

# Institutional investors in PPP projects

'Locusts' or providers of added value?

Private equity investors in the infrastructure market have come under some public scrutiny with the perception that investors are acting like 'locusts' that move into a field, eat it to the ground, and move on to the next without looking back. This profile, after a brief market review, will put some of these criticisms to rest and show that it is no longer a 'locust' style playing field, but a field in which the contribution of the institutional investor to the development of PPP is becoming increasingly important.

## The market trend

The total worldwide PPP volume in 2005 amounted to €32.7bn with a five year growth rate of 24% pa (and nearly 18% pa in the Americas). Alone in 2006 and the first half of 2007, more than €26bn was committed to infrastructure funds. This can be explained by the apparent pipeline of opportunities that lay ahead, and the expectations that, with a 'reasonable' risk profile, steady and attractive returns can be generated.

Although quite impressive, it is important to look at these numbers in terms of infrastructure definition, region, asset type (primary vs. secondary), recent market turbulence, as well as investment horizon. Factoring all, it can be argued that the corresponding project volume to the capital that has been allocated is mismatched – with available capital by far exceeding the investment opportunities as timeframes can take longer than expected.

From another angle, even if the full impact of the sub prime market disruption is still not known, it may turn out to be a healthy development to correct the partially blurred risk return relation that we see in the pricing of assets, including PPP.

In any case there is some certainty that the first tier of mature markets led by Europe,

Australia and Canada will generate a decent project pipeline in the short term.

## Aligned interests with the public sector

As of today, only a limited number of funds have been established with durations in excess of 20 years, providing a long-term solution for public clients whilst providing a solution to the problem of the long financing of pensions and other social liabilities through stable and sustainable private equity investments in PPP infrastructure projects. That will translate into assets not only to be built at competitive prices, but to be amply operated and maintained throughout the project life. It is the long-term investor who shares this objective of investing throughout the life of the asset. Returns for these investors will be generated when most of the industrial sponsors have walked away from the project. This is one reason why we see, in particular in Australia, consortia led by financial investors rather than by industrial sponsors.

## Social responsibility

A further trend with institutional investors is the willingness to demonstrate social responsibility in relation to environmental, internal and external policy, as well as economic policy. This translates into such actions as implementing strategic partnering boards, involving the local community, ensuring corporate governance, and improving human resource conditions.

The approach of the investor that is involved from the development throughout the operations under the umbrella of social responsibility aligns with the public sector objective of receiving value for money. The days where the investors tried to have limited and short-term involvement aiming to maximise profits have, at least for the PPP market, passed.

## More beneficiaries

It is not only the public sector ultimately benefiting; the private equity investors see themselves more and more as both a provider of capital, and also a developer achieving the objectives above. In doing so, the following consequences have surfaced for institutional investors: sharing the high development costs of PPP schemes; providing technical, operational, financial, legal and project management expertise; establishment of a risk management process from day one; taking majority shares in a consortium/concession company – helping industrial sponsors who face consolidation constraints, as well as allowing them to recycle their capital more effectively.

## Meridiam Infrastructure Fund

Meridiam is a €600m PPP long-term investment fund investing mainly in Europe, the US and Canada with a duration of 25 years. Meridiam would put itself in the category of the long-term investor described above. Coming back to the initial question – whereas sheep are around in every industry, not all of them are black and mutate into locusts.



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