Keynote Address - Michaela Sved, Director, MVision

A lot of capital has been raised for infrastructure in 2013, but with a record number of funds on the road, fundraising is increasingly competitive. How can infrastructure managers stand out from the crowd?

2013 was another strong year for fundraising, though we are still a long way from the peak. When it comes to distinguishing yourself from the crowd, top of the list is realized returns – are there any realizations which demonstrate that the manager is on track to meet the stated target returns? The infrastructure sector is nascent; funds have long lives, so we have not seen many funds complete a full cycle of investments and realizations. In that situation, investors focus on yield as a performance measure – are there strong distributions in line with what the fund originally promised?

In circumstances where the fund is not yet distributing capital, investor due diligence may involve drilling down into individual asset performance. As well as requesting historical performance information, we are seeing greater reliance on reference calls with portfolio company CEOs. LPs are looking for a relatively independent view of the prospects for the asset. They also use reference calls as an opportunity to investigate how much value the infrastructure manager is adding to the asset. Management continue to be a hot topic for LPs, so they want to hear that their managers are actively driving value at portfolio assets. Qualitative factors, such as sticking to investment strategy, low team turnover and transparency around valuations and portfolio performance are other criteria investors look to.

It is critical to create momentum in a fundraise to get LPs to process the fund. The market is highly competitive so investors have a lot of options. Even though infrastructure is becoming an established asset class in its own right, often the person dealing with infrastructure is the same person who covers the private equity portfolio, so they have a lot of competing opportunities in front of them at one time.

A strong and imminent pipeline will encourage LPs to review a fund as they will not want to miss out on investment opportunities. Once you have assembled a core group of LPs for a first close, you can create even more excitement in the LP community by deploying capital for your first investments. Having that first deal shows proof of strategy and gives potential LPs an opportunity to go on site and due diligence the asset. We have found that a strong first deal completely changes the pace of the fundraise.

A pipeline of co-investment opportunities is an attractive incentive for LPs as they look to reduce fees and deepen their relationship with GPs. But we are still finding that a lot of LPs do not take up their rights. GPs spend time and effort to negotiate co-investment terms as part of LPs' commitments to the fund, but often find that when it comes to the crunch, the LPs do not have the time capacity to commit to due diligencing a co-investment.

Investors are increasingly looking for managers with strong track records. Is it getting harder for first-time fund managers to raise capital?

It is often challenging for first-time managers to raise capital – many LPs have a policy of not reviewing first-time funds. However, a first-time manager with a clean slate and a compelling investment thesis may in fact have an easier time raising capital than a manager raising a second fund with no realizations and performance issues at the asset level. A number of managers who raised their first funds in 2006/7 are in this position.

There are a few factors that drive the success of first-time funds. Firstly, has the team worked together before? It makes a difference if the team have spun out of a firm or have a history doing deals together, as there is a team track record they can point to. It is a much more challenging proposition marketing a fund which is a group of people who are working together for the first time.

As we already discussed, creating momentum through a pipeline of imminent transactions is key for getting LPs to process. Same goes for first-time funds, but it is even more important in the case of a new fund as it alleviates blind pool risk and enables investors to confirm, through due diligence, that the asset matches the stated strategy. We often tell first-time managers who come to us to for advice to raise capital from friends and family and deploy it in a couple of deals before going out to the broader market. That way investors have an asset or two to due diligence.

Securing a first close is critical. It demonstrates that the fund is going to happen. To the extent that you can get some institutional investors into a first close (as well as capital from family and friends) the manager will be even better positioned as those institutional investors often serve as references to the investor community. Investors willing to back a first-time fund are often a tight group, and once you are able to tap into one of those investors, they are often willing to introduce you to their 'friends' in the investor community who they think will support you.

Are there particular regions or sectors that are attracting particular investor interest at the moment?

The majority of investors considering infrastructure are still looking to add core developed markets managers. With increasing competition for infrastructure in core developed markets, from more funds and LPs going direct, asset prices are being aggressively bid. In some cases we are seeing single digit returns, so it is hard to understand how those managers are going to achieve their core infrastructure target returns. A few years ago core was low double digits, and I think a lot of LPs have revised their expectations to assume they will receive single digit returns from core managers. Though it is interesting that most core managers continue to promise double digit returns.

Investors have started to recognize that core asset returns do not necessarily compensate for the associated risk. The utility sector in the UK is a prime example – every time you open the paper there is a new debate on energy pricing and this political debate is now impacting asset returns.

As a result, we are seeing a strategic shift for LPs who have traditionally focused on core infrastructure directs in developed markets – this group is now looking to enhance and protect returns in response to the increasing competitiveness of the core infrastructure space and the resulting impact on returns. They are doing this either through moving into core plus infrastructure investments, or even through investing in emerging markets infrastructure.

In emerging markets we are seeing LPs that you would traditionally consider direct investors committing capital to funds so they are able to access local deal opportunities. They do not have the on-the-ground sourcing capabilities that they have in Europe/North America, so they look to partner with local managers to get their foot in the door. Often they due diligence fund commitments to those GPs by working alongside them on a direct investment opportunity first.

Do most investors now see infrastructure as a distinct asset class, and are you seeing more create dedicated allocations to the asset class?

In general investors have an appreciation for the role infrastructure plays in a diversified portfolio, and they continue to create separate buckets for infrastructure investments. There is strong interest in the asset class as it is seen as a way to reduce risk across the portfolios and hedge against inflation.

We have seen a big growth in the number of infrastructure debt funds being launched this year. Is this trend likely to continue in 2014, and where does infrastructure debt sit within institutional investors' portfolios?

Given where core infrastructure returns are going, debt fund returns are starting to look relatively attractive! The space is highly competitive, with a lot of new, unproven entrants. We are seeing those with track records raise capital much more successfully, and also have greater success in deploying capital. I am surprised how few deals have been done given the amount of capital that has been raised so far.

How do you decide which infrastructure managers you work with?

We have a pretty similar process to investors when it comes to due diligencing established funds. I would say that we have a very different process compared to our peers. Of course performance, track record, distributions, whether the fund has stuck to investment strategy etc. are some of the key criteria we look for when it comes to choosing infrastructure managers. Understanding the status of existing investors and the deal pipeline is also very important to us given they are such key drivers for the first close.

As well as processing performance data we take a very strategic approach when it comes to reviewing which managers we work with. Our role is to help our clients establish a long-term business, not just fund sales. When it comes to first-time funds, which make up about half our fund portfolio, we get very involved early on in developing their strategy and building their brand. Often we work with them for over 12 months before we commence drafting any materials or talking to investors. We often take a strategic role with established managers also, and have had particular success in resolving performance or succession issues, for example, so that we deliver a successful fundraising outcome for our clients.

Thank you for your time.

Founded in 2001, MVision is widely recognized as one of the world's leading independent international advisory firms, focusing on raising capital for Private Equity, Real Estate, Real Assets, Credit and Direct transactions in both the developed and emerging markets.

MVision has a long-standing reputation for working with winners - the firm's clients are current and future market leaders across the globe. MVision firmly believes that fund-raising is far more than a one-time event; it continues to assist clients with the on-going task of funding and growing their businesses effectively, managing issues such as positioning, growth and performance.

The MVision team of over 50 professionals provides a global service to clients covering institutional investors worldwide. Together the team represents 17 nationalities, speak 20 languages and operates out of offices in London, New York, Hong Kong and Sydney. The depth of the team's expertise across all areas of the market allows their clients privileged access to the strategic industry insights vital to achieving success.

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