



Key Markets: Infrastructure Investment in Asia

Ee Fai Kam provides a top-down examination of the Asian infrastructure universe, drawing attention to critical themes and issues within the region's different infrastructure markets.

The Asian Infrastructure Investment Environment

Asia has been an important engine of growth in the global economy over the last decade. The World Bank reports that between 2003 and 2012, Asia's two most populous countries, China and India, averaged GDP growth of 10.8% and 8.2% respectively, compared to 1.6% posted by the US and 1.4% recorded by the EU. According to IMF estimates, Asia is expected to record strong real GDP increases of 5.7% in 2013 and 6% in 2014. As GDP and infrastructure spending typically rise in tandem, the amount of capital flowing into infrastructure projects in Asia is expected to grow in line with the growth in the economy. This is especially so considering that approximately 85% of Asian countries are developing economies that are in great need of new infrastructure development such as power plants, water treatment facilities, road networks and port connections.

Asian Development Bank (ADB) predicts that Asia's infrastructure needs between 2010 and 2020 will reach \$8tn. According to ADB, a significant \$1tn of this is expected to be invested in India, particularly in the utilities sector. In July 2012, India experienced its largest power outage in history; approximately 700mn people across the northeastern region were affected. As a result, the Indian government's plan to overhaul the national power grid for \$400bn has gained additional traction.

Elsewhere in Asia, infrastructure spending in ASEAN is also garnering increasing attention. This grouping of nations in the southeastern corner of Asia consists predominantly of emerging economies such as Indonesia, Thailand, Myanmar and Vietnam. In addition to the typical infrastructure needs of individual countries, ASEAN nations are putting in place mutually beneficial support infrastructure due to a common desire for regional connectivity. Consequently, they have instituted initiatives such as ASEAN Highway Network, Singapore-Kunming Rail Link and Trans-ASEAN Gas Pipeline. In total, ADB estimates ASEAN infrastructure needs

over the next seven years will reach an estimated \$600bn. One channel of public capital that is already in place to satisfy some of these needs is ASEAN Infrastructure Fund, a loan facility set up by ASEAN nations and ADB. The platform is expected to begin lending operations in H2 2013 for a \$1bn pipeline of energy, road and transportation deals. As a result, there is huge scope for private infrastructure investment in both greenfield and brownfield assets across Asia.

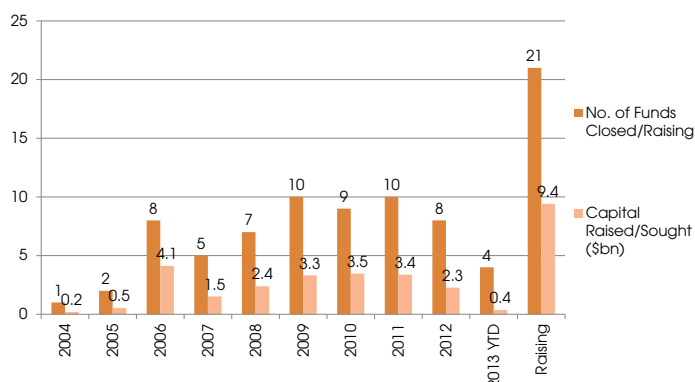
Fund Managers Active in Asia

According to Preqin data, there are currently 88 unlisted infrastructure fund managers that invest in Asia, 21 of which have a fund on the road and are looking to raise a collective \$9.4bn. Fig. 1 shows that since 2004, 64 Asia-focused private infrastructure funds have reached a final close, securing an aggregate \$22bn in commitments. Interestingly, the number of vehicles and aggregate capital raised for Asia-focused infrastructure funds peaked in the years following the 2008 global financial crisis.

ADB estimates that Asia needs to invest \$750bn in national infrastructure annually over the next seven years. However, when compared to Preqin data, this would suggest that the \$9.4bn in total private capital currently being sought by Asia-focused infrastructure funds in market would only meet 1.3% of the overall short-term infrastructure demand. While this means that fund managers are likely to have no shortage of investment opportunities, the majority of Asia's infrastructure needs will continue to rest on the shoulders of governments or project financing loans made out by banks. However, these entities are unlikely to have the resources to cope with this demand, so significant opportunities for private investors to plug the financing gap are still likely to exist.

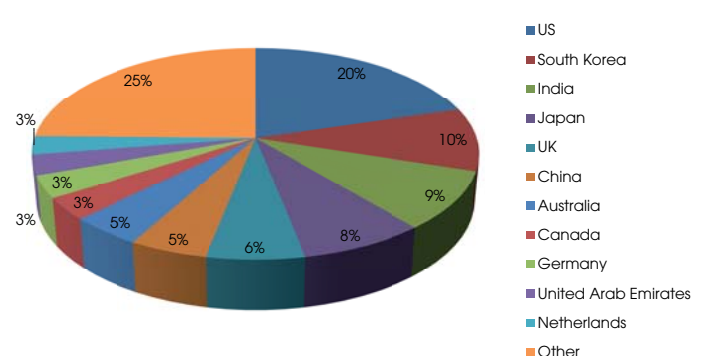
However, there are risks when operating in a developing market. In June 2011, managers raising infrastructure debt funds in India were affected by the introduction of new regulations; fund managers now

Fig. 1: Annual Asia-Focused Infrastructure Fundraising, 2004 - 2013 YTD (As at 2 July 2013)



Source: Preqin Infrastructure Online

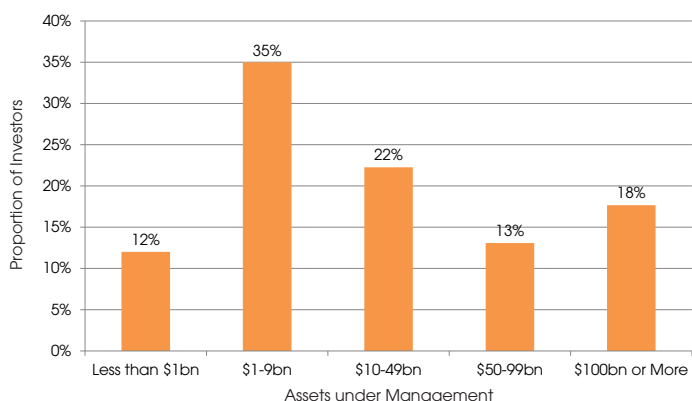
Fig. 2: Breakdown of Infrastructure Investors with a Preference for Asia-Focused Investments by Country Location



Source: Preqin Infrastructure Online



Fig. 3: Breakdown of Infrastructure Investors with a Preference for Asia-Focused Investments by Assets under Management



Source: Preqin Infrastructure Online

had the option of setting up their vehicles as a trust regulated by Securities and Exchange Board of India or as a company regulated by the Reserve Bank of India. The rollout of new regulations meant that managers that were on the fundraising trail at the time had to halt and re-register their vehicles. There was confusion and delay in the process and as a result a number of funds were abandoned. This episode highlights one of the risks managers undertake in developing markets such as those in Asia; investors may need to be flexible to respond to potential regulatory changes as well as other political and economic issues that surround investment in developing economies.

Investors in Asian Infrastructure

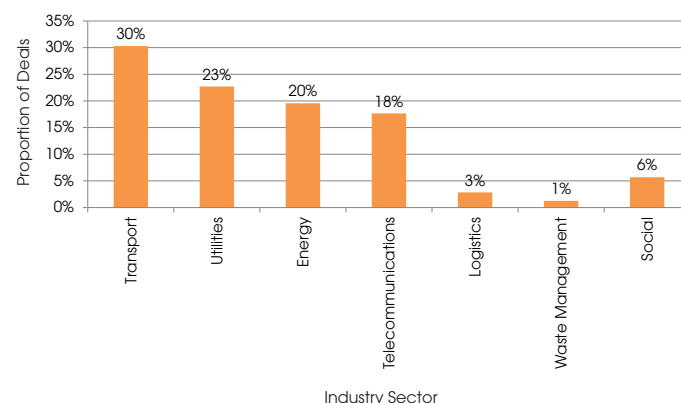
As shown in Fig. 2, the US is home to the largest proportion of infrastructure investors with an interest in Asia-focused investment. Making up 20% of the institutional investor pool, there are twice as many US-based institutions than South Korean investors investing in Asian infrastructure. Indian investors make up 9% of all investors interested in Asian infrastructure. It is interesting to note that only 40% of institutional investors known to have made a previous commitment to an Asia-focused infrastructure fund are actually based within Asia.

Many Asia-based investors appear more prepared to target the additional returns that may be generated by greenfield exposure, while most investors based elsewhere are focusing on gaining exposure to lower-risk, income generating assets.

In terms of strategy, unlisted funds are the most favoured route to market with both Asia-based and non-Asia-based investors, followed by direct investments and listed funds. Infrastructure funds are the most viable route to market for most investors, with the high barriers to entry and significant resources required for direct investments meaning it is very difficult for many investors to gain exposure to the asset class through this route.

Due to the typically large investment size of infrastructure assets and the higher risk associated with investment in developing economies, infrastructure has traditionally attracted larger institutions. Fig. 3 shows this remains the case; according to Preqin data only 12% of investors interested in Asian infrastructure have less than \$1bn in total assets under management (AUM). Thirty-five percent of investors have total AUM of between \$1bn and \$9bn, with a further 35% of investors having total AUM figures of

Fig. 4: Breakdown of Infrastructure Deals in Asia by Industry Sector, 2004 - 2013 YTD (As at 2 July 2013)



Source: Preqin Infrastructure Online

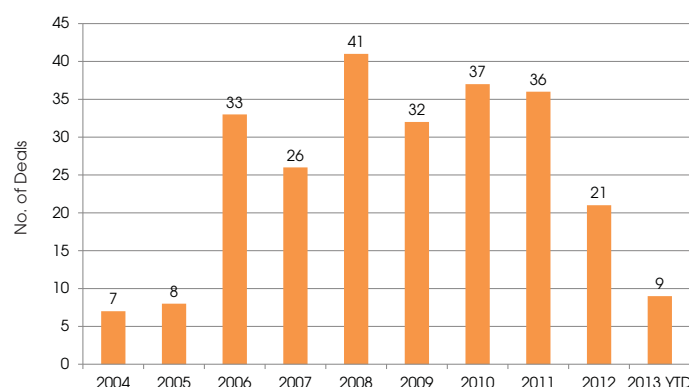
between \$10bn and \$99bn; only 18% of investors have total AUM above \$100bn.

Deals

Within Asia, the transport sector has seen the greatest proportion of infrastructure deals in the period since 2004. As can be seen in Fig. 4, 30% of all Asian deals made by unlisted infrastructure fund managers during this period have been transport-related and include assets such as airports, railroads, roads and sea ports. Utilities infrastructure makes up the next largest proportion of deals in Asia (23%), while energy and telecommunications assets make up 20% and 18% of total deals made in Asia respectively. Social infrastructure represents 6% of total unlisted infrastructure deals made in Asia since 2004. As most of Asia is still under development, core infrastructure, which provides essential services to the population, has generated the most interest.

A case in point is Myanmar, a nation that was ruled by a military junta as recently as November 2010. Having renounced its troubled past, the country – the largest on the southeast Asian mainland – has instituted political and economic reforms, and set itself on the road to a democratic nation with a free market. In June 2013, Myanmar granted telecommunications licenses to two consortia to build and operate a nationwide mobile phone network. The country has plans to develop and upgrade new/existing airports under PPP/PFI arrangements; it has already identified a series of airports such

Fig. 5: Annual Number of Deals Made in Asia by Unlisted Infrastructure Fund Managers, 2004 - 2013 YTD (As at 2 July 2013)



Source: Preqin Infrastructure Online



as Yangon, Mandalay, Hanthawaddy and Dawei as potential deals for private capital. In addition, there is an urgent need to expand road and rail networks in order to fulfil the nation's obligations to the ASEAN regional connectivity plan. In 2013 so far, nine deals have been completed by private infrastructure fund managers in Asia (Fig. 5). This figure is likely to rise as investment opportunities in Myanmar and others across the rest of Asia provide significant avenues for infrastructure managers seeking to put their capital to use.

Conclusion

Asia presents a unique combination of developed markets such as Singapore and South Korea, interspersed among emerging economies like India, Laos and Myanmar. The demographics and economic conditions of each nation generate different infrastructure demands, which offer rich investment opportunities for a wide spectrum of managers and investors. With ASEAN aiming to reach economic integration by 2015 and the opening up of China and India continuing, there lies the promise of freer flow of capital, goods, labour and services within the whole of Asia in the years to come. Infrastructure investors and fund managers should therefore pay attention to the region and keep on top of economic and political changes in order to benefit from the wealth of investment opportunities being created in the region.

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