2012 Preqin Global Infrastructure Report

Contents

Outlook for Infrastructure in 2012 - The Road Ahead
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In 2010, the unlisted infrastructure sector welcomed a resurgence in investor confidence which resulted in over $30bn being raised by fund managers worldwide. Despite this growth, it seemed clear that 2011 would continue to shape the future direction of the infrastructure industry with activity still some way off returning to pre-crisis levels. As such, in January 2011, we predicted that investors would remain cautious when making new fund commitments, creating a saturated and highly competitive fundraising market. This proved accurate and resulted in subdued fundraising levels in 2011.

How will the infrastructure sector develop in 2012? The factors that hindered growth in 2011 will likely still apply in the coming 12 months, enhanced by the extreme levels of economic uncertainty around the world. However, with a record number of funds on the road and increased public reliance on the private sector as a source of capital for infrastructure development, it seems likely that the market will continue to grow over the longer term.

Infrastructure Fundraising

In 2011, 28 unlisted infrastructure funds reached a final close having raised an aggregate $16.1bn. This represented a 49% decrease from the $31.8bn raised by infrastructure funds closed in 2010, but is still 85% more than was raised by funds closing in 2009 in the midst of the economic crisis. The average size of funds closed in 2011 amounted to $575mn, lower than the $776mn in 2010 but again higher than the $414mn average in 2009. Despite this dip in annual fundraising, a further $13.1bn in fresh capital was raised by funds holding interim close in 2011, showing good momentum in the fundraising market moving into 2012.

Fundraising Market

As of January 2012, a record 144 unlisted infrastructure funds are on the road targeting $93.2bn in institutional investor commitments. This represents 15% more funds than were on the road in January 2011 and an 8% increase in the total capital being sought by infrastructure fund managers worldwide. In addition, six infrastructure funds of funds and five real asset funds of funds were on the road seeking to raise capital as of January 2012. The fundraising market will remain crowded and challenging in the coming 12 months, and only those managers offering the most attractive opportunities will be successful.

Fund Terms and Conditions

In response to shifting investor sentiment, many infrastructure fund managers have begun to adjust their terms and conditions in order to attract investor commitments. In our mid-2011 study of institutional investor attitudes towards the asset class, 62% of respondents highlighted management fees as the main reason for the misalignment of interests between fund managers and investors, down from the 72% that stated the same in our mid-2010 study. This shows that more fund managers are beginning to recognize the importance of closer GP and LP alignment in order to successfully raise capital. However, more must be done in this area for the market to continue to grow in 2012.

Infrastructure Investors

Investors are now considerably more cautious when committing capital to unlisted infrastructure funds. However, many institutional investors will continue to invest capital, both in 2012 and over the longer term. A significant 62% of respondents to our mid-2011 investor study planned to make infrastructure fund commitments in the following 12 months, while a further 8% planned to make direct investments only and 2% would only make co-investments. Of those that planned to make future fund commitments, 22% expected to invest on an opportunistic basis while 20% expected to make multiple fund commitments. A further 22% remained undecided and expected to finalize their investment policies in Q1 2012.

Infrastructure Deals

A solid 224 deals were completed by unlisted infrastructure fund managers in 2011, a figure that is expected to rise once more information becomes available. However, the number of completed investments is unlikely to rise significantly beyond the 256 deals completed in 2010. Although the strain on the debt markets has eased since 2009, infrastructure fund managers continue to be hindered by the lack of affordable long-term debt financing, as well as growing economic uncertainty. Despite this, it is likely we will see a growing number of deals made by private infrastructure fund managers in the future as governments attempt to reduce their widening infrastructure funding deficits.

Outlook

The road ahead for the infrastructure asset class appears positive. Although 2011 fundraising levels fell short of those achieved in 2010, much of the capital raised was fresh investor capital committed over the past 18 months. A further $13.1bn was raised by infrastructure funds holding an interim close in 2011, showing that institutional investor appetite for such vehicles remains strong. This, coupled with a growing demand for private sector investment to aid in the development of public infrastructure, suggests that the market will continue to grow in the future.

However, with the majority of funds on the road having been launched since the financial crisis, the fundraising market is largely comprised of new vehicles targeting lower and more realistic levels of capital. Institutional investors will remain cautious in 2012, meaning these funds are likely to be on the road for some time and hold several interim closes before reaching a final close. It is therefore unlikely that 2012 fundraising figures will rise significantly beyond those achieved in 2011, if at all, as both investors and fund managers continue to adapt to life in the post-crisis marketplace.

Assets under Management and Dry Powder

Defined as the uncalled capital commitments (dry powder) plus the unrealized value of portfolio assets, the assets under management of the unlisted infrastructure fund industry stand at over $170bn.

Fig. 3.1 charts the measure of infrastructure assets under management, and shows that the assets managed by unlisted infrastructure fund managers more than doubled between December 2006 and December 2008, from $53.8bn to $112.2bn. This growth was due to a successful period of fundraising combined with an increase in the unrealized value of investments.

Despite this dip, assets under management held within the unlisted infrastructure fund market have improved significantly since June 2009, rising to $125bn by December 2009 and $160bn by December 2010. By June 2011, infrastructure assets under management had risen to a record $174bn, 37% higher than in June 2009. This increase was predominantly due to the recovery of the unlisted infrastructure fundraising market following the financial crisis, which resulted in a number of sizeable fund closures in 2010 and H1 2011. Several of these vehicles had already held interim closes enabling them to make investments in portfolio assets prior to holding a final close. As a result, unrealized equity values increased 13% between December 2010 and June 2011, from $92bn to $106bn, whereas dry powder levels remained consistent.

Fig. 3.1: Infrastructure Assets under Management, 2003 - 2011

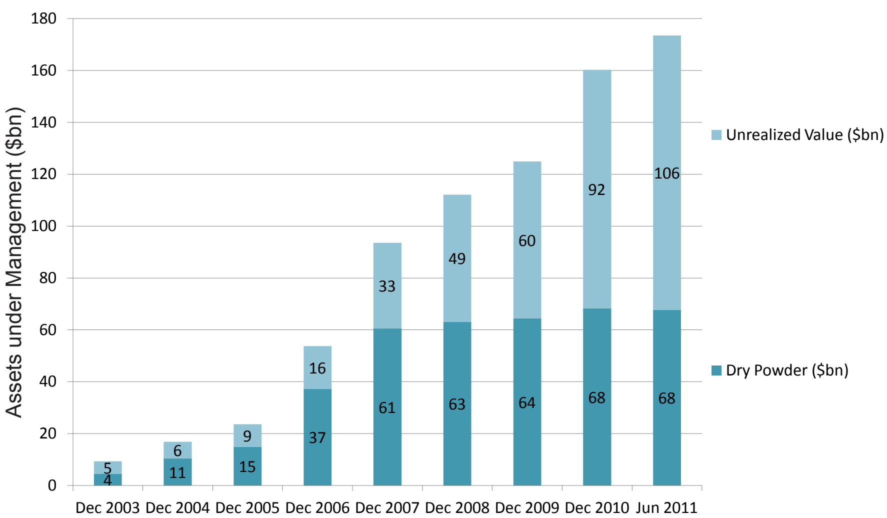
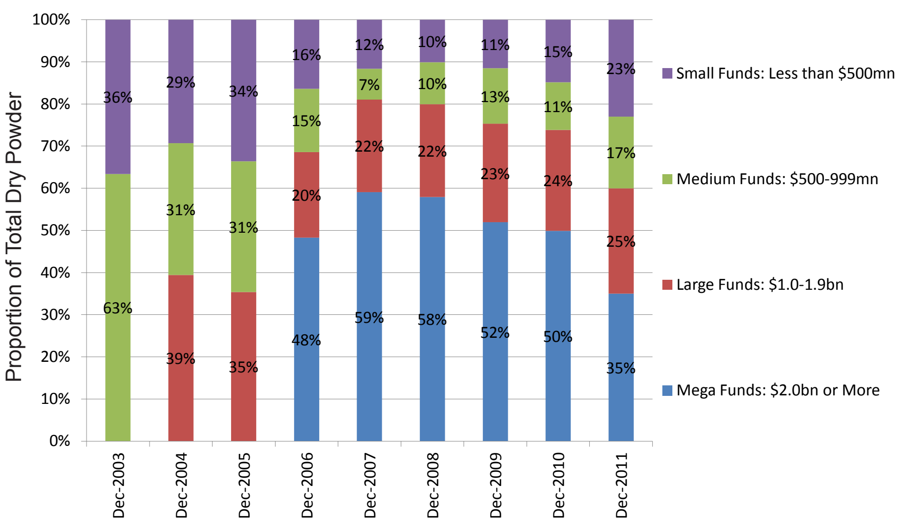


Fig. 3.2: Breakdown of Infrastructure Dry Powder by Fund Size, 2003 - 2011



Infrastructure Dry Powder by Fund Size

Between 2003 and 2007, the average size of unlisted infrastructure funds grew considerably in response to increased investor appetite and rising demand for infrastructure development around the world. Diminishing public resources for infrastructure investment increased the need for private sector involvement, prompting fund managers to launch vehicles with wider and more ambitious investment strategies, leading to increasingly larger fundraising targets.

The emergence of mega infrastructure funds, defined here as those of $2bn or more in size, can be seen in Fig. 3.2. These vehicles began contributing to dry powder in 2006, and from December 2007 to December 2009 accounted for the majority of the dry powder available to infrastructure fund managers. However, in recent years market volatility and increased investor caution caused by the global financial crisis have forced many fund managers to set lower and more realistic fundraising targets. This is shown by the decreasing proportion of mega infrastructure funds' contribution to dry powder levels since 2008.

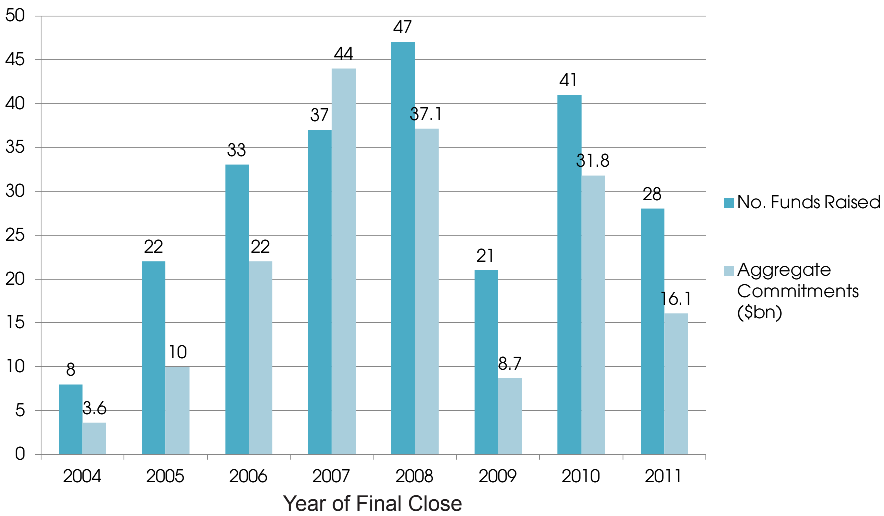
As of December 2011, mega infrastructure funds had $23.8bn of dry powder, which equated to 35% of the total available to infrastructure funds of all sizes. Small and medium-sized infrastructure funds

Overview of the Fundraising Market in 2011

Unlisted infrastructure fundraising fell in 2011, despite a resurgence in fundraising activity during the previous year in the aftermath of the global financial crisis. Fund managers found it difficult to raise capital in 2011 due to the saturation of the fundraising market caused by increased investor caution and growing economic uncertainty. However, much of the capital raised by funds closed in 2011 was fresh capital committed after the financial crisis, which shows that institutional investors are still looking to make new fund commitments.

As shown in Fig. 4.1, 28 unlisted infrastructure funds closed in 2011 having raised an aggregate $16.1bn. This represents a decrease of 49% on the aggregate capital raised by the 41 funds closed in 2010, but still an 85% increase on the aggregate capital raised in 2009. An additional $13.1bn in capital was raised by funds holding an interim close in 2011, which again shows good momentum within the current market.

Fig. 4.1: Annual Infrastructure Fundraising, 2004 - 2011



Average Fund Size

The average fund size in 2011 was $575mn, lower than the $776mn in 2010 but higher than the $414mn average in 2009. Interestingly, 54% of the infrastructure funds to close in 2011 either reached or exceeded their predetermined fundraising targets, with a significant 42% bypassing their targeted levels. In contrast, just 33% of funds that closed in 2010 exceeded their fundraising targets.

The largest fund to close in 2011 was the $3.31bn ArcLight Energy Partners Fund V, which closed in November and exceeded its $2bn fundraising target by 66%. Another sizeable fund to close was the $1.2bn InfraRed Infrastructure Fund III, which raised $200mn above its target. While some managers achieved fundraising successes, other managers struggled to raise capital. Nine infrastructure funds were either abandoned or placed on hold during 2011, indicating continued tough conditions.

Geographic Breakdown

Of the $16.1bn raised by funds closed in 2011, vehicles primarily focused on North America featured prominently, with $8.5bn raised by nine funds. This represents 53% of the total capital raised globally by funds closed in 2011. Seven funds primarily focused on Asia reached final close, raising an aggregate $2.6bn, while six funds closed primarily targeting European opportunities, also raising $2.6bn. Six funds primarily focused on assets based outside these markets closed having raised $2.4bn.

Industry Focus

A breakdown of the funds closed in 2011 by infrastructure industry focus shows that the majority of funds target economic infrastructure assets, mainly in core sectors. Of the 28 funds that closed in 2011, only three focused on a combination of both social and economic sectors, with 25 vehicles targeting economic sectors alone.

Fig. 4.2: Five Largest Infrastructure Funds Closed in 2011

Fund	Manager	Target Size (mn)	Final Size (mn)	GP Location
ArcLight Energy Partners Fund V	ArcLight Capital Partners	2,000 USD	3,310 USD	US
United States Power Fund IV	Energy Investors Funds	1,750 USD	1,713 USD	US
First Reserve Energy Infrastructure Fund	First Reserve Corporation	1,500 USD	1,228 USD	US
InfraRed Infrastructure Fund III	InfraRed Capital Partners	1,000 USD	1,200 USD	UK
Macquarie State Bank of India Infrastructure Fund	Macquarie Infrastructure and Real Assets (MIRA)	2,000 USD	1,169 USD	Australia

Overview of Infrastructure Deals

Fig. 7.1: Annual Number of Deals Made by Unlisted Infrastructure Fund Managers, 2004 - 2011

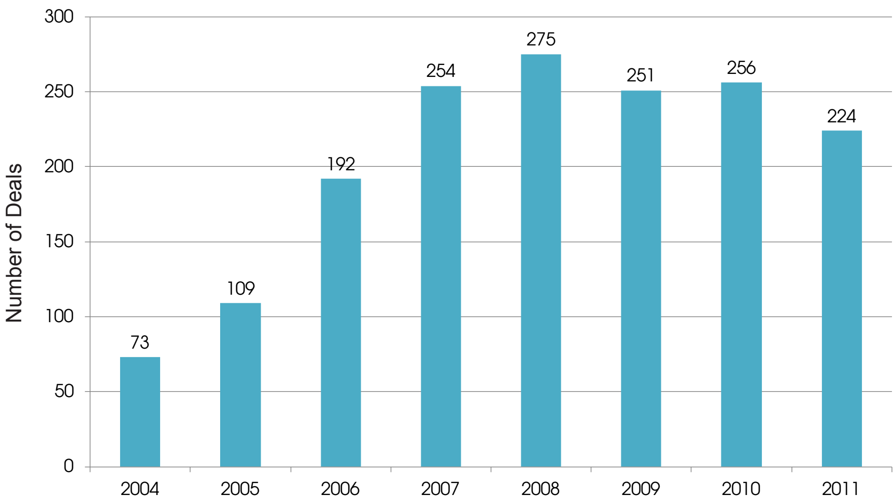
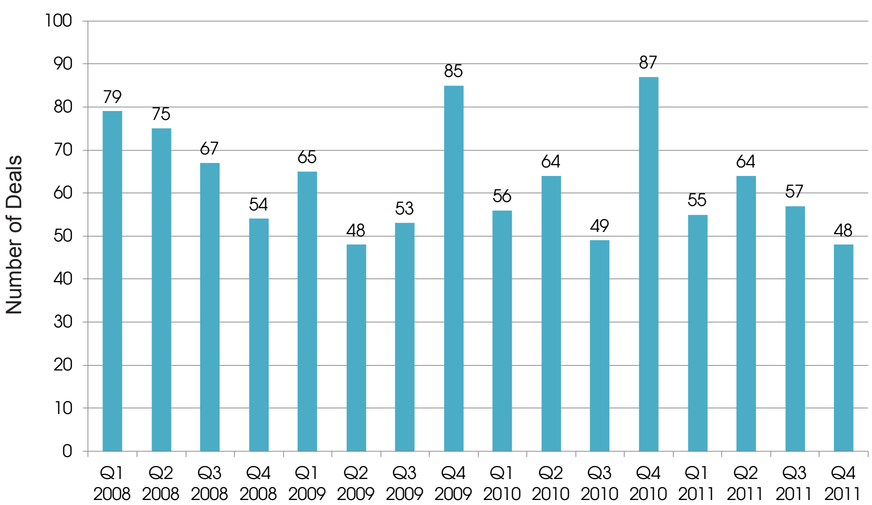


Fig. 7.2: Quarterly Number of Deals Made by Unlisted Infrastructure Fund Managers, Q1 2008 - Q4 2011



A number of notable transactions were completed by unlisted infrastructure fund managers in 2011, including the €1.5bn purchase of the Finnish electricity and heat distribution assets of Swedish utility Vattenfall by the Lakeside Network Investments consortium in December. The consortium, which included 3i Infrastructure Fund, 3i Group, GS Infrastructure Partners II and Ilmarinen Mutual Pension Insurance Company, invested around €525mn in equity and gained over €1bn in debt financing to complete the deal, which is expected to be finalized in early 2012.

As shown in Fig. 7.1, the number of deals finalized by unlisted infrastructure fund managers grew steadily between 2004 and 2008, which mirrors the growth in fundraising experienced during the same period. In terms of the number of deals completed, 1,634 separate investments have been made by unlisted infrastructure fund managers since 2004. Deal flow peaked in 2008 with 275 transactions completed during the year, but has fallen slightly since due to the impact and ongoing effects of the financial crisis and recent economic uncertainty.

The plateau in the number of deals executed per year since 2008 can be attributed to a number of factors. Although the strain on the debt markets has eased since 2009, fund managers continue to be hindered by the lack of affordable long-term debt financing, as well as growing economic uncertainty. Two hundred and twenty-four deals were executed by unlisted fund managers in 2011, a figure that is expected to rise as further information becomes available. However, the number of completed investments is unlikely to rise significantly beyond the 256 deals completed in 2010.

Quarterly Deal Flow in 2011

Analysis of infrastructure deal flow by quarter shows that, aside from the 87 deals completed in Q4 2010, the quarterly number of deals completed by fund managers has remained relatively constant over the past two years. As shown in Fig. 7.2, the average number of deals completed quarterly in 2011 amounted to 56 transactions, less than the 64 per quarter in 2010, 63 in 2009, and 69 in 2008.

Deal Flow by Transaction Size

A number of factors play a role in determining individual deal sizes including asset valuations, leverage, the economic climate, the location and industry sector of the asset, and the fund manager's predetermined investment strategy. Consequently, deal sizes vary greatly throughout the infrastructure industry, ranging from a few million dollars to billions of dollars.

Despite these variations between individual assets, the average size of deals made by unlisted infrastructure fund managers has remained relatively constant since 2004. A small number of exceptionally large deals were completed

Infrastructure Investor Universe by Location

The infrastructure investor universe is geographically diverse, with investors from over 70 countries currently featured on the Preqin Infrastructure Online database. As shown in Fig. 9.3, Europe continues to provide more infrastructure investors than anywhere else, accounting for 42% of the investor universe. North America accounts for the second largest proportion, with 30% of investors, and Asia and Rest of World makes up the remaining 28%.

Europe and Australia played a key role in developing private investment in the infrastructure asset class, and it is therefore unsurprising that a high proportion of investors are based in these regions. The early development of the then niche sector was due to governments in these regions shifting towards privatization, and the adoption of public-private partnerships (PPPs) or private finance initiatives (PFIs). These project finance structures were introduced to provide financing from the private sector for public services such as transportation and healthcare infrastructure. Thirteen percent of infrastructure investors are based in the UK alone, while 7% are based in Australia, the majority of which are superannuation schemes.

A quarter of investors in infrastructure are based in the US, making it the most prominent country in terms of investor numbers. The number of US-based investors interested in infrastructure investment has grown in recent years following the easing of state government restrictions on private and foreign investment in infrastructure assets. This includes several states opening up to private investment through PPP/P3/PFI schemes. The demand for infrastructure development in the US is also increasing following the financial crisis, meaning it is likely that the number of US-based investors will continue to grow over time.

As shown in Fig. 9.4, investors located in the US account for 37% of those considering committing capital to infrastructure, again reflecting the changing government regulations for infrastructure investment in the country. 17% of potential infrastructure investors are based in the UK and 7% are based in Switzerland. In total, Europe accounts for 47% of all investors currently considering an infrastructure allocation.

Fig. 9.4: Breakdown of Investors Considering Investing in Infrastructure by Location

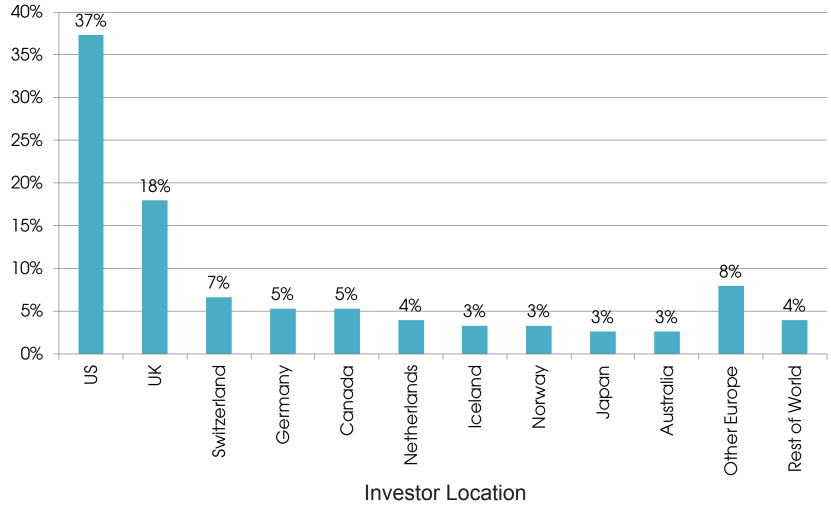


Fig. 9.5: Breakdown of Infrastructure Investors by Assets under Management

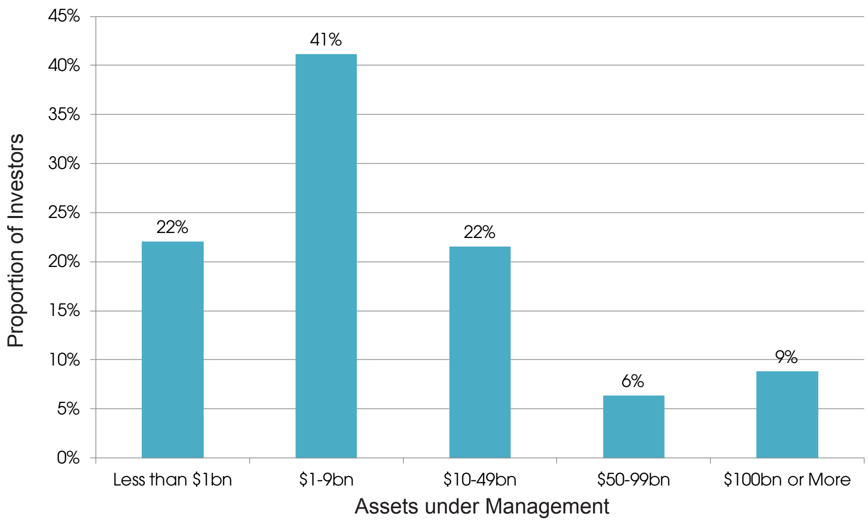
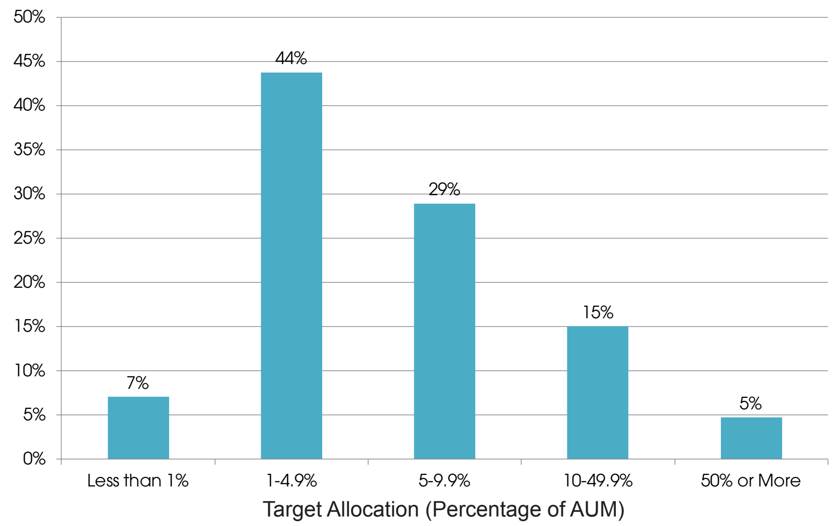


Fig. 9.6: Breakdown of Infrastructure Investors by Target Allocation



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