



Targeting Investor Capital: How Can GPs Address Investor Concerns?

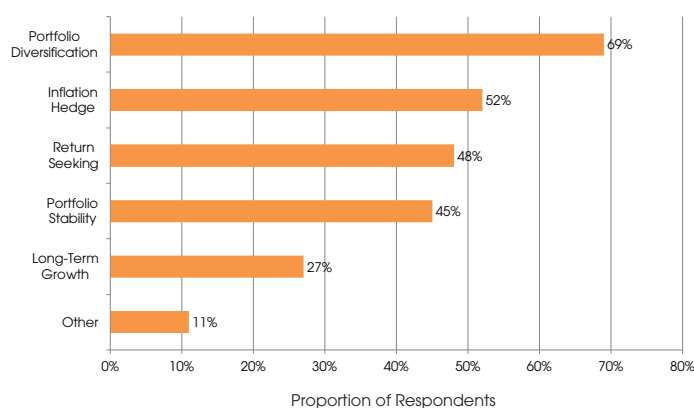
Although a significant proportion of infrastructure investors are planning to make new commitments in the coming year, fund managers face a number of challenges when it comes to securing capital. [Elliot Bradbrook](#) explores investors' key concerns and how GPs can target and address these when bringing their funds to market.

Earlier this month, Global Infrastructure Partners II reached an historic \$8.25bn final close, becoming the largest unlisted infrastructure fund raised since the asset class's inception. Following the closure, Meridiam Infrastructure reached a \$1.05bn final close on its Meridiam North American Infrastructure Fund, taking the total capital raised by unlisted infrastructure funds in 2012 YTD to \$19.6bn. These closures have completely changed the profile of the 2012 fundraising market, with the total capital raised by infrastructure fund managers this year almost doubling within the first few weeks of Q4 2012.

This shows what can be achieved by fund managers able to illustrate strong past performance and offer investors attractive terms and conditions. Although very positive, the general infrastructure fundraising outlook remains unchanged. The market is still highly congested, with 141 funds currently on the road targeting an aggregate \$86.4bn. Investor interest in the infrastructure space is growing, but issues such as high fund manager fees, liquidity, and a lack of manager experience continue to impact investor appetite for infrastructure funds. Many institutions still have reservations about either entering or increasing their exposure to the asset class.

In Preqin's most recent survey of infrastructure investors published in the 2012 Preqin Infrastructure Review, institutions were asked about the key issues preventing the flow of investor capital into the infrastructure asset class. In this feature article we explore these issues further in order to highlight how fund managers can address key investor concerns when looking to secure fresh capital commitments.

Fig. 1: Breakdown of Infrastructure Investors by Reason for Investing in Infrastructure



Source: 2012 Preqin Infrastructure Review - August 2012 Preqin Investor Study

What are Investors Looking for?

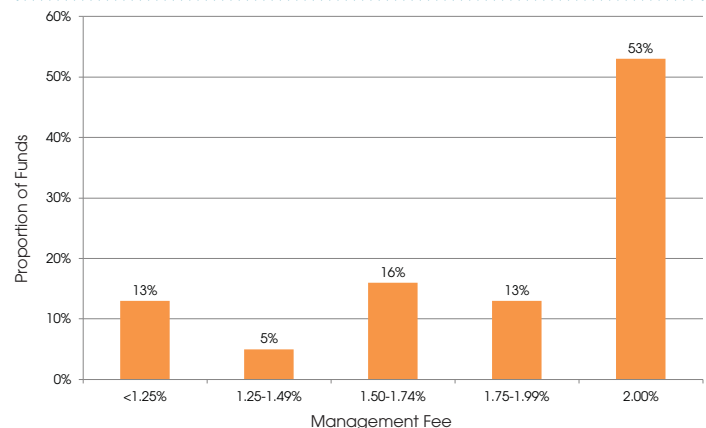
Fig. 1 shows that institutional investors target infrastructure assets for a number of different reasons. Fund managers should consider paying close attention to these requirements in order to improve the chance of fundraising success, particularly in such a challenging and crowded marketplace. A significant 69% of respondents to our investor study look to infrastructure to provide portfolio diversification, while 52% use infrastructure as an inflation hedge and 45% invest in the asset class for portfolio stability. A further 48% consider infrastructure to be a return seeking investment, while 27% invest in infrastructure for its long-term growth potential.

Depending on the type of infrastructure fund being raised, fund managers may consider structuring their funds with these concepts in mind in order to attract investor commitments. Institutional investors are now considerably more cautious when committing capital to unlisted infrastructure funds and will only invest with those managers able to clearly illustrate an understanding of their investor base.

Key Investor Concerns

Many institutional investors continue to struggle with the discrepancy between the risk/return profile of infrastructure assets and the level of management fees charged by fund managers utilizing the private equity fund model. One investor summarized: "There are very few core fund offerings with reasonable fees. The private equity model is too expensive given the return characteristics of

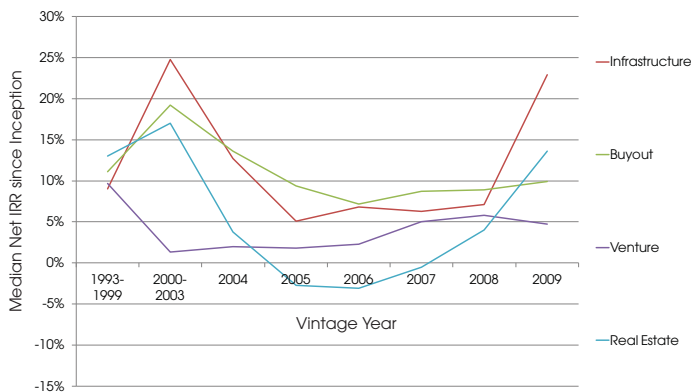
Fig. 2: Management Fee Charged During the Investment Period for Funds Raising and Vintage 2010-2012 Funds Closed



Source: Preqin Infrastructure Online



Fig. 3: Infrastructure vs. Other Private Equity Strategies - Median Net IRR by Vintage Year

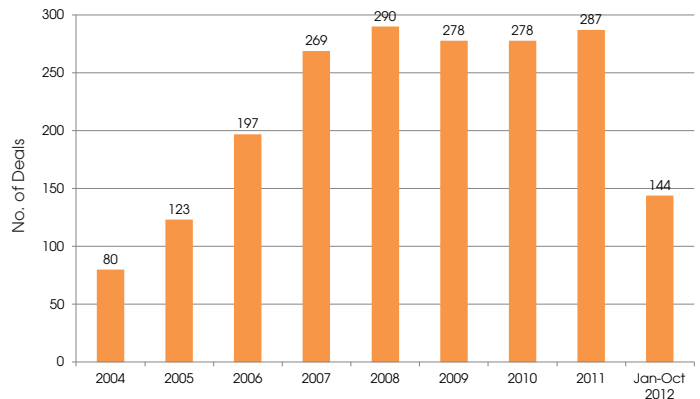


Source: Preqin Infrastructure Online

the underlying asset.” Investors are now largely unwilling to pay high fees, particularly to managers without a proven track record or those targeting assets likely to generate a lower rate of return. However, many GPs continue to operate under the traditional 2/20 private equity structure.

Fig. 2 shows the management fee charged during the investment period by funds currently raising capital and vintage 2010-2012 funds closed. Fifty-three percent of these funds have a management fee of 2%, showing that despite increased investor pressure, over half of fund managers continue to apply the private equity model to infrastructure funds. However, a significant 47% of fund managers are charging a fee lower than 2%, with 13% charging lower than 1.25% during the investment period. Many

Fig. 4: Number of Deals Completed by Unlisted Infrastructure Fund Managers, 2004 - October 2012



Source: Preqin Infrastructure Online

GPs also have structures in place to reduce the management fee charged in different circumstances, such as in return for a higher level of investor commitment.

A fair proportion of managers are therefore beginning to consider investor demand when it comes to setting management fees. Higher fees may be warranted for funds targeting higher risk developmental infrastructure projects, which are more closely aligned with the private equity structure, but not for those funds targeting lower risk brownfield and secondary stage assets. Investors recognize and are largely comfortable with the fact that infrastructure funds may generate lower returns than private equity or real estate vehicles, but expect management fees to reflect this.

Preqin Quarterly - Q3 Editions Out Now!

All the latest statistics, analysis and commentary on key industry trends are now available to download, covering the Infrastructure, Private Equity, and Private Real Estate asset classes.

These complementary research reports include exclusive data and analysis on investors, fundraising, deals, dry powder, performance, fund terms and conditions and much more.

Click below to download your complimentary copies:

Private Equity

Private Real Estate

Infrastructure

www.preqin.com/quarterly



Another factor that contributes to the debate over the level of management fees charged by infrastructure fund managers is the lack of clear performance benchmarks for the infrastructure industry as a whole. One investor summarized: "A core challenge for us is benchmarking the industry given the lack of matured funds." The majority of unlisted infrastructure funds were launched post-2004, meaning there is only limited performance data available for these vehicles. Unfortunately, until these infrastructure funds mature, benchmarking will continue to be a problem for both fund managers and investors operating in the asset class.

However, the performance of older infrastructure funds gives an indication of what to expect from more recent funds. According to Preqin data, 84% of unlisted infrastructure funds target a net IRR of between 10% and 20%. This is lower than the level of return traditionally sought by private equity or real estate GPs, but older vintage infrastructure funds have performed well in comparison. Fig. 3 shows the median net IRRs achieved by infrastructure, buyout, venture capital and real estate funds of vintages 1993-2009, revealing that despite infrastructure funds traditionally targeting lower returns, the performance actually achieved by vintage 1993-1999 infrastructure vehicles is similar to that of the other fund types shown. Fund managers able to demonstrate a record of good past performance will likely be more successful in the current market, although few firms are realistically able to do so.

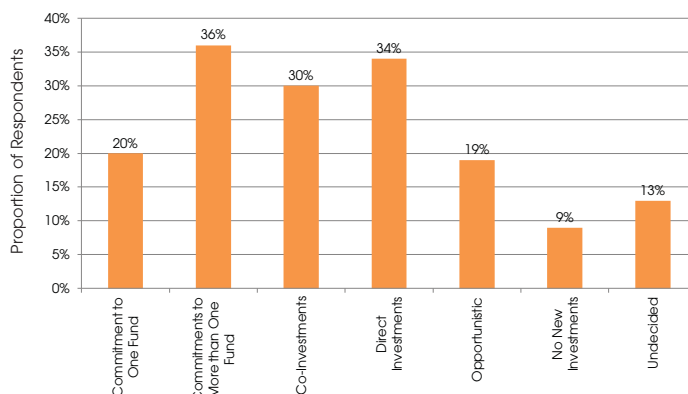
The availability and high cost of debt financing in the current environment is also limiting investor appetite and affecting deal flow. As shown in Fig. 4, the number of deals completed by unlisted infrastructure fund managers grew steadily year-on-year prior to the financial crisis but has plateaued since due to banks becoming less inclined to provide long-term affordable debt financing. A growing number of fund managers have begun to launch debt funds in order to compensate for the shortfall in infrastructure debt financing; however, not all LPs view these vehicles as attractive investment opportunities. One investor highlighted: "The limited availability of debt will restrict deal flow but infrastructure debt funds will close the gap. Unfortunately, infrastructure debt funds will fail to meet our minimum return requirements."

Other notable challenges highlighted include the illiquid nature of the asset class, inappropriate fund structures, high asset valuations and a lack of manager experience. Investors are also concerned that increased competition for assets in the market is driving up the prices of the best infrastructure assets, resulting in the expected level of return becoming unattractive.

Outlook

Growing demand for infrastructure development worldwide has increased private sector interest in the space, with more GPs launching funds and more LPs committing capital to such vehicles. Investor appetite has regained momentum following the financial crisis, although many investors now follow more cautious and conservative investment strategies. As a result, some infrastructure fund managers are now having to make greater concessions to investors in order to secure fresh fund commitments, and are spending more time in market.

Fig. 5: Investor Plans for Infrastructure Investment in the Next 12 Months



Source: 2012 Preqin Infrastructure Review - August 2012 Preqin Investor Study

The amount of fresh capital raised by infrastructure fund managers over the past 18 months shows a healthy investor demand for such exposure. This looks set to continue over the next 12 months, with 78% of surveyed investors stating plans to make some form of infrastructure investment in the next year. As illustrated in Fig. 5, 36% of respondents plan to make multiple unlisted fund commitments in 2012 and 2013 and a further 20% expect to make a single fund commitment. Thirty-four percent plan to pursue direct investments in the next 12 months, while 30% will look to make co-investments. Nineteen percent of interviewed investors will operate an opportunistic investment policy.

This shows that investor interest in the infrastructure asset class remains strong. However, as mentioned, several key issues still constrain the flow of investor capital into unlisted infrastructure funds. Though many fund managers are becoming more attuned to investor concerns, the future growth of the unlisted fundraising market may be dependent on a larger effort to resolve these issues. Managers seeking to raise capital need to be prepared to consider investors' concerns, and address and mitigate them if necessary in order to secure capital commitments. The greater alignment of interest between GPs and LPs that this could produce has the potential to encourage more investors to become active in the asset class.

Subscriber Quicklink:

Subscribers can click [here](#) to access our [Future Searches and Mandates](#) feature, where you can filter investors by their future plans for committing to infrastructure and access their detailed investor profiles.

Infrastructure Online's [Future Searches and Mandates](#) feature allows subscribers to identify potential LPs by searching for institutional investors by their future investment plans, which are constantly updated based on Preqin's direct contact with investors. Please see page 11 for a detailed look at the new feature.

For more information or to arrange a demo, please visit:

www.preqin.com/infrastructure

2012 Preqin Infrastructure Review



alternative assets. intelligent data.

The 2012 Preqin Infrastructure Review, now in its fifth edition, represents the largest and most comprehensive review of the unlisted infrastructure asset class available. With detailed analysis covering the breadth of the industry, including investors, fundraising, performance and more, plus in-depth profiles of GPs, funds and LPs across the world, this year's larger than ever Infrastructure Review is a must have purchase for infrastructure fund managers, investors and third-party service providers.

This year's fully updated edition includes:

- Detailed analysis sections showing the latest trends in all areas of the industry: deals, fundraising, investors, terms and conditions, and the results of our latest in-depth survey of LPs' intentions.
- Profiles of over 350 infrastructure firms and 640 funds. Profiles feature strategy and deals data, as well as direct contact information for key professionals.
- Profiles for over 310 institutional investors in the sector, including investment plans, strategic preferences and key personnel contact details.
- Detailed listings of all funds ever closed, plus funds currently raising capital.
- Information gathered by our dedicated team of analysts from numerous data sources, including via direct interaction with fund managers and investors to ensure the information in the Review is as accurate, comprehensive and exclusive as possible.



www.preqin.com/infreview

Visit www.preqin.com/infreview for more information

Completed Order Forms:

Post (to Preqin):

New York
One Grand Central Place
60 E 42nd Street
Suite 2544
New York
NY 10165

Tel: +1 212 350 0100
Fax: +1 440 445 9595

London

Equitable House,
47 King William Street
London, EC4R 9AF

Tel: +44 (0)20 7645 8888
Fax: +44 (0)87 0330 5892

Singapore

One Finlayson Green
#11-02
Singapore
049246

Tel: +65 6305 2200
Fax: +65 6491 5365

San Francisco

580 California Street
Suite 1638
San Francisco
CA 94104

Tel: +1 415 635 3580
Fax: +1 440 445 9595

Email:
info@preqin.com

I would like to purchase the 2012 Preqin Infrastructure Review:

Single Copy:

- \$795 + \$40 Shipping
- £465 + £10 Shipping
- €550 + €25 Shipping

Additional Copies:

- \$180 + \$20 Shipping
- £110 + £5 Shipping
- €140 + €12 Shipping

Data Pack:

- \$300 / £180 / €220

Shipping costs will not exceed a maximum of \$60 / £15 / €37 per order when all shipped to same address. If shipped to multiple addresses then full postage rates apply for additional copies.

Data Pack contains all underlying data for charts and graphs contained in the publication. Only available alongside purchase of the publication.

Payment Details

- Cheque enclosed (please make cheque payable to 'Preqin')
- Charge my: Visa Mastercard Amex
- Please invoice me

Card Number: _____

Name on Card: _____

Expiry Date: _____

Security Code: _____

Shipping Details:

Name: _____

Firm: _____

Job Title: _____

Address: _____

City: _____

Post/Zip: _____

Country: _____

Telephone: _____

Email: _____



American Express, four digit code printed on the front of the card.



Visa and Mastercard, last three digits printed on the signature strip.