

Roundtable

Asset management

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Future-proofing assets

At a time of great political and technological upheaval, infrastructure fund managers are ever more pressured to plan for both threatening developments and promising trends. Five industry luminaries tell **Matthieu Favas** how they go about it

In the world of ride-hailing apps, we have yet to find out who is going to have the last laugh. Taxis were first displaced by private cabs, which then suffered when Uber arrived. But the latter could soon be displaced by the rise of driverless cars – or it may thrive by successfully embracing their arrival.

This kind of swift, wide-ranging disruption also impacts those who pilot infrastructure assets and sometimes own them for decades. Sure, infrastructure assets are big pieces of kit, essential and concrete. But for long-term investors in car parks, toll roads and airports, this reasoning is no longer enough. As asset managers will tell you themselves, the monopolies they

hunt for are becoming an increasingly rare species.

What is not changing are the capabilities needed to keep afloat in the quicksand. “Excellent project management is a skill that will never go out of fashion,” says Valeria Rosati, an executive director at Hastings Funds Management. As we scan through the various issues making



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asset management an ever more crucial part of investors' businesses, her words ring true: confronting rapid change requires meticulous attention to detail and a great deal of anticipation.

It starts long before the acquisition target becomes part of a portfolio. As managers ponder on whether to take part in a deal, they need to approach the problem by asking the right questions.

“Our fund targets long-term, core infrastructure assets. For us, it's less about immediately looking to add value or coming up with a significant growth plan; it's much more about reducing volatility and protecting the downside. That said, I don't think any manager these days can just sit back and clip coupons – strong governance and oversight is critical and as an owner you have to expect to be actively involved,” says Graeme Dunbar, an investment director at SL Capital Partners.

Mark Crosbie, a managing partner at Antin Infrastructure Partners, has another view. “We are not different from an

AROUND THE TABLE



Juan Angoitia, managing director, Ardian

Based in Madrid, Angoitia joined Ardian in 2013. He previously worked five years at Citi Infrastructure Investors as investment principal, based in London, after spending a decade at Ferrovial.



Mark Chladek, transaction director, Infracapital

Chladek joined Infracapital when it was founded in 2005. He has 17 years' experience across infrastructure M&A, project finance, investment and financial markets.



Mark Crosbie, managing partner, Antin Infrastructure Partners

Crosbie joined Antin at its outset in 2007. He was previously with UK utility Centrica, where he spent eight years, after senior stints at UBS and Peregrine Investment Holdings in Hong Kong.



Graeme Dunbar, investment director, SL Capital Partners

Dunbar joined SL Capital in 2008 after 10 years at KPMG in the UK and Australia, latterly as a manager in corporate finance acting as lead advisor on a variety of M&A and private equity transactions.



Valeria Rosati, executive director, Hastings Funds Management

Rosati joined Hastings in May 2006. Her previous experience includes advising on transactions, particularly in the infrastructure sector, at Gleacher Shacklock, Merrill Lynch and Lehman Brothers.



“In the early days, we were perhaps too kind and let it go [on] a little bit longer than [it] perhaps should have, but we’ve learnt a lot since” **Crosbie**

industrial player: we would look to invest in assets where we can create significant value. We need to get a clear view of what we’ll do with the business when buying it. In some cases we acquire businesses from large corporates that were constrained in their growth. Perhaps the owners did not see the value we saw.”

For Mark Chladek, a transaction director at Infracapital, this mindset is all the more justified as the appetite for plain-vanilla, “plug-and-play” infrastructure assets has boomed in recent years. That is prompting managers to look at various ways to develop a business. “We have significant operational expertise within our team. So we’re actively looking at opportunities where we can utilise this, in particular where there is potential for organic growth, contract wins, add-on acquisitions or operational efficiencies.”

Any red lines? Rosati sees two major ones. “We wouldn’t invest in very mature PPP-type assets if mostly, at the acquisition

stage, you can only win by taking part in a cost-of-capital shootout. We also look at the underlying risks of the assets to answer the question: is it infrastructure? As the asset class’s definition is continuing to evolve, getting the answer right requires a lot of scenario testing.”

Her point is echoed by Juan Angoitia, a managing director at Ardian. A major criteria for investing, he says, is the degree of alignment that exists between his firm and its potential co-investment partners. “If you talk to an industrial player, they know what they want to do with the assets. At Ardian, we also do the same and have a clear strategy for the investment. You need to make sure you are on the same page with your partner. The red line starts when assets stop being essential infrastructure: greenfield, brownfield or yellowfield, they need to be essential and non-discretionary.”

THE 100-DAY PLAN

Once a deal is complete, fund managers quickly move to put their plan in action. And beyond figures and processes, much will come down to people.

“In the period that follows closing a transaction, there is a migration of focus from the transaction team to the asset management team taking the business forward. The key to our 100-day plan is about setting everything up for long-term ownership covering areas such as management, business plan, due diligence items, governance and reporting. It’s essential to address these early so that down the line they don’t turn into distractions,” says Chladek.

Yet redirecting resources towards managing portfolio companies – and ensuring assets are watertight when it comes to the basics – is only a pre-condition to a smooth transition. Of equal significance are the people who are going to be directly at the helm of the company and their fit with the demands and culture of its new owners. “It’s a marriage”, as Angoitia puts it, and it can go both ways. “The senior

management team has to feel that the new shareholders want to change tack, that there is a new push, a new energy in the company, accompanied by a willingness to do things.”

It is hard to overstate the responsibility of those in charge of implementing this new strategy, especially in times of swift and unpredictable change.

“Often one of the greatest challenges is having the discipline and timeliness to decide when a management team, despite having been in place for a long time, is no longer equipped to face the internal and external pressures associated with today’s environment. And then you have to manage senior staff exits carefully, if there are some, and find a replacement that has a different experience and potential,” Rosati says.

If managing recruitment is one side of the coin, then having the right incentive schemes in place is the other, Chladek adds. On both aspects, time is of the essence. “If you’re going to make management changes because you think the existing team is not up to the task you’d better do it quickly. In the early days, we were perhaps too kind and let it go [on] a little bit longer than [it] perhaps should have, but we’ve learnt a lot since. We’re focused on that from day one,” agrees Crosbie.

DEALING WITH DISRUPTION

But being prepared does not mean everything can be anticipated. Many a company deemed previously sound has been rocked by the arrival of new technologies and business models: think Kodak, Barnes and Noble or Adison Lee. And while it has taken some time, disruption is starting to make waves in the infrastructure industry.

Of course, not every asset is the same: some segments of the market look better protected. “We buy core infrastructure assets which are slightly lower risk with good visibility on the cashflows. But you can never be complacent. During the due diligence we try and pick the most appropriate advisors and ask the right questions,

but you spend three to six months diligencing assets, then you can spend 10-plus years owning them. In that amount of time lots of things can change so the market and business drivers require constant monitoring and having the right range of knowledge and skills on the board and within the management team is critical,” notes Dunbar.

For Rosati, the trend is at an inflexion point. “Much more than before we spend time and money trying to understand the risks posed by changing technologies. Things like driverless cars or artificial intelligence, for example.”

Angoitia underlines that different types of assets have different levels of exposure. CLH, a Spanish oil storage business Ardian owns, has no retail dimension. In this sense, changes it will have to embrace have more to do with plant automation or running a connected business.

The situation is different for customer-facing businesses. What is the impact of Bla Bla Car – a ride-sharing company – on

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toll road revenues, he asks? “It is this sort of trend that you have to anticipate. If you react while it happens, it’s already too late.”

Obviously, new technologies can turn into opportunities in the infrastructure world as well. Infracapital exploited this trend when it invested in Calvin Capital, a smart metering business. That required investment and the development of proprietary systems, Chladek points out. “We had to track a portfolio of over six million meters and data quality was very important to the business and its customers. Having the right IT and reporting tools in place is essential to monitor asset performance.” Similarly, he underlines the potential of fibre-optics, which he says has now emerged as a “new public utility”.

Establishing partnerships can also be useful to stay ahead of the curve. Crosbie explains that Antin has set up programmes with a top-ranking university in Europe and a US counterpart to focus on disruptive technologies, both of which

have produced “very insightful things”, he says. “It’s good to get some fresh thinking, a different perspective.”

THE WORRYING WIDE WEB

Sometimes disruption can mean outright danger. In recent years, a worrying number of large companies have fallen prey to cyberattacks and there is no reason to think that infrastructure assets are operating in a bubble.

The trouble, as Dunbar describes it, is that IT threats are especially hard to understand for the uninitiated. “You know they exist, but it’s hard to know where they’re coming from. Unlike a lot of business risks that you can sensibly get your head around, cyber is a different kind of threat that is constantly evolving and requires very specialist knowledge and expertise to ensure you are protected [as far as possible].”

Chladek concurs, suggesting that cybersecurity is now a “board-level item”, where “it’s got to be completely clear who

is accountable and responsible for it”.

This explains why some operators spend a great deal of money erecting barriers against potential intrusions or attacks. “Most of the companies we invest in are large [and] as a result they have resources that can be dedicated to this. We monitor this at individual company and portfolio level. Our businesses typically have cybersecurity assessments, external system penetration testing and we also work with different industry bodies and government agencies to exchange best practice and understand trends,” Rosati says.

Value-add investors like Antin must also deal with similar considerations: what happens if CATS, a gas pipeline that transported 13 percent of the UK’s gas production in 2013, suddenly gets jammed? “For assets that have got those type of characteristics you tend to have by necessity a heightened IT security network,” Crosbie says.

To broaden its thinking on such issues,



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Antin a couple of years ago created an IT directors’ club that meets every quarter to share best practices. The last edition of 2016 was focused on cybersecurity; the firm had invited a former top hacker – now in charge of protecting Belgium’s nuclear plants – to put the IT directors of its portfolio companies to the test. “Everyone learnt a lot,” Crosbie notes.

NO EXCUSES

Closely tied with such existential issues are considerations related to accountability – still a grey area for fund managers, in some cases. “When you’re dealing with an asset like CLH, which handles the storage and transportation of refined oil products in Spain and holds the strategic oil reserves of a number of EU countries, you have to coordinate with the department of defence, intelligence services, everybody. Sometimes even at the board level we don’t know what is happening. Agencies can’t disclose some information to management because it is linked to

national security,” recalls Angoitia. Rosati thinks the legal answer to this question matters, but is somewhat beside the point. “The problem of accountability is a problem of reputation, at the end of the day. Ultimately, as a board director or shareholder, you are accountable because there is a reputational impact, even when a decision is classified. You can’t divorce yourself from it.”

Where excuses will no longer work either is in the field of environmental, social and governance issues. The topic is well documented, but our participants are keen to underline that investor demands in the field are getting ever more formal and institutionalised. “LPs are increasingly aware of ESG and it is an issue that has grown significantly in importance. Not just that, but these issues are among the things LPs now expect feedback on routinely. How you report on what you’re doing at the portfolio level to cover this aspect of asset management is essential,” says Dunbar.

“Investors want to be made aware of how these issues are being addressed, rather than just assuming they are, as was often the case in the past.”

As this increasingly complex web of demands lands on fund managers’ desks, what upcoming trends should they be looking out for?

Angoitia says politics may become an even more relevant factor. “Five years ago everybody was speaking of integrated networks, with the eventual objective, perhaps, to have a European-wide network for everything. I don’t know what’s going to happen in the future. [With] elections in France and the Netherlands, Brexit, there are developments that could have an impact on the best way to build toll roads, oil and gas networks and things like that.”

As Chladek concludes: “A lot of political outcomes are out of our hands or that of our businesses. This is why risk management will continue to be at the heart of what asset management is about.” ■