2012 Infrastructure Review: Is the Market Regaining Momentum?

Though the unlisted infrastructure fundraising market suffered as a result of the financial crisis, recent data suggests that the market may be regaining momentum. Elliot Bradbrook explores the current infrastructure market and outlook for the future, featuring data from the newly released 2012 Preqin Infrastructure Review.

The unlisted infrastructure fundraising market has undeniably struggled to regain momentum following the global financial crisis. A number of factors have contributed to this, including increased investor caution, a misalignment of fund manager and investor interests, and ongoing global economic uncertainty. Infrastructure fund managers are now faced with a highly competitive fundraising market featuring a large number of funds on the road seeking capital from an increasingly conservative investor base.

Fundraising

As illustrated in Fig. 1, unlisted infrastructure fundraising declined by 77% between 2008 and 2009 in the midst of the financial downturn, and although a healthy $32.1bn was raised by 46 funds reaching a final close in 2010, much of this capital was raised pre-crisis by funds that had been on the road for over two years. Subsequently, in 2011, 40 infrastructure funds closed having raised $22.4bn in aggregate capital, an unsurprising 31% decline on the amount raised in the previous year. As of September 2012, 22 unlisted infrastructure funds have reached a final close in the year to date, raising $10.1bn from investors.

This gradual fall in annual fundraising is also evident in the average size of funds to close during the period – $699mn in 2010, $586mn in 2011, and $507mn between January and September 2012. Despite fund managers continuing to successfully raise capital from institutional investors, the vehicles they are raising have decreased in size in recent years as GPs target lower and more realistic levels of capital. Therefore, although infrastructure fund managers have managed to close a respectable number of funds year on year since 2010, the aggregate capital raised has been less.

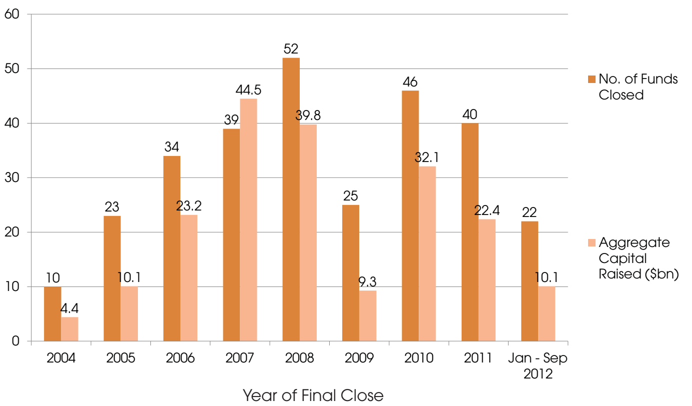
Despite this, it should be noted that many of the funds to reach a final close over the past two years were relatively new to the market and closed having raised fresh institutional capital. A considerable $19bn was also raised by funds holding an interim close between January and September 2012, which suggests investor appetite for infrastructure funds remains resilient. Many of these funds expect to hold final closes in the coming months, which will boost final 2012 fundraising figures by the end of the year.

Fundraising conditions are expected to remain tough in 2013, although infrastructure fund managers continue to launch new vehicles. As shown in Fig. 2, 143 unlisted infrastructure funds are currently on the road seeking an aggregate $92.6bn, a 15% increase compared to the number of funds that were in market in January 2011 and 7% more in terms of aggregate capital sought. With investor interest in the infrastructure space on the increase coupled with rising demand for private investment in infrastructure, we can expect fundraising to improve going forward, although fund managers must continue to adapt their terms in order to stand out in such a crowded marketplace.

Deal Flow

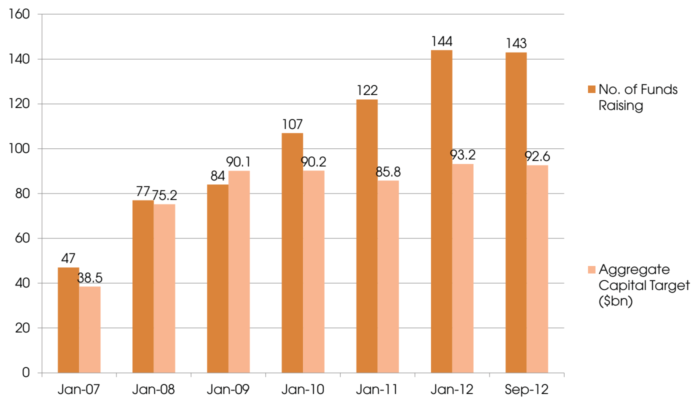
Infrastructure deal flow also remains subdued when compared to the steady growth in the number of deals completed by unlisted infrastructure fund managers prior to 2008. The financial crisis

Fig. 1: Unlisted Infrastructure Fundraising, 2004 - September 2012



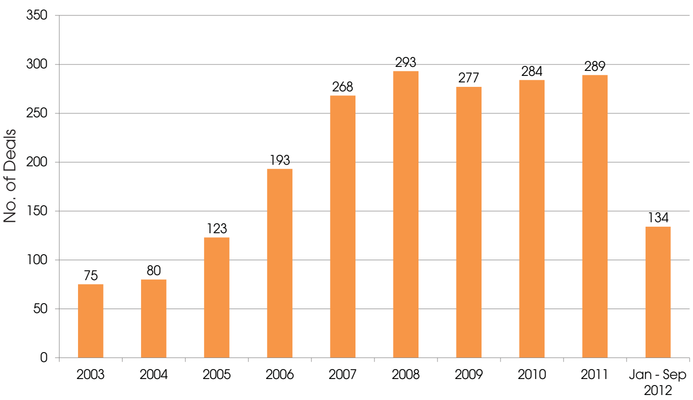
Source: 2012 Preqin Infrastructure Review

Fig. 2: Unlisted Infrastructure Funds on the Road over Time, January 2007 - September 2012



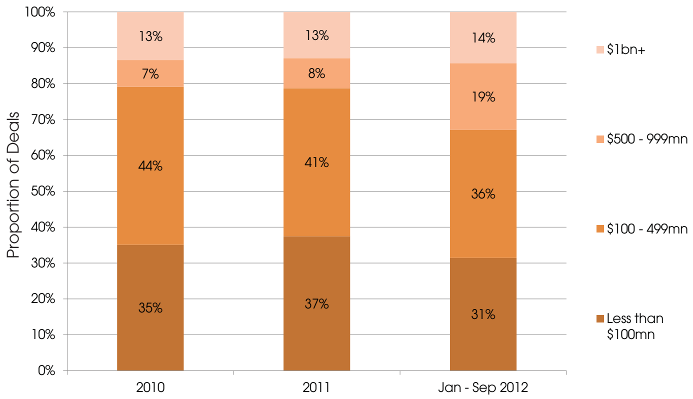
Source: 2012 Preqin Infrastructure Review

Fig. 3: Annual Number of Deals Made by Unlisted Infrastructure Fund Managers, 2003 - September 2012



Source: 2012 Preqin Infrastructure Review

Fig. 4: Breakdown of Unlisted Infrastructure Deals by Transaction Value, 2010 - September 2012

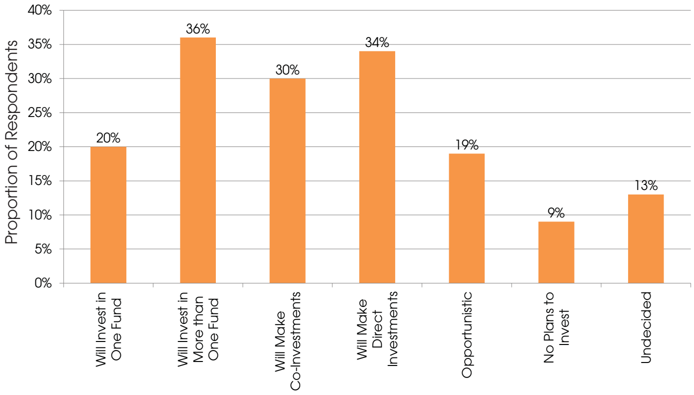


Source: 2012 Preqin Infrastructure Review

placed a huge strain on the credit markets, which has been accompanied recently by ongoing volatility and the impending banking regulations on capital adequacy and liquidity. Infrastructure assets traditionally require significant levels of long-term debt financing, which has become less available and more costly in recent years, causing a plateau in the number of deals being made by fund managers on an annual basis. Unrealistically high asset valuations have also contributed to a subdued level of growth.

Fig. 3 shows the annual number of deals made by unlisted infrastructure fund managers since 2003. Although January to September 2012 deal flow figures will rise as more information becomes available, it is unlikely that the number of completed investments during calendar year 2012 will differ significantly from the 289 deals executed in 2011. However, deal flow has remained relatively steady since 2009, showing that fund managers are still able to source and execute deals regardless of tough market conditions. As shown in Fig. 4, 33% of deals completed between

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



Source: 2012 Preqin Infrastructure Review

January and September 2012 were valued at $500mn or over, a higher proportion than in each of the previous two years.

Investor Sentiment

Preqin's Infrastructure Online database of institutional investors in infrastructure has grown considerably since it was launched in 2008. As of September 2012, the database features profiles of over 1,650 investors actively investing in infrastructure opportunities, plus an additional 160 institutions potentially looking to add an infrastructure element to their investment portfolios in future. These investors gain exposure to infrastructure assets via several routes to market, although the vast majority invest through commitments to unlisted infrastructure funds.

The results of our August 2012 infrastructure investor study illustrate the growing prominence of infrastructure investment among the institutional investor community, with infrastructure now considered a core part of an alternatives portfolio alongside more established asset classes such as private equity and real estate. As shown in Fig. 5, in the 12 months following August 2012, a significant 78% of investors interviewed plan to make some form of infrastructure investment. Thirty-six percent of respondents plan to commit to multiple infrastructure funds, while 20% will invest in a single fund and 19% will pursue an opportunistic investment strategy. Just 9% of investors do not plan to make investments in the next 12 months and 13% remain undecided.

Institutional investor interest in direct investment is growing, with 34% of surveyed investors looking to make direct investments in the 12 months following August 2012. However, direct investment is not feasible for the majority of institutional investors with smaller assets under management and limited internal resources. As such, those investors with more experience may look to make co-investments alongside portfolio managers in order to gain some degree of direct exposure to infrastructure. Thirty percent of respondents plan to make co-investments in the coming 12 months.

These results suggest that despite investor caution, appetite for exposure to infrastructure assets is strong. This looks set to continue going forward, with 62% of surveyed investors planning to increase their exposure to infrastructure over the long term. However, the study also highlighted several issues currently limiting investor activity in infrastructure, such as fund manager fees, a lack of manager experience, and the absence of solid performance benchmarks for the industry. Fund managers must therefore seek to mitigate these concerns in order to successfully attract investor commitments in future.

Outlook

The private sector has grown into a vital source of investment capital for infrastructure over recent years. Although the current economic climate is not conducive to growth, demand for global infrastructure development is on the increase and the public sector is no longer capable of meeting this demand alone. As such, a greater reliance on institutional investors and infrastructure fund managers will develop in future, as governments look to reduce their growing infrastructure funding deficits.

Infrastructure fundraising has suffered since the global financial crisis. However, fund managers continue to successfully raise fresh investor capital and more institutional investors are becoming active in the space. A significant 78% of respondents to our August 2012 investor study are planning further infrastructure investments in the coming 12 months, showing positive investor sentiment over the short term, with many intending to commit capital to unlisted funds. Therefore, irrespective of tough market conditions, infrastructure fundraising looks set to improve going forward.

In order to ensure future market growth, infrastructure fund managers must continue to address investor concerns and seek to more closely align fund manager and investor interests. Issues such as high fund manager fees and fund managers' limited track records continue to restrict the flow of institutional capital into the infrastructure sector, meaning fund managers may need to make some concessions in fund terms for the private infrastructure sector to grow and develop going forward.

2012 Preqin Infrastructure Review

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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.
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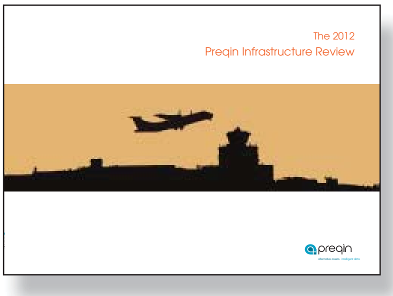
- Detailed listings of all funds ever closed, plus funds currently raising capital.
- Information gathered by our dedicated team of analysts from numerous data sources, including via direct interaction with fund managers and investors to ensure the information in the Review is as accurate, comprehensive and exclusive as possible.



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