

KEYNOTE INTERVIEW

Lessons from a decade in infrastructure



*Transparency, discipline and diversification are key, says
Wim Blaasse, managing partner at DIF Capital Partners*

Q What changes have you witnessed in the size and shape of the infrastructure industry?

So much has changed since we started DIF in 2005. Back then, infrastructure was a new asset class and many institutional investors were not even aware of what infrastructure projects looked like or the potential returns the asset class might generate. That has changed, and very quickly. Infrastructure today is a large and mature market with a lot of capital flowing in.

In this low-interest-rate environment, everybody is looking for yield and, in terms of risk-adjusted returns, infrastructure is one of the most attractive asset classes. In that context, the rate of growth is unsurprising and we have seen the emergence of some real mega players. Even mid-market firms like DIF, which started out raising €100 million vehicles, are now raising funds of €2 billion-plus.

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Q How have investment parameters evolved alongside this growth and what lessons have been learned about balancing opportunism with the need to avoid strategy drift?

The definition of infrastructure has certainly expanded. We are seeing investments happening that would never have been considered as infrastructure 10 years ago. Take the Australian land registry deals: infrastructure players have gone after these services and their related cashflows, although there are no hard assets involved.

DIF's own investment remit has also evolved and expanded. Initially, our firm focused almost exclusively on public-private partnerships, which was a big market be-

tween 2005 and 2010. But that market gradually changed and, while those deals are still important to us, they are only part of the opportunities we look at. Similarly, DIF also used to have a dedicated fund for renewables, but this has become part of a broader fund mandate over time. And three years ago, we launched a new strategy, targeting slightly higher-risk investments in the telecom, transportation and energy sectors.

It is important to stay focused and understand where the firm fits within the broader landscape. DIF, for example, has never touched the private equity end of infrastructure. Another key lesson we learned is that markets change over time and adjusting to change is critical, otherwise you can end up with no deals and you are out of business. Only 10 years ago, a PPP-only fund might have worked well, but as we have seen in the UK, those opportunities can dry up quickly.

Managers also need to observe what



Becalmed: onshore wind forecasts failed to deliver on projections

developments are taking place in the market and adjust to those in a considered and careful way, not leap into doing something completely different – that is where strategy drift comes in and that is something investors do not like. The other important lesson is transparency. Always be open with limited partners: a manager that explains why it needs to respond to changing circumstances will find its investors understand.

Q Are there specific examples of sectors where infrastructure players failed to heed a change in market conditions on time?

A prime example is the onshore wind projects developed in Western Europe between 2007 and 2009, and which were completed immediately before, or in the early stages of, the global financial crisis. Those projects were based on the wind forecasts of the previous 25 years, but they failed to deliver on projections because wind levels fell. A lot of parties across the industry suffered disappointing wind production as a result.

That is why DIF decided not to make further investments in wind projects in 2010. As the picture is a lot clearer and forecasts are more conservative nowadays, we are making wind investments again, although primarily in North America and Australia.

“We are seeing investments happening that would never have been considered as infrastructure 10 years ago”

Q You talked about transparency. What about when things go wrong? What lessons have been learned there?

Transparency is absolutely key in those circumstances. In 2018, DIF experienced a difficult situation where a serious incident took place. We informed investors immediately and were completely transparent throughout on the steps we were taking to rectify the issue. Investors still tell us how much they appreciated that approach. Even though a tragedy was involved, which had a negative impact on the valuation of a single asset, investors valued our openness. That has been an important confirmation of our approach and apparently not so normal.

Our firm works hard to encourage that ethos of transparency within our organisation. It is not only about being transparent with investors but within the whole team. Within DIF you won't be blamed for failure. Everybody makes mistakes. But you should always proactively inform senior management. We shouldn't find out about it by ourselves.

Q Infrastructure is a fairly young asset class which has not yet been through multiple cycles. With another downturn potentially on the cards, are there any specific lessons learned from the financial crisis?

Some regulatory changes linked to the financial crisis have had a real impact, specifically the retroactive changes to solar subsidies in Italy and Spain. That caused a wave of uncertainty and made investors question whether they wanted to commit to sectors that relied on regulatory support. So the fallout from the financial crisis alerted investors to the risks in areas vulnerable to changes made by politicians.

Investing in sectors that society considers essential can help reduce the impact of a recession, should one happen. DIF, for example, currently has Spanish assets like transportation hubs and hospitals in its portfolio. A government cannot afford to close down a hospital or abandon a transport route if times get tough. But it can afford to pull support for a solar project because, frankly,



Dealing with the unpredictable

Q The asset class has experienced a handful of major failures, most recently with Carillion in the UK. What lessons can the industry take from what happened there?

Infrastructure investors must recognise that the unforeseeable sometimes happens. Nobody predicted that a company the size of Carillion could end up in bankruptcy so quickly. Fortunately, DIF had only one project involving Carillion, but that was still in the construction phase. Although it was a relatively small investment – just €5 million – it still took us almost 18 months to fully restructure the asset and get it back on track.

The big lesson here is diversification. DIF has between 25 and 30 assets in each fund portfolio and to minimise risk we make sure they are well spread across geography and sector. The unpredictable can happen, and managers need to make sure that in the event of the worst-case scenario actually occurring it is not going to blow up the fund.

who cares if a solar project is no longer operational in the midst of financial turmoil?

Q What important lessons have been learned about investment in your own organisation and team?

DIF has nine different offices, which is significantly more than most general partners of our size, so investing in communication is key. It is critical to travel to the different offices on a regular basis and to talk to the origination teams and the asset-management teams, and make sure everyone is pulling in the same direction.

Team stability at the manager level is incredibly important to investors, so investing in your team is critical for staff retention. DIF organises an annual offsite where we discuss strategy and work through business cases, but also do sports and teambuilding activities together. It is essential to maintain a coherent

culture and to pay attention to the softer factors, alongside financial remuneration.

We work hard to make sure all teams across the business are integrated and that everyone's interests are aligned. We also have a broad partnership – we currently have 14 partners – and that means younger staff can see the potential to grow into a partner role. That provides incentivisation. It also means that success is shared, it encourages collaboration and it avoids self-interest. As a result, DIF has had no senior staff leaving in the past decade.

Q How important nowadays are environmental, social and governance credentials across the industry? What can go wrong if they are not in place?

ESG is of far more significance for managers now. Discussions around health and safe-

ty, for example, are far higher up the board agenda than they were in the past. However, sometimes ESG best practice is not always followed through, so action needs to be quickly taken to rectify situations.

But lessons can be learned from this too. For example, DIF had one project under construction where a particular manager failed to follow the procedures in place and there were construction workers smoking weed on site, with all the safety risks involved. Immediate measures were taken. The rules that govern ESG must be adhered to at all times.

Q What lessons have been learned regarding hands-on asset management more generally?

Hands-on asset management is critical. It is not only about generating higher returns but also preserving value. If you have more than 150 assets across various funds, as DIF does, there will always be projects that require added focus to ensure, for example, that construction remains on budget. It is about structuring the transactions correctly at the outset, making sure the right contracts are in place with the right counterparties, and then actively managing those contracts to make sure you get what you are paying for. Investing and then just leaning back can lead to some nasty surprises.

Q Summarise the biggest lessons you have learned at DIF over the past 10 years

Transparency has been the number one lesson. A manager is in difficult territory if their investors do not trust them. The other two key lessons are the importance of diversification of the portfolio and discipline: a manager needs to carry out what they have committed to do.

There are many exciting investment opportunities in the market, so managers must continually ask themselves if a specific opportunity fits with a fund's remit and what is expected of the firm. If a manager feels they cannot explain a deal to investors, then they are most likely better off not proceeding with it. ■

Wim Blaasse has been managing partner of DIF Capital Partners since the firm was founded in 2005. He was a partner at PricewaterhouseCoopers responsible for infrastructure/PPP and energy-related transactions. He was also head of project finance at Rabobank International