



## Infrastructure Newsletter

Issue I

October 10, 2008



Dear PCA Client,

The infrastructure sector remains an attractive asset class within the market. We believe these challenging economic times will test global infrastructure to ensure that the cash flows related to investments remain stable and predictable. Given infrastructure's low correlation to more traditional asset classes, infrastructure assets should continue to provide low volatility within portfolios.

### ***Effects of the Credit Crisis – New Market Opportunities?***

Certainly the credit crisis has had an impact on the infrastructure market. Whereas some previous infrastructure investments carried high leverage levels, which were refinanced at some point to provide investors with dividends, capital structures are now more conservative. The financial engineering we previously witnessed is no longer feasible in the marketplace. As such, we expect transaction prices and multiples to contract somewhat in the near future. This will provide opportunities for investment managers to acquire assets at more reasonable valuations.

In some ways the existing credit crisis has widened the landscape of opportunity within the infrastructure sector. As more states and municipalities experience budget and funding problems, they may look to infrastructure as an alternative means of generating funds. "Facing a recession, (New York) Gov. David A. Paterson's administration said on [September 28, 2008] that it would set up a commission to explore ways to privatize public assets, including the lottery system and bridges like the Tappan Zee. Administration officials said that the governor was not seeking to plug holes in the budget by selling off the state's assets. Still, any money raised could be used to make capital investments that the state otherwise would be unable to make in a financial downturn." New York Times, September 30, 2008.

Unfortunately with the recession-like environment, slumping housing market and challenging credit cycle, New York is not the only state that is experiencing budget problems as a result of the turbulent markets. In early October California Governor Arnold Schwarzenegger forewarned that if the state could not borrow funds from the public credit markets that it would be forced to go to the federal government and ask for up to \$7 billion



of assistance. With credit frozen, it was estimated that California had enough cash reserves to last until October 28<sup>th</sup>.

States are certainly considering all financing options and infrastructure assets are being evaluated even more closely now that states are suffering from substantial budget deficits. Infrastructure investment activity continues as transactions such as the leasing of the Midway Airport in Chicago was announced in early October. The Chicago City Council approved a \$2.5 billion deal to lease Midway Airport to a group of private investors led by Citi Infrastructure Partners and one of its portfolio companies Vancouver Airport Services. This concession marks the privatization of the first large airport in the United States. In addition, the City of Chicago is looking to privatize its lottery while the State of Florida is actively pursuing public-private partnerships for its transportation assets including roadways, tunnels and ports.

However, not all states are completely comfortable with public-private partnerships. Recently, the Pennsylvania legislators failed to ratify the proposed toll-road lease pertaining to the 537-mile Pennsylvania Turnpike. Consequently, some of the partners in the consortium to lease the turnpike pulled the \$12.8 billion bid for the asset and let the cash offer to buy the asset expire.

***PCA encourages clients to continue to do their homework when evaluating infrastructure opportunities. Be cautious and diligent and take your time to fully explore the activity in this sector.***

### ***Infrastructure Fund Pricing – Pension Plans Are Being Heard***

PCA pension plan clients have been vocal about the disconnect between infrastructure returns and the private equity-like fees that have been associated with many infrastructure funds. Many pension plans are looking to infrastructure for modest yet stable returns while infrastructure fund fees have been modeled with a 2% management fee and 20% carry structure. As investment funds have been more aggressive in targeting pension plan investors, they are beginning to listen to plan sponsor concerns. PCA is observing that fees for infrastructure funds are coming down and investment managers are more willing to construct more creative fee structures based on varying commitment levels.

### ***Federal Infrastructure Regulation – Is It Coming Soon?***

Within the United States there is no federal regulation pertaining to infrastructure. In addition, within Washington D.C. there are very few groups that are focused on the developments of infrastructure and there is no organized voice for infrastructure. While the presidential candidates have both recognized there is an infrastructure need within the U.S., it is still unclear as to how this country's dire infrastructure needs will be addressed in the near term. Tyler Duvall, Acting Under Secretary for Policy and Assistant Secretary for Transportation Policy, commented at a recent conference that currently there is a growing momentum pertaining to infrastructure activity within the U.S. He and others are trying to establish federal regulations which would demonstrate a high-level commitment to this asset class. PCA hopes that this effort will also address the education and marketing of infrastructure to the public. Stay tuned!



## **PCA Infrastructure Newsletter**

### **Recent Infrastructure Articles**

#### **New State Panel to Study Privatizing Public Assets** **September 30, 2008**

Subject: New York State Governor Paterson to set up a commission to explore ways to privatize public assets.

**Link:**

**[http://www.nytimes.com/2008/10/01/nyregion/01privatize.html?\\_r=1&ei=5070&emc=eta1&oref=slogin](http://www.nytimes.com/2008/10/01/nyregion/01privatize.html?_r=1&ei=5070&emc=eta1&oref=slogin)**

#### **Midway Deal Likely to Cost Fliers** **October 1, 2008**

**Subject:** The Chicago City Council has approved a \$2.5 billion deal to lease Midway Airport to a group of private investors.

**Link:** **<http://www.chicagotribune.com/news/local/chi-midway-01-oct01,0,5816543.story>**

#### **Abertis Lets Bid Expire for Pennsylvania Turnpike** **October 1, 2008**

Subject: Spain's Abertis Infraestructuras SA decided to pull its \$12.8 billion bid for the Pennsylvania Turnpike off the table, dealing a blow to the most ambitious privatization project in the U.S. infrastructure sector, a spokesman for Pennsylvania Gov. Ed Rendell confirmed.

**Link:** **<http://online.wsj.com/article/SB122281758238892323.html>**

#### **California Hopes Washington Brings Credit Relief** **October 4, 2008**

Subject: Bond Offering of \$7 Billion Will Now Go Forward, But Emergency Federal Loan to Pay Teachers and Police May Be Necessary

**Link:** **<http://online.wsj.com/article/SB122305751973202869.html>**



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