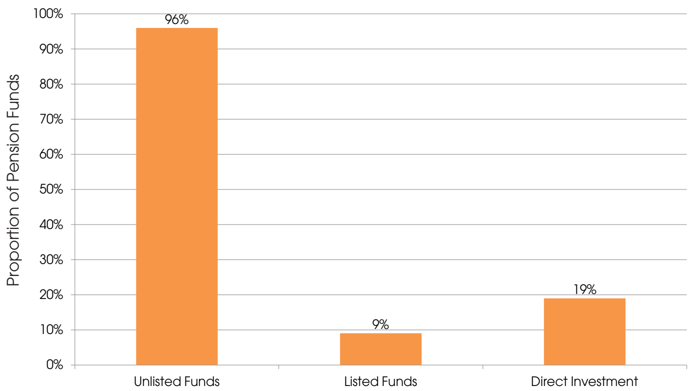
The relative youth of the infrastructure asset class and a lack of available resources mean many pension plans utilize the services of an infrastructure investment consultant when making investment decisions. Of the 619 pension plans included in the sample, 55% are known to make investments based on the recommendations of a consultant, and 11% use the services of an internal in-house advisory team. Experienced and popular infrastructure consulting firms include Hewitt EnnisKnupp, Hymans Robertson, JANA Investment Advisors, Mercer Investment Consulting and Towers Watson.

Fig. 3: Current / Target Allocations to Infrastructure for Pension Funds



Source: Preqin Infrastructure Online

Fig. 4: Proportion of Pension Funds Investing in Infrastructure Directly, via Unlisted Funds and via Listed Funds



Source: Preqin Infrastructure Online

Largest Pension Fund Investors

The table in Fig. 5 shows the 10 largest pension plan investors in the infrastructure asset class by capital currently committed. The list features a mix of public pension funds, private sector pension funds, and superannuation schemes. The largest such investor is Canadian public pension plan OMERS, which has $14.3bn invested in infrastructure opportunities through direct investments made by its subsidiaries Borealis Infrastructure, OMERS Strategic Investments, and the newly launched Global Strategic Investment Alliance. Other significant pension plans active in the market include New York-based private sector pension plan TIAA-CREF and Melbourne-based AustralianSuper.

Fig. 5: Top 10 Pension Funds Investing in Infrastructure by Current Commitment Size

Investor	Currently Committed to Infrastructure ($bn)	Investor Type	Investor Location
OMERS	14.3	Public Pension Fund	Canada
CPP Investment Board	9.2	Public Pension Fund	Canada
Ontario Teachers' Pension Plan	7.8	Public Pension Fund	Canada
TIAA-CREF	6.5	Private Sector Pension Fund	US
ABP	6.0	Public Pension Fund	Netherlands
AustralianSuper	5.1	Superannuation Scheme	Australia
ATP Lifelong Pension	2.6	Public Pension Fund	Denmark
Public Sector Pension Investment Board	2.3	Public Pension Fund	Canada
Construction and Building Industries Superannuation Fund	2.2	Superannuation Scheme	Australia
California Public Employees' Retirement System (CalPERS)	1.7	Public Pension Fund	US

Source: Preqin Infrastructure Online

Outlook

Pension plans are the most significant investors in the infrastructure asset class and will remain a vitally important source of capital for infrastructure fund managers going forward. Demand for infrastructure development on a global basis is growing and the private sector will inevitably be required to provide the majority of investment capital needed to meet this demand in future. With pension funds representing a significant 40% of all active investors in the market, and with more schemes making their maiden allocations, these institutions look set to shape the future of the asset class as public resources for infrastructure development continue to dwindle.