Bird & Bird

Barometer of infrastructure funds activity in 2022: a pivotal year for the asset class

June 2023

Bird & Bird's International Infrastructure Practice Group are delighted to share the third edition of its barometer on the activity of infrastructure funds in 2022. This long-term study provides a snapshot of the activity of these financial investors over the past year. The study is based on data collected through a survey conducted in partnership with CFNews INFRA and on interviews with managers of infrastructure funds with assets under management ranging from €300m to €15bn. It is also part of a collaboration with France Invest, using the figures published in its annual study on the activities of French private equity and infrastructure fund players, carried out in partnership with Grant Thornton, and the Conatus Finance database at the end of September 2022[1].

Introduction

The rapid increase in interest rates since spring 2022 has already disrupted the private equity market, which is now facing headwinds after a decade of ultra-accommodative monetary policies following the euro crisis. Low - or even negative - returns on deposits encouraged investors into risky assets, while the availability and low cost of credit benefited asset classes that relied on debt, such as real estate and private equity. These particularly favourable conditions helped to broaden the base of LPs beyond “natural” investors such as pension funds and insurance companies. By contrast, monetary tightening tends to shift investment towards fixed income.

In this respect, as we predicted in the 2021 edition of the Bird & Bird barometer, there has been a significant reallocation of assets to money market investments, and all private equity players are finding it increasingly difficult to raise funds. Nevertheless, infrastructure funds remain to be particularly attractive due to their specific characteristics (outstanding performance, low risk profile, resilience in a deteriorating environment). In addition, assets in portfolio are benefiting from the inflationary environment, as their cost structure is largely made up of fixed costs (the cost of debt), while their income is indexed to inflation, which should allow the funds deployed to exceed their initial IRR targets.

The implicit promise of protection against inflation, the vigorous action taken by public authorities to accelerate the energy transition and digitalisation, the growing importance of ESG and the attractiveness of the risk/return trade-off remain strong drivers for infrastructure investment. Thus, despite the restrictive monetary environment, the asset class is likely to remain very buoyant, although inflows are expected to decline sharply in 2023.

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[1] **Conatus Finance –** *“Les Infrastructures non cotées - Collecte record dans un contexte global délicat, poursuite des mégatendances (digitalisation et transition énergétique), léger retour vers le Core”* – October 2022

Collect

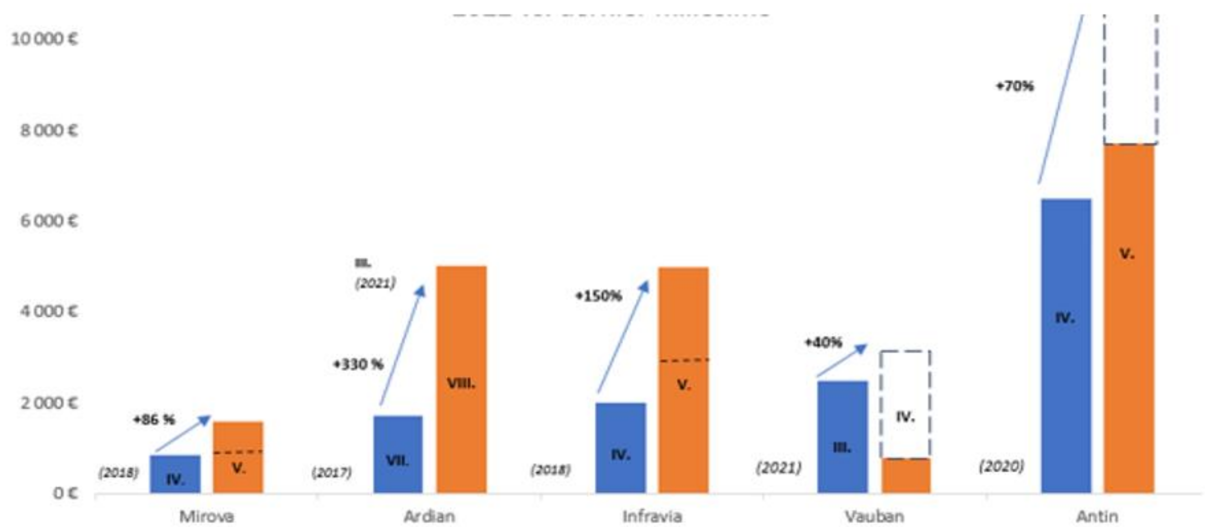
France: fundraising concentrated on a few leading players

In 2022, infrastructure funds continued to raise funds at a high level, confirming the attractiveness of the asset class. According to France Invest, fundraising amounted €16bn in 2022. The slight decrease compared to 2021 (€17.2bn) is mainly due to the concentration of fundraising on a few major players, which leads to some volatility from one year to the next depending on the fundraising calendar of the main management companies, which are now among the world leaders in infrastructure investment. For example, Meridiam, which raised €5bn in 2021, to finance the acquisition of Nouveau Suez, did not launch a new vehicle in 2022. On the other hand, Ardian Infrastructures, Infravia and Mirova raised significant funds during the year. The Ardian ASF VIII Infrastructure secondary fund closed at $5.25bn in April 2022, tripling in size compared with the VII fund raised in 2017. Ardian Americas Infrastructure V closed at $2.1bn. In March 2022, Infravia closed the fifth year of its flagship European Fund at €5bn, well above its initial target of €3bn, and in July, Mirova closed its Energy Transition V fund at €1.6bn against a target size of €1bn. Cube Infrastructures Partners has raised €400m by 2022. Other major funds are still in the process of being raised, including Antin Infrastructure Partners V (€7.7bn raised at the end of March 2023 against a target of €10bn, with a hard cap of €12bn, which would make it the leading infrastructure fund in France) and Vauban (target size of €3.5bn), not to mention Marguerite, with has raised more than €600m by the end of 2022.

This represents a spectacular increase on previous years for these funds. Antin IV closed at €6.5bn in 2020, Infravia IV at €2bn in 2018, Mirova IV at €859m in 2018 and Vauban Core Infra at €2.5bn in 2021. Buoyed by their remarkable performance and investors' appetite for Article 9 funds, asset management companies are finding it easy to retain their existing subscribers and attract new ones by launching increasingly ambitious vehicles.

The chart below illustrates the growth of flagship funds by comparing the current fundraising of a selection of funds with the fundraising of the previous vintage of the same funds.

Fundraising 2022 vs. previous year



Previous year Fundraising 2022 -- Target size

In terms of investors (LPs), the France Invest study shows that pension funds, funds of funds and insurance companies remain the main investors in the asset class, accounting for almost 80% of the amounts raised in 2022. However, the share of sovereign wealth funds has almost doubled in 2022 to 11% of the funds raised, thanks to a sharp increase in subscriptions (+83% to €1.744m). Given the ongoing reallocation process, several players expect the LP base to refocus on “natural” investors in the asset class over the coming months, i.e., those with long-term liabilities such as pension funds and insurance companies.

It should be noted that foreign investment will account for 80% of the capital raised by French infrastructure funds in 2022[2]. This share is higher than the 2017-2021 average, which was only 69%. Furthermore, 37% of the funding came from Europe and 43% from outside Europe.

Increase in global fundraising driven mainly by mega funds

Globally, according to Preqin data used by Conatus Finance, 2022 has been a record year for infrastructure fundraising, with a threshold of $139.6bn[3] raised in the first three quarters, to which was added more than $40bn raised in the last quarter to exceed $180bn. By the end of September 2022, the amounts raised were already 8% higher than the amounts forecast for the whole of 2021. Infrastructure funds have seen double-digit growth every year since 2011 (excluding 2020), when they totalled just $29.9bn, five times less than in 2022. These figures are even more impressive given that the number of funds is roughly the same as in 2021 (70 in 2021 compared to 65 in 2011, following a peak of 155 funds in 2019).

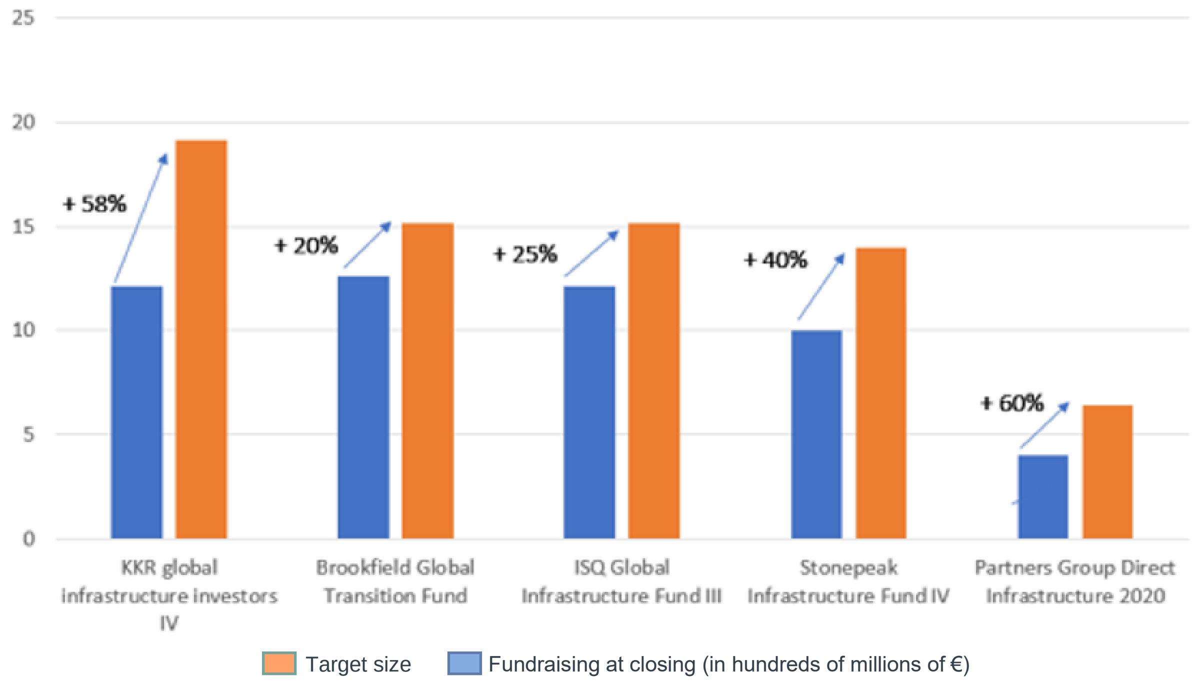
As in France, there has been a high concentration of fundraising in a few mega-funds: four of them have raised more than $10bn (KKR, Brookfield, ISQ, Stonepeak) and three others raised between $5 and $10bn, including France's Ardian (ASF VIII) and Infravia (European Fund V). This naturally implies a larger ticket size and a larger average fund size. The larger funds raise significantly more, well above their hard cap.

The energy transition attracted €27.8bn in capital worldwide, raised by eight funds, representing an 85% increase compared with 2021. However, a large part of this amount is attributable to the $15bn raised by Brookfield, while 13 other funds continued their fundraising in 2022 for smaller amounts of less than €1bn.

The chart below shows the main funds that raised money in 2022, comparing the amount raised at closing with the initial fundraising targets. Among them are the biggest names in the sector: KKR closes at $17bn via its KKR Global Infrastructure Investors IV fund, Brookfield raises $15bn for Brookfield Global Transition, as does ISQ for ISQ Global Infrastructure Fund III. Next in line are Stonepeak Infrastructure Fund IV with $14bn and Partners Group Direct Infrastructure with $6.4bn. Ardian (ASF VIII Infrastructure), InfraVia (InfraVia European Fund V) and Macquarie (Macquarie Asia Infrastructure Fund III) complete the picture, with inflows of around $5bn. But the smaller funds have also exceeded their target size.

[2] **Etude France Invest & Grant Thornton –** “*Activité des acteurs français du capital-investissement”* – March 2023
[3] **Etude Conatus Finance –** *“Les Infrastructures non cotées - Collecte record dans un contexte global délicat, poursuite des mégatendances (digitalisation et transition énergétique), léger retour vers le Core”* – October 2022

5 largest infrastructures fundraisings worldwide - September 2022



The Conatus study also highlights the relative attractiveness of the “infrastructure” asset class compared with other non-listed strategies, all of which are experiencing declining inflows. At the end of September 2022, infrastructure accounted for 14% of funds raised in non-listed strategies, compared with 9% in 2021, overtaking real estate for the first time. The impact of rising interest rates is particularly pronounced in private equity (down 36% at end-September 2022 vs. FY 2021) and real estate (down 51%). Until interest rates stabilise or even fall, infrastructure funds appear to be relatively unaffected by investor aversion to unlisted assets.

Strategies

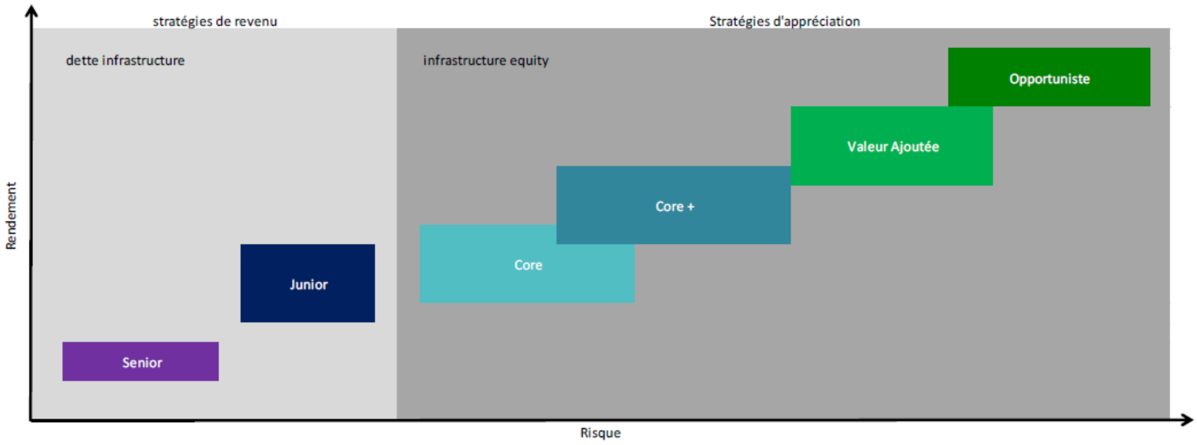
Core + and Value-Added assets remain at the heart of fundraising

On a global scale, Core + and Value-Added strategies dominated inflows in 2022, with no fewer than 19 funds in this segment closed at the end of the year for a total value of €87.2bn. This represents 60% of all capital raised. Not to mention the fact that three funds had not yet completed their fundraising, for an additional aggregate target of more than €20bn. This trend is also evident in France. These include the Vauban Core Infra IV, Ardian Americas Infrastructure Fund V and Antin Infrastructure Partners V funds, which are positioned in the Core + and Value Add segments.

Progressive refocusing on Core strategies

Another key trend in 2022 will be a refocusing on core strategies. In recent years, the boundaries between private equity and infrastructure investment have become blurred. The acquisition of the new Suez by Meridiam, Caisse des Dépôts and GIP in January 2022 can be seen as a predominantly infrastructure private equity investment. Similarly, investments in certain social infrastructures (crèches, nursing homes, etc.) or in assets such as campsites, reflect a certain overlap between the strategies of infrastructure funds and those of "traditional" private equity funds. The search for higher IRRs, investor appetite and the abundance of credit have pushed infrastructure funds to the frontiers of their natural field of intervention.

By contrast, the current environment is more favourable to funds specialising in core strategies, which involve very long-term investment horizons in assets with zero or very low risk, but, logically, with more limited ambitions in terms of IRR. In this respect, we note the consistency of Vauban, whose flagship Core Infrastructure fund has very similar characteristics from one vintage to the next. In the allocators' portfolios, the infrastructure asset class has thus fully rediscovered its role as an intermediary investment between debt and equity, as illustrated by the graph below[4].



Several asset management companies have also recently launched more core-focused strategies, including EQT, Blackrock, Macquarie, Brookfield, etc., usually through evergreen funds. Fundraising targets in this segment amounted to €58bn, spread across 25 funds, representing a third of prospected stocks compared to 20% in 2021. Core-oriented funds did not raise much in 2022, with only six funds, and for cumulative values of less than €10bn. However, these low levels are specific to this asset class, which requires smaller funds. In addition, several new vehicles have been launched this year. Their fundraising targets were more ambitious than usual, resulting in a moderate decline in core and super-core strategies. These include Macquarie European 7, which has already raised €6bn in 2022, Blackrock Evergreen and EQT Super Core which are targeting €5bn, etc. Not forgetting the evergreen funds, most of which are core funds, but which are rarely included in the amounts raised at a fixed date.

Emergence of new strategies
Managers already well established in the asset class are also experimenting with new approaches. Brookfield and Copenhagen Investment Partners, for example, have launched a new strategy based on clean hydrogen. Ardian soon followed with its Hy24 fund, which closed at €2bn. According to the Hydrogen Council's latest report (2021)[5], decarbonised hydrogen represents no less than $300bn, including $70bn in public investment. The depth of this market points to the development of this sector as a new investment universe, driving renewed infrastructure strategies. In the hydrogen sector, 2022 saw Mirova and Hy24 invest €200m in Hy2gen AG, a pioneer in the production of green hydrogen.

On the edge of the "pure infra" asset class, the launch by InfraVia of a fund dedicated to critical metals offers another example of diversifying strategies into related sectors linked to the energy transition. The fund is targeting €2bn in assets under management, of which €500m will be contributed by the French government as part of the France 2030 plan.

Investments

General trends

In France, while inflows have fallen slightly, infrastructure investment has increased sharply compared with 2021. According to France Invest, infrastructure funds invested €11.6bn (+30%) to support 176 projects (+15%). 26 projects were supported with at least €100m, including six with more than €500m, compared to only two in 2021.

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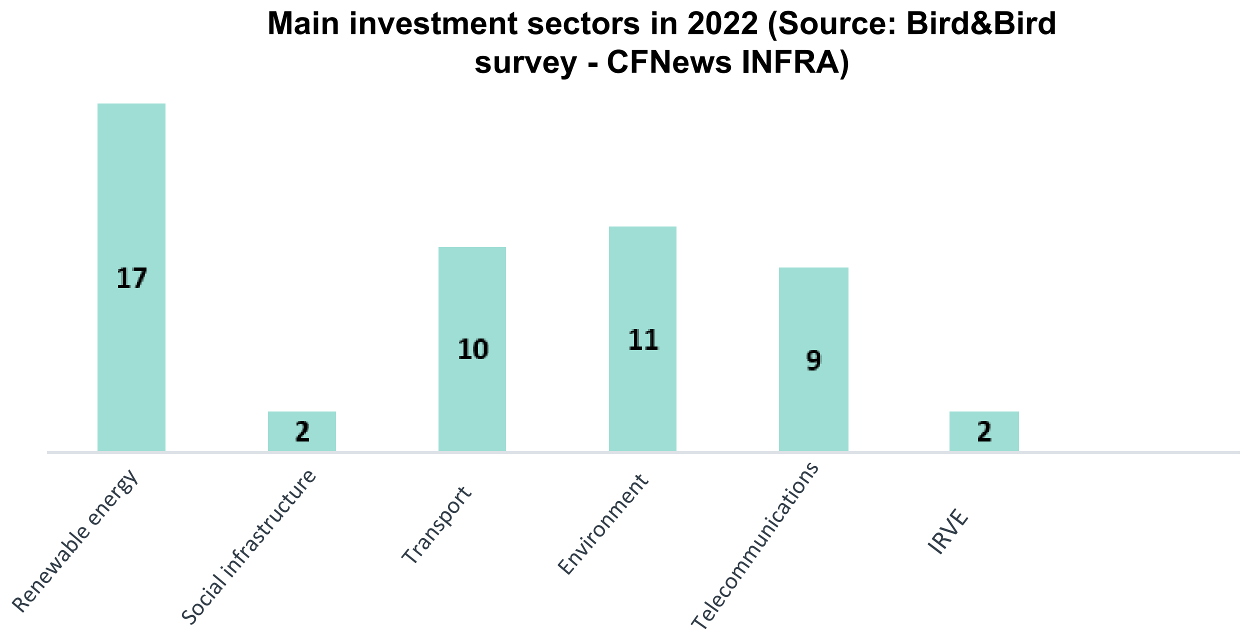
4 Source Blackrock, February 2015

5 [Les investissements annoncés dans l'hydrogène dépassent 300 milliards de dollars - Transitions & Energies (transitionsenergies.com)]

There was a significant increase in the number of companies invested in (176, i.e., +15% compared with 2021). These funds were mainly allocated to projects in France (27%) and Europe (57%).

Investment Sectors



In terms of investment sub-sectors, the environmental and digital transition remains the core target, especially as it benefits from strong public support, from the recent IRA law in the United States to the Fit for 55 package in Europe. According to France Invest, French infrastructure funds have invested €3.914m in renewable energy, in France and abroad, an increase of 79% compared to 2021. Ardian has also launched its very first evergreen fund in this investment universe: Ardian Clean Energy Evergreen, with a target of €1bn. Decarbonised energies are attracting an increase share of investment, while the financing of fossil fuel is becoming more difficult (both in terms of equity and debt, with the gradual withdrawal of major financial institutions). The most notable investments of the year were Ardian's acquisition of 75% of GreenYellow from Casino in October 2022 (valued at €1.4bn, giving an EBITDA multiple of 17.5x) and the sale of Reden Solar by Eurazeo and InfraVia to Macquarie in March 2022, for an enterprise value of €2.5bn (18x EBITDA).

The sub-sector includes wind and solar infrastructure, but also energy storage, electric vehicles, and smart cities, as well as hydrogen, which is emerging as a separate segment through the HY24 fund (Ardian), which is fully dedicated to this resource, and Mirova Energy Transition 5, which invested €200m in Hy2gen AG, a producer of green hydrogen. In 2022, renewable energies will account for 61% of projects financed by infrastructure funds worldwide and 71% of infrastructure projects in France.

Data centres also continue to attract investor interest. This is particularly the case in the United States, but Europe is also offering more and more storage capacity. The global market for these facilities is expected to double between 2021 and 2028, rising from $206.2bn to $404.9bn. French investment in telecoms networks has increased by 75% between 2021 and 2022 to reach €3.7bn, making it the second most dynamic sector after renewable energy. Digital infrastructures are also benefiting from public incentives such as the Connecting Europe Facility programme and its $33.7bn investment in digital infrastructures between 2021 and 2027. One billion of this is earmarked for the development of fibre and 5G.

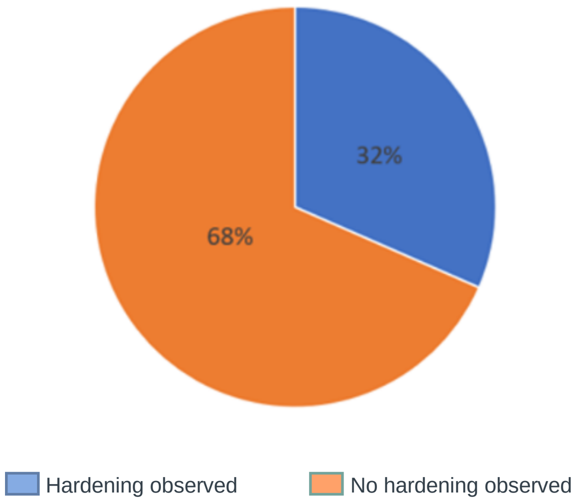
In terms of valuation, multiples remain elevated, albeit slightly lower. Sought-after assets such as data centres and telecoms towers are still trading at 20x to 25x EBITDA, while renewable energies are trading at around 20x, according to Conatus Finance. Again, the effect of rising interest rates is clearly playing a role, as investors seek a return slightly above than the risk-free rate, which automatically leads funds to be more disciplined in their investment policies.

Performance

A successful sector despite a troubled economic climate

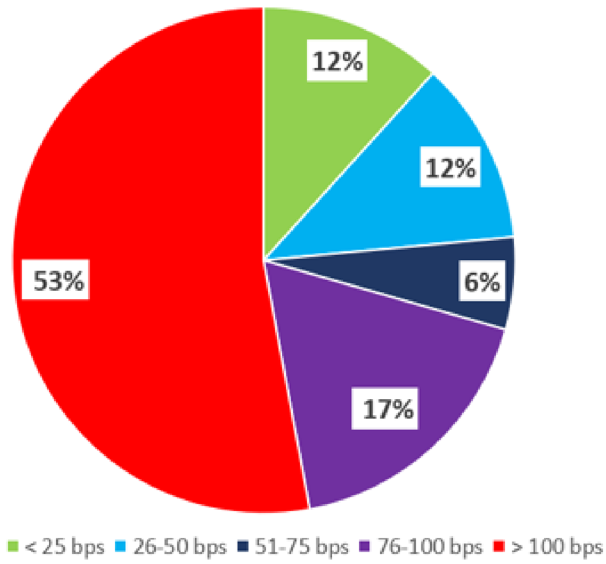
The resurgence of inflation has boosted the performance of the assets in the portfolio, as costs are largely fixed (interest charges on fixed-rate debt), while income is in line with price increases. The funds already invested should therefore, on average, generate significant outperformance compared with the IRR targets originally set. Moreover, the increase in interest rates has not, in most cases, led to a tightening of borrowing conditions, as most lenders do not require additional banking covenants over and above the usual terms and conditions.

Tougher covenants demanded by creditors



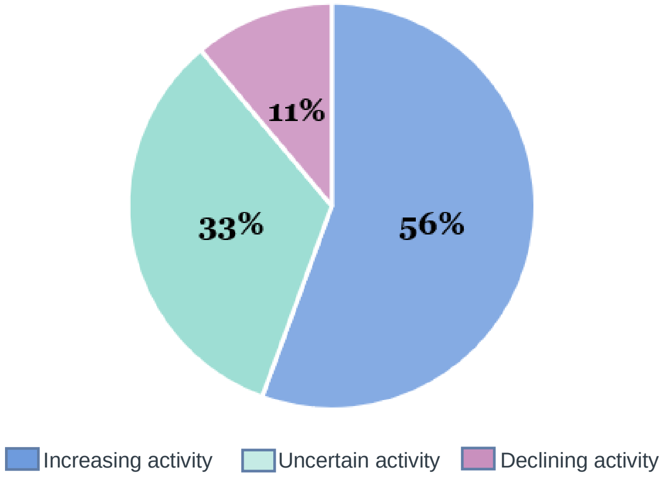
The increase in rates was not uniform across the curve, with long rates rising more slowly than short rates. The maturities most affected by the increase were those of one to three years and three to five years, which rose by around 300 bp in € (400 bp in $).

Average spread increase



Perspectives

Observed trends and outlook for 2023
(Source: Bird&Bird survey - CFNews INFRA)



The slowdown in inflows observed since H2 2022 continued in H1 2023, although it remains relatively contained compared to other unlisted asset classes. Investment needs, the need to "green" managers' portfolios and the attractive risk profile of infrastructure remain strong medium-term drivers. In addition, the infrastructure asset class appears to be relatively immune to inflation, although this hypothesis remains to be tested (particularly in the context of PPPs and regulated assets, whose revenues are in principle index-linked, but which may also be subject to discretionary decisions by public authorities or to the temptation to amend contracts, as the current debate on motorway concessions demonstrates).

After peaking at 25x EBITDA in the renewable energy sector, valuations are now returning to levels more in line with investor's return requirements. Recent transactions in the sector (acquisitions of Reden Solar by Macquarie, Photosol by Rubis, etc.), even if the amounts of the transactions are not always public, suggest multiples of 17/18x EBITDA, which would allow a reasonable margin to be maintained in relation to the current cost of debt and continue to channel investment into this crucial sector to meet the challenge of global warming. A market recovery could therefore lead to capital losses on some historic investments over the next few half-years.

In 2023, a number of notable deals will be highlighted, demonstrating the vitality of the sector. In addition, Caisse des Dépôts, Vauban Infrastructures Partners acquired Coriance, one of France's leaders in heating networks. The deal was worth no less than €1.6bn. This move is part of the megatrend of the energy transition and, more specifically, decarbonisation, for which this sector is crucial. Antin Infrastructure Partners is also consolidating its position with the acquisition of the Spanish company Opdenergy. This listed producer and supplier of renewable energies (solar, wind, storage) has joined the group in a deal worth €866m, at a 46% premium to its last recorded price. This is the second investment made by the flagship V d'Antin fund, following the acquisition of Germany's Blue Elephant Energy in 2022. In France, the market is also expecting a major transaction in the second half of the year, with the sale of Akuo Energy to an infra-french or international fund.

Lastly, the launch of a new fund dedicated to rare metals, considered "critical" to the success of the energy transition has been entrusted to Infravia, at the instigation of the government, which will contribute €500m, i.e., a quarter of its target size by 2025. This sub-segment is supported by the France 2030 plan, which provides for major public investment[6]. The fund will invest in the extraction, transformation and recycling of these strategic components. It thus marks the consolidation of a relatively new investment universe, reinforced by the arrival of a new leader in a wider context of regional re-industrialisation and the recovery of sovereignty in an increasingly threatening geopolitical environment.

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[6] https://www.economie.gouv.fr/france-2030#

Overall, favourable trends are emerging for infrastructure, based on its own merits as a useful, resilient and high-performance asset class. In addition to this unique status, there are several positive factors, such as the reallocation of funds and the gradual arrival of new investors through retail networks, particularly in the life insurance portfolios of individual investors.

Over the coming half-year, the ability of portfolio assets to perform regardless of inflation and interest rate levels will be a real stress test for investors' view of the sector. Legal certainty and respect for the rule of law remain central to investment decisions, particularly in regulated sectors. The attractiveness of the asset class, which is a prerequisite for financing the significant investment needs of the energy and digital transitions, will largely depend on the stability of the contractual and regulatory framework.

Thank you

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