PHOTOGRAPHY: ANTHONY JEONG

Keynote

David Ridley,
Westbourne Capital

Lessons from a decade in infra debt

Westbourne Capital was one of the first pure-play infrastructure-debt managers when it was founded by a trio of former Hastings executives. On its 10th anniversary, founder and managing director David Ridley talks to **Daniel Kemp** about increasing competition, LP appetite and what the future holds

When David Ridley left Hastings Funds Management to start Westbourne Capital in 2008, he wouldn't have expected that competition from his old firm would cease to exist within 10 years. He was confident, of course, that his involvement with Hastings would stand him in good stead to compete – but not that he would outlast his venerable former employer.

"Westbourne was really set up with the learnings and experience of the senior team's time at Hastings and also was an extension of pioneering the infrastructure debt asset class there," Ridley tells *Infrastructure Investor*, as we meet on the eve of his company's first decade in business. "It is sad to see what's happened to them – it was a good business."

Ridley established and led the alternative debt business at Hastings before making the leap to start Westbourne, where he's also a managing director. He took Hastings' investment director Li-Yu Loh and associate director Nathan Taylor with him to become Westbourne's head of client relationships and head of asset management, respectively – and all three remain in those roles today.

That three-person executive team has since grown to 16, with offices in Melbourne and London, deploying $6.7 billion into 63 debt investments across Europe, North America and Australia.

A PERFECT BIRTHDAY GIFT

We sit down in the boardroom of Westbourne's Melbourne office, with black-and-white images of various infrastructure assets on the walls, both inside this room and out in the lobby. The office isn't huge and has a professional but relaxed atmosphere – staff walked past amused while Ridley had his photograph taken for this interview.

This culture, with continuity in the business's leadership since day one, has been crucial to Westbourne's success, Ridley says. The firm is still majority-owned by its executive team, which Ridley says creates a "strong alignment" with institutional clients. Japanese investment giant Mitsui & Co became a 20 percent shareholder in 2015, but he says he wouldn't expect to see any "substantial change" in ownership any time soon.

That strong alignment has paid off handsomely, with Ridley clearly pleased to reveal that Westbourne has reached a first close on its new fundraising platform – a perfect birthday present for the firm's leadership team. Westbourne is aiming to raise $3 billion in the current round and Ridley says the firm has secured commitments totalling $1.5 billion so far.

"Our priority has been to work with our existing LPs to make re-ups or new commitments now that the capital they've previously provided has been invested," he says. "And we also anticipate raising some commitments from LPs who are new to the Westbourne platform. We're in reasonably progressed discus-

sions with a series of pension and sovereign wealth funds to be able to execute that over the coming months."

Its existing sovereign wealth clients include Australia's Future Fund and the National Pension Service of Korea, while pension clients include Qantas Superannuation Fund, Mercer, LGIA Super, HESTA and First State Super.

The firm aims to complete fundraising by the end of 2018, with capital to be deployed over the subsequent three years. That's similar to what Westbourne has done before, even if that might be a little slower than other managers.

"We've historically been pretty conservative around deployment pace. Obviously, it's a consideration for institutional investors, but at the same time we want to invest those funds wisely and sensibly, and so three years is the guidance that we provide," Ridley says.

Around 45 percent of the capital committed to date for this fundraising has come from pension funds, 40 percent from sovereign wealth funds, and 15 percent from insurers, with the latter becoming more active in the infrastructure-debt space, Ridley says. On the divide between overseas and domestic Australian investors, the split is 70-30 in favour of foreign capital.

"Insurance companies are seeking to replace lower-returning government bonds for their fixed-income portfolios with an asset class that they feel comfortable lending into for a sufficiently long period that it will add value to their liability-management programme," Ridley says. "So, I think there's just going to be a growing demand from those insurance-company-type investors as we go further."

Deployment will target opportunities consistent with Westbourne's past activity, focusing on the transport, utilities, energy and telecommunications sectors in OECD countries. Ridley anticipates that increased market volatility will provide more secondary-market opportunities, though he insists his firm is "agnostic" on whether opportunities come from the primary or secondary side.

"To date, we've invested about 70 percent of our capital in primary-market transactions and about 30 percent in the secondary market. Our experience has been that, in periods of credit-market volatility and any periods of dislocation, there will be an increased opportunity set becoming available in the secondary market," he says.

"If we look back to when the Westbourne programme commenced in 2010, we still had some of the residual dislocation from the global financial crisis – and since that time we've had several periods of market volatility, including the European sovereign-debt crisis and the volatility caused by the energy markets in 2015-16.

"In each of these periods, we've been able to access additional investments in the secondary market. From our perspective, while we don't require it in terms of executing our investment strategy, we expect to continue to see periods of volatility going forward."

> We've historically been pretty conservative around deployment pace"

GOING BIG

The story then, as far as Ridley is concerned, is one of continuity, and of ongoing relationships with a growing number of LPs that are gradually leading to a bigger footprint for Westbourne in the infrastructure-debt space that it has done a great deal to grow.

"We're really seeking to make six to 10 investments over a three-year investment period with the current fundraise," Ridley says. Thus, despite increased competition compared with when Westbourne started out in 2008, particularly in the subordinated-debt sector, the addressable market is still big enough for the firm and its competitors to do the deals they need to.

"For example, over the past 18 months, we've made 20 infrastructure-debt investments, which would represent invested capital in excess of $2 billion. A number of those are in the subordinated-debt sector and five of those have been for investment amounts, in terms of Westbourne's position, of $200 million or more," he says. "Our strategy has been to act as either the cornerstone lender, or the sole lender, which we have been in a number of those situations. Going forward, we will really try to increase the size of each investment we're making, rather than significantly increasing the number of investments we make."

That potentially means investments in the range of $200 million to $300 million in future, with the flexibility to go larger or smaller as the situation requires.

A decade ago, the institutional infrastructure debt market was still in its infancy and Ridley says the early years of Westbourne required his team to educate many of their clients on what was then a new asset class.

"Many of our institutional clients had very active infrastructure equity programmes, so there was a very good understanding of the asset class and its characteristics. But I guess the challenge was to include a debt component in their investment programme. And clearly there's been a set of institutional investors who are new to the asset class [altogether], so there's been a lot of education," he says.

Appetite from LPs for the asset class remains "relatively healthy", Ridley says, a slightly more qualified response than you might expect from someone in his position. But he explains this by saying pension and sovereign-wealth investors now weigh up infrastructure debt on a "risk-reward" basis, as they've gained a stronger understanding of the asset class, highlighting that subordinated debt is particularly attractive to defined-contribution pension clients who are actively seeking returns. Around 90 percent of Australian superannuation funds fall into this category, as opposed to defined benefit.

THE SENIOR/SUBORDINATED DIVIDE

On subordinated debt, despite more players entering the space in recent years, Ridley says there is "significantly less competition" here than on senior investment-grade debt. "There is really only a small group of investment managers with the scale and the experienced investment teams that can execute in the subordinated debt sector," he says.

So, have returns in subordinated debt started to compress yet?

"Interestingly, we haven't seen that.

"One observation I'd make is that, to some degree, the institutional loan markets on the subordinated side compete with high-yield bond markets. Not all borrowers can, or want, to go to those high-yield markets – but when they are aggressively pricing transactions, then borrowers may seek to tap them in preference to the institutional-loan market, which would command a higher return for the same instrument relative to the public bond markets," he says.

High-yield bond market spreads are just starting to widen now after a long period of contraction, he points out. "That's indicative of our sense that the returns that we're seeking are going to continue to be available in the markets in which we're investing," he says.

Ridley reveals he's heard anecdotally that Westbourne's clients who also run equity programmes are seeing returns there and in subordinated debt converging, thanks to increased competition in the equity market and the low-interest-rate environment.

And with less risk in the debt sector, subordinated debt investments are becoming more attractive. "I don't see subordinated infrastructure debt replacing infrastructure equity, but I see it as a complementary asset class for those that are investing in the infrastructure equity market," he says.

Westbourne has seen more investment opportunities recently, though, where subordinated debt investors are being asked to take on more equity-style risks, he adds. "This indicates to us that, to some degree, we're in the later stage of the credit cycle."

On the senior debt side, Ridley says Westbourne sees increasing competition, both from other investment managers and institutional investors acting directly. But, he adds, the infrastructure asset class is "very significant", so there is still enough room for everyone to play a role.

OPPORTUNITIES AHEAD

Ridley is optimistic about the next 10 years for Westbourne Capital and anticipates the asset class will continue to grow, with an increase in financing options to keep pace.

"There's certainly room for more investment managers in the space. We're fortunate to have been one of the early players, post the GFC environment, so we've built up a good reputation," he says.

He highlights the changing global energy market environment as an opportunity, with the build-out of renewables continuing to provide deals on both the senior and subordinated debt sides.

"The other interesting trend is the growing pressure on regulated entities," Ridley says. "It's a combination of regulators seeking to tighten the economics under which regulated companies operate, coupled with low interest rates which is feeding into a lower cost of capital for those entities.

"We see there will be a need in some regulated sectors for additional loan financing to better reset some of those companies' capital structures to deal with the impacts of tight regulation." The UK water sector is at front-of-mind here, as it is set to undergo historically low costs of capital during its next regulatory period.

The interview ends on an intriguing note. Ridley is proud of Westbourne's status as a pure-play infrastructure debt investor, with no equity or advisory businesses that could potentially lead to conflicts of interest – a point he returns to multiple times.

"When we established Westbourne, we felt that the infrastructure debt sector was an emerging asset class, not as developed as the infrastructure equity class. And we felt there had been some reservations about conflicts of interest, so there was an opportunity to have a pure-play infrastructure debt business. And we felt that could have a long-term role in the industry," he says.

But when asked to look ahead, he doesn't definitively rule out the possibility of ever changing tack. "I think we'll always be focused on infrastructure debt," he says. "Or I should say – our skill set is in the infrastructure debt space, so we'd anticipate that it will continue to be our focus."

After a successful first 10 years, it will be interesting to see what the next decade holds for Westbourne Capital. ■

Westbourne at a glance

LITTLE DRY POWDER

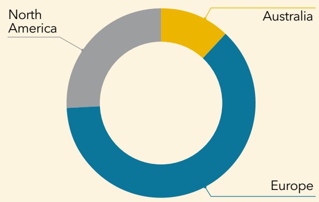
Westbourne has invested practically all of the money it's raised

$8bn
Capital raised to date from more than 40 LPs

$6.7bn
Capital deployed to date into 63 debt investments

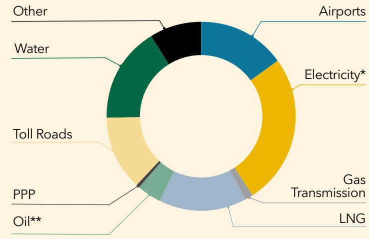
EUROPE RULES

The Old Continent has accounted for more than 60% of Westbourne's investments



POWERHOUSE

Electricity has received the lion's share of the manager's loans



Source: Westbourne Capital

*Includes generation, distribution & transmission
**Includes transmission & services