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2012 Infrastructure Investor Study: LPs Look to Infrastructure for Stability

This month, Preqin interviewed 75 leading institutions in order to gauge their reasons for investing in infrastructure assets, determine whether their investments have lived up to expectations, and find out more about their plans for the long term. Elliot Bradbrook looks at the results and what we can expect from the asset class in the future.

Infrastructure's Role in Investor Portfolios

In our 2011 investor study, all investors interviewed stated that infrastructure assets would remain an important part of their investment portfolios in future, and this continues to be the case. As shown in Fig. 1, institutional investors invest capital in infrastructure opportunities for a number of reasons; a significant 69% of respondents 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. These reasons for investing have grown in importance, particularly since the global financial crisis, as investors look to establish more diversified and less correlated portfolios in order to reduce risk.

Twenty-seven percent of respondents invest in infrastructure to seek long-term returns; one investor summarized: "We look to infrastructure for a long-term, stable annual yield." The asset class can allow investors to combine portfolio stability with the desire for long-term returns. Additionally, a significant 48% of respondents regard infrastructure as a return-seeking investment strategy similar to private equity and hedge funds.

Breakdown of Study Participants

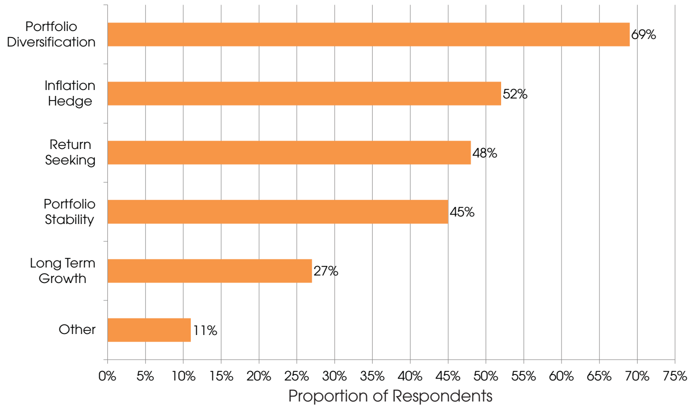
In total, 75 institutional investors were interviewed, including a range of different institutional types based in various locations around the world. Thirty percent of investors interviewed were public pension funds and 9% were private sector pension funds. These two categories represent the most prominent group of active infrastructure investors in the market and therefore provide insight into general investor sentiment. Thirteen percent of respondents were asset managers, 13% were insurance companies and a further 12% were banks. The remaining 23% of respondents included superannuation schemes, family offices, foundations, and sovereign wealth funds, among others.

In terms of geographic location, 43% of respondents were based in Europe, 29% in North America, and 13% in Asia. The remaining 15% of investors interviewed were based outside of these core regions, mainly in South America and the Middle East.

Preferred Routes to Market

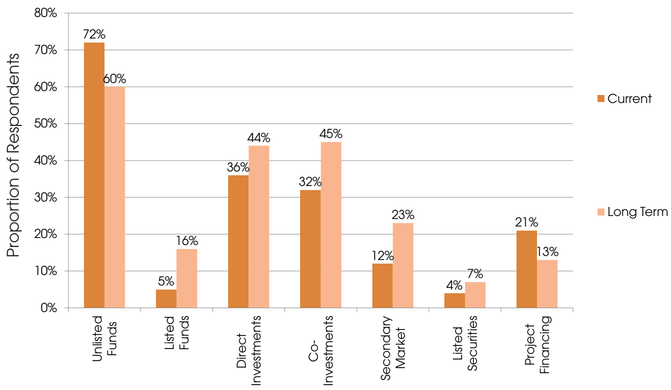
As illustrated in Fig. 2, unlisted infrastructure funds are the primary route to market for the majority of LPs, with 72% of respondents currently utilizing this route. Despite the proportion of respondents planning to invest via unlisted funds in the long term falling to 60%, unlisted funds still look set to be the main route to market for most investors in future. The private infrastructure market was born out of the private equity mould, and it is unlikely that the financing model will change drastically in future, although infrastructure fund/fee structures will continue to be adapted to suit the risk profile of specific assets.

Fig. 1: Investors' Reasons for Investing in Infrastructure Opportunities



Source: Preqin

Fig. 2: Investors' Current and Long-Term Preferred Routes to Market for Infrastructure Investment



Source: Preqin

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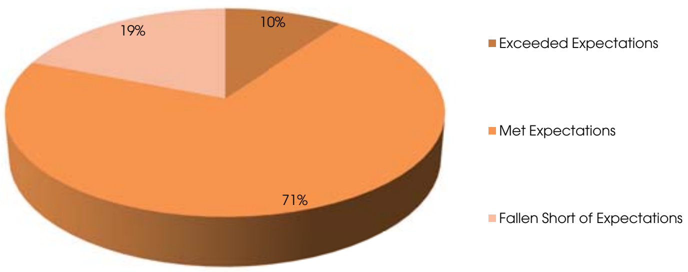
However, as investors gain experience in the asset class and look for different ways of gaining exposure to infrastructure assets, several other routes to market have the potential to grow in the future. Thirty-six percent of investors interviewed currently invest directly in infrastructure assets, growing to 44% for long-term plans, while 32% of respondents make co-investments alongside fund managers currently, growing to 45% for long-term plans. Despite this, the majority of infrastructure investors do not have the resources to begin investing directly, as highlighted by one Canadian public pension fund: "We are simply too small to make direct investments, and will continue to focus on fund commitments and select co-investments."

The infrastructure secondary market also has potential for growth, with 23% of respondents looking to buy or sell fund interests on the secondary market in future, an increase compared to the 12% which do so currently.

Fig. 3: Proportion of Investors that Feel Their Infrastructure Investments Have Lived up to Expectations



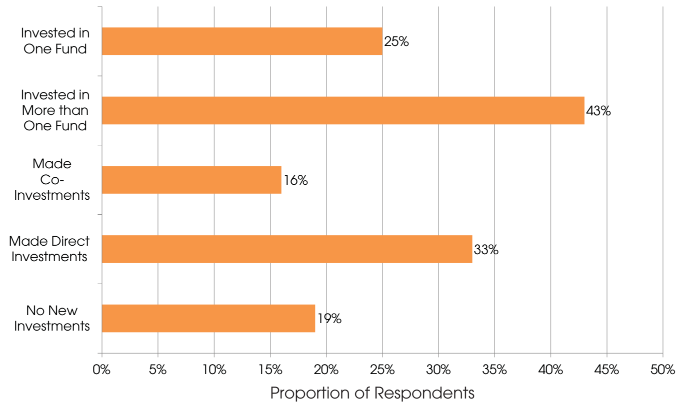
Source: Preqin

Portfolio Performance

The relative youth of the infrastructure asset class often makes it difficult to gauge the performance of infrastructure investments. In order to gain insight into the asset class's current performance, we asked investors to disclose whether the performance of their infrastructure investments has exceeded, met or fallen short of expectations. A significant 71% of investors interviewed stated that their infrastructure investments had performed as expected, and a further 10% felt that their infrastructure returns had exceeded expectations (Fig. 3). One North American bank commented: "As an investor in the asset class since 1998, the sector exceeded our expectations prior to 2007. Since then, returns have been more subdued, and the sector now is meeting expectations."

However, 19% of respondents felt dissatisfied with the returns from their infrastructure portfolios. One North American public pension fund highlighted the difference in performance between higher and lower risk infrastructure strategies: "The private equity model in infrastructure has been disappointing, but the core/long-term model has delivered according to expectations." Several other institutions commented that although infrastructure had not quite lived up to expectations, it had outperformed equities which validated its inclusion in the portfolio.

Fig. 4: Investor Activity in Infrastructure over the Last 12 Months



Source: Preqin

Past Activity and Future Investment Plans

As shown in Fig. 4, 81% of investors surveyed made some form of infrastructure investment over the last 12 months. A significant 43% of respondents committed to multiple unlisted infrastructure funds during the period, while 25% committed to a single fund. Thirty-three percent of investors interviewed made direct investments in infrastructure assets and 16% made co-investments alongside portfolio fund managers.

Encouragingly, 78% of investors interviewed stated plans to make further infrastructure investments in the coming 12 months, and just 9% do not expect to increase their exposure; 13% remain undecided. As illustrated in Fig. 5, 36% of respondents plan to make multiple fund commitments in 2012-2013 and a further 20% plan to make a single fund commitment. Thirty-four percent expect to pursue direct investment strategies in the coming 12 months, while 30% will look to make co-investments. Nineteen percent of interviewed investors will operate an opportunistic investment policy.

Long-Term Allocation Plans

Institutional investor interest in infrastructure assets looks set to continue over both the short and long term, according to Fig. 6. A significant 58% of respondents expect to increase their allocation to infrastructure over the coming 12-24 months, a figure which rises to 62% over the long term. Thirty-eight percent of interviewed investors will aim to maintain their existing level of exposure in the coming 12-24 months, while 36% plan to keep the same level of exposure over the long term.

None of the surveyed investors plan to remove allocations to infrastructure from their portfolio going forward. Just 4% of investors expect to decrease their level of exposure over the coming 12-24

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months, and only 2% plan to reduce their allocation to infrastructure over the long term.

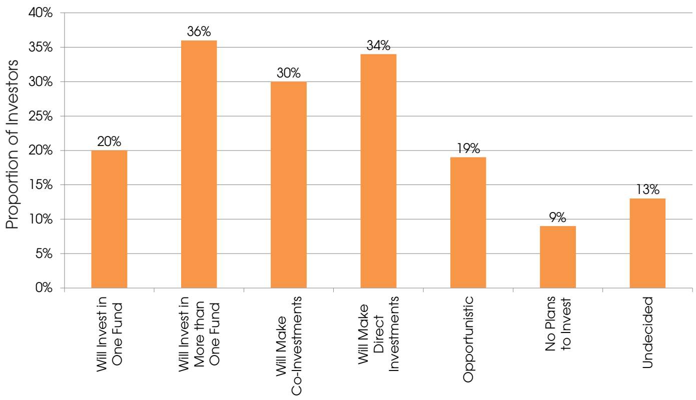
Outlook

The results of Preqin's study suggest a positive outlook for the infrastructure asset class. Institutional investor appetite for infrastructure exposure has risen significantly over the past decade and will continue to grow as these institutions look to capitalize on the increasing demand for infrastructure development worldwide. The private sector will be a vital source of investment capital going forward, and this study suggests that many investors are willing to invest capital in infrastructure opportunities.

Eighty-one percent of investors taking part in the study made infrastructure investments over the past 12 months, and a significant 78% will look to make investments in the coming year. These investors will likely utilize various routes to market including unlisted fund commitments, direct investments, co-investments and secondary market transactions, with a significant 58% looking to increase their infrastructure exposure in the coming 12-24 months. Just 9% of surveyed investors have no plans to invest in the next year.

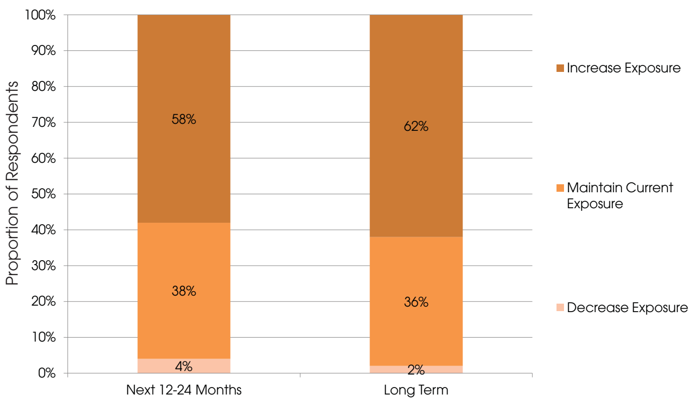
Although those institutions interviewed by Preqin appear to provide encouraging evidence for increasing infrastructure fundraising levels, investors remain highly cautious when making new investments in the current environment. Unlisted infrastructure fundraising remains subdued compared to previous years, with 21 funds reaching a final close in 2012 so far having raised an aggregate $10.2bn. Despite challenging conditions, a significant 144 unlisted infrastructure funds are currently on the road seeking $90.7bn in investor capital, which, in light of the results of our study, suggests that both institutional investors and fund managers are optimistic about the future growth potential of the private infrastructure investment market.

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



Source: Preqin

Fig. 6: Investor Plans for Future Infrastructure Exposure



Source: Preqin

Data Source:

This month's feature article uses data collected for the forthcoming 2012 Preqin Infrastructure Review, the most comprehensive review of the unlisted infrastructure asset class due to be released at the end of September.

To register your interest in the publication and be notified when it is released please contact info@preqin.com.

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