3Q20 Europe League Tables: Signs of recovery amidst the downturn

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While there are clear winners and losers from the crisis, the COVID-19-fueled downturn for the sector could have been worse, while for some green shoots of recovery beckon. Stefano Berra and Antonio Fabrizio report

Cracks are starting to show in the European infrastructure and energy market. While the first half of 2020 closed in line with 2019, investment levels faltered over the past three months, as the ripple effects of COVID-19 began to be felt more acutely.

Infrastructure and energy deal volume across the continent fell by 10% year-on-year to USD 142bn for the first nine months of the year, compared with USD 158bn at the same time in 2019, according to *Inframation*'s Q3 league tables.

Deal numbers were also down by more than 20%, with 586 transactions closed so far this year compared with 740 in 2019.

This year's winners and losers are also emerging more clearly, as some sectors enjoy record activity while others are in a deep crisis.

A slowdown in the transport market was the main reason for the lower figures. Traffic rebound after the end to the initial coronavirus lockdowns was slow, and uncertainty over long-term prospects remains high. Just USD 5.3bn of transport deals closed in Q3, the lowest quarterly data in more than eight years. Deal volumes are down 45% year-on-year so far this year.

Dealmaking in the airport sector is in freefall, as airport owners across the continent see their investments increasingly at risk and restructure their operations with heavy job cuts. This time last year, airports accounted for nearly a third of all European transport deal volumes, but they represent just 8% of the transport market so far this year – with just EUR 1.9bn of deals closed.

Airports crisis grounds transport market

Little M&A in the sector appears to be on the cards. The sale of Prestwick Airport in Scotland to a Macquarie-backed buyer was pulled and there is no sign that big privatisations such as those of Paris airport operator ADP or Athens Airport will restart soon. Major European airport operators are scaling back investment. Some governments in Eastern Europe, including Ukraine, are preparing the ground for new concessions, but these deals are at early stages.

The EUR 660m bond refinancing of Atlantia-backed Nice airport in July was the largest European airport financing in Q3. It was driven out of necessity – to push forward debt maturities – and the owners had to pay relatively high margins to be able to do so, one source on the deal admits.

Other airport deals were also linked to similar issues. Liverpool Airport's shareholders, including Ancala Partners, had to step in to provide loans to help refinance its maturing GBP 75m debts.

More airport groups continued to tap banks and bond investors as they urgently searched for liquidity. Further airport deal flow likely to come in over the last months of the year is likely to be from restructurings, infrastructure bankers say.

Roads were also hit hard by lockdowns. Traffic bounced back more quickly and so did investor interest, but deal volumes are still about a quarter of 2019 levels.

Ardian increased its exposure to Italian toll road operator ASTM in September, after three infrastructure funds bought up stakes in the A28 Alis toll road in France from Abertis at the end of June – suggesting some investors are hopeful of a recovery. DIF also upped its stake in two availability-based roads in Portugal last month.

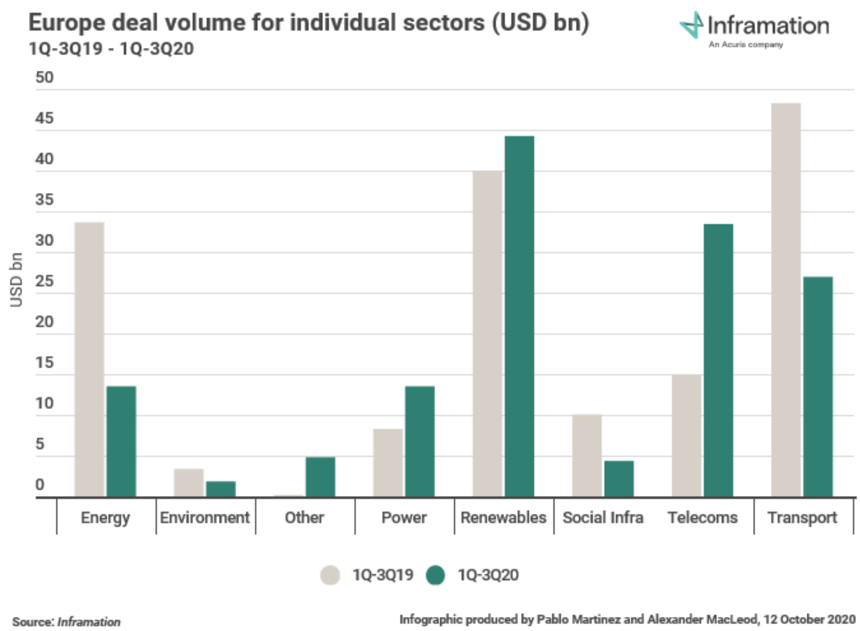
Ongoing road M&A deals are faring relatively well, with the sale of ACS-backed Baixo Alentejo motorway attracting six bidders in the final phase despite carrying some traffic risk. And the upcoming closing of APG's Brisa takeover should boost numbers in Q4.

For greenfield roads, the German market was a bright spot. Strabag and Meridiam closed in August the USD 1.2bn A49 motorway PPP in Hessen, one of the largest PPPs of the year. The project was the second major PPP closed in the country since the coronavirus outbreak, after the USD 1.67bn A3.

Both deals were shielded from traffic risk but John Philip Weiland, head of banking at Kommunalkredit, which advised the A49's consortium, says it was still challenging to close the deal "in a short time window during the summer break in a market environment which had significantly changed" due to COVID-19.

But the Netherlands, a PPP stalwart, saw no greenfield transport PPP closing for the first time in eight years. The country's only ongoing road PPP – the Via15 – is bogged down in legal proceedings.

Procurement of other projects is slowly advancing. The A456 road PPP in the UK was awarded in the summer and is set to close, while in the Czech Republic, the long-delayed D4 motorway is set to reach preferred bidder stage, while some slow progress is also being made in Norway on the EUR 1bn Sotra connection road PPP.



Even though commuter trains remain half-empty, rolling stock is growing in importance. Rolling stock deals accounted for just 5% of transport deal volumes in the first nine months of 2018, growing to 18% over the same time last year and 28% so far in 2020.

"The Covid crisis has had an impact on us like on the whole economy, but the long-term trend for rail is good," says a senior rail industry source. "We need more zero-emission transport."

But there are mixed signals in the UK, where some in the rolling stock sector welcomed the government's move to replace the franchise system with direct intervention in September, others fret about the future. In France, infrastructure investors are eyeing the country's first private-sector passenger contracts, while Germany marches on with large-scale deals to modernise its train fleet, including major debt raises approaching in Munich and Berlin.

Ports are suffering from a drop in global trade, and deal value is down nearly 20% this year.

But infrastructure investors are taking notice of opportunities in the crisis, with deals agreed in Q3 including CDPQ's extra USD 4.5bn investment in its global joint venture with DP World, and DIF's more modest acquisition of a stake in a Spanish container terminal alongside shipping line CMA CGM. Port deals account for 12% of the transport market so far this year, up from 8% in 2019.

But while Europe is travelling less, it is striving to become more connected and greener.

Telecoms and renewables gaining ground

The telecoms market continued its seemingly unstoppable march in Q3. The value of telecoms infrastructure deals closed so far this year - about EUR 30bn - is already nearly three times higher than last year. Investment in telecoms infrastructure now represent almost a quarter of the total European infrastructure and energy market, compared with just 9% in Q3 2019.

The list of transactions is long. In Q3, Eir closed the sale of its towers to Blackstone-backed Phoenix Tower, InfraVia completed the sale of its Welsh data centre business NGD to Vantage Data Centres, and Alinda Capital Partners invested in UK fibre operator Glide, to name a few.

Many more deals were struck in the fibre market, with some yet to close. Antin agreed to sell a minority stake in Eurofiber to PGGM, Asterion agreed its first Italian deal in the sector, and a UBS AM unit committed to invest in French group Altitude Infrastructure. AMP Capital also bought a majority stake in a specialist Swedish broadband group, and Warburg Pincus moved to take control of London-focused Community Fibre.

On a larger scale, Macquarie, 3i and AustralianSuper entered exclusive talks to buy the European telecom assets of US group GTT Communications for USD 2.15bn. And in early October, Polhem Infra said it will buy Swedish giant Telia's international fibre network for EUR 900m.

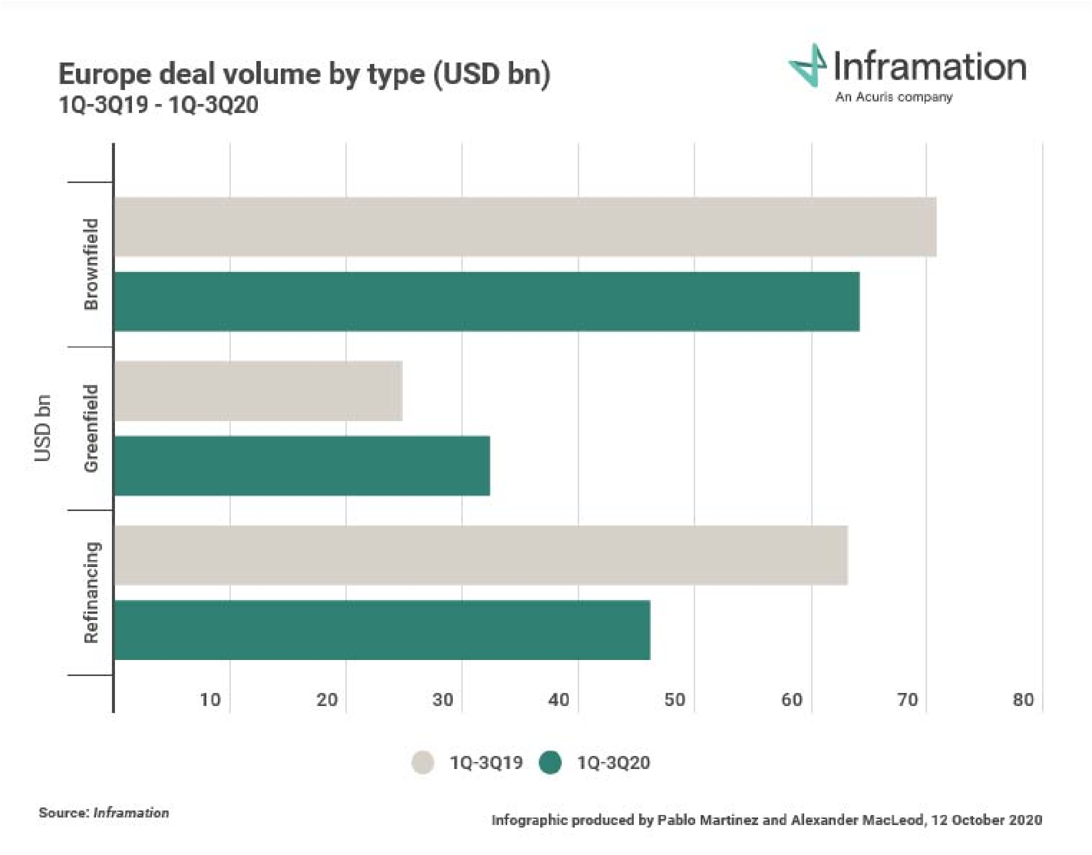
Even larger telecoms behemoth acquisitions lie around the corner. Orange resumed the sale of a stake in its EUR 2.5bn French fibre business, and Telefonica is set to pick investors and lenders to roll out a fibre network in Germany worth at least EUR 3bn. To say nothing of Italy's fibre saga, with Macquarie and KKR Infrastructure poised to invest in wholesale operator Open Fiber and in TIM's network, which may be merged into a company with a whopping EUR 15bn enterprise value.

Another sector on the rise is the renewables market. In the first nine months of 2020, renewables deal volumes (USD 44bn) were above the previous three-year average even though the number of deals closed was lower, indicating that the market is moving towards larger deals.

This is borne out by the growing importance of larger offshore wind deals – now accounting for almost 40% of all renewables deals, up from 27% in the past two years. One of the largest deals struck so far in 2020 is the financing and stake sale of the GBP 3bn 1 GW Seagreen 1 project, set to become Scotland's largest offshore wind farm.

More offshore wind M&A is on the cards. Orsted is selling a stake in the 752 MW Borssele I & II wind farm and Vattenfall could offload part of its shares in the Hollandse Kust Zuid wind park in the Netherlands, while Equinor and SSE are in the final rounds of selling a stake in the monster 2.4 GW Dogger Bank A & B project in the UK.

The sale of energy-from-waste group Viridor to KKR Infrastructure for GBP 3.7bn closed in July, also boosting this year's renewables figures. It is set to be followed by the separate sales of Macquarie's and SSE's stakes in EfW assets of Wheelabrator Technologies later this year.



Ups and downs in energy and social

But a mixed picture emerges in other markets, including social infrastructure, where deal volumes are less than half of those recorded last year, partly due to a halving of greenfield investment.

But within the sector, more money is flowing into healthcare (about EUR 2bn closed so far), which now accounts for half of social infrastructure investment, up from just 25% last year.

Among recently-agreed healthcare M&A deals, EQT Infrastructure partnered with CDPQ to buy French care home business Colisee, while DWS agreed to buy an F2i-backed diagnostics business in Italy, and Antin Infrastructure sold French psychiatric clinic company Inicea.

Some of the dealflow is also linked to restructurings, however, chiefly of Turkish hospital PPPs. One of the first - for the Etlik hospital - has closed and others are set to follow, according to sources.

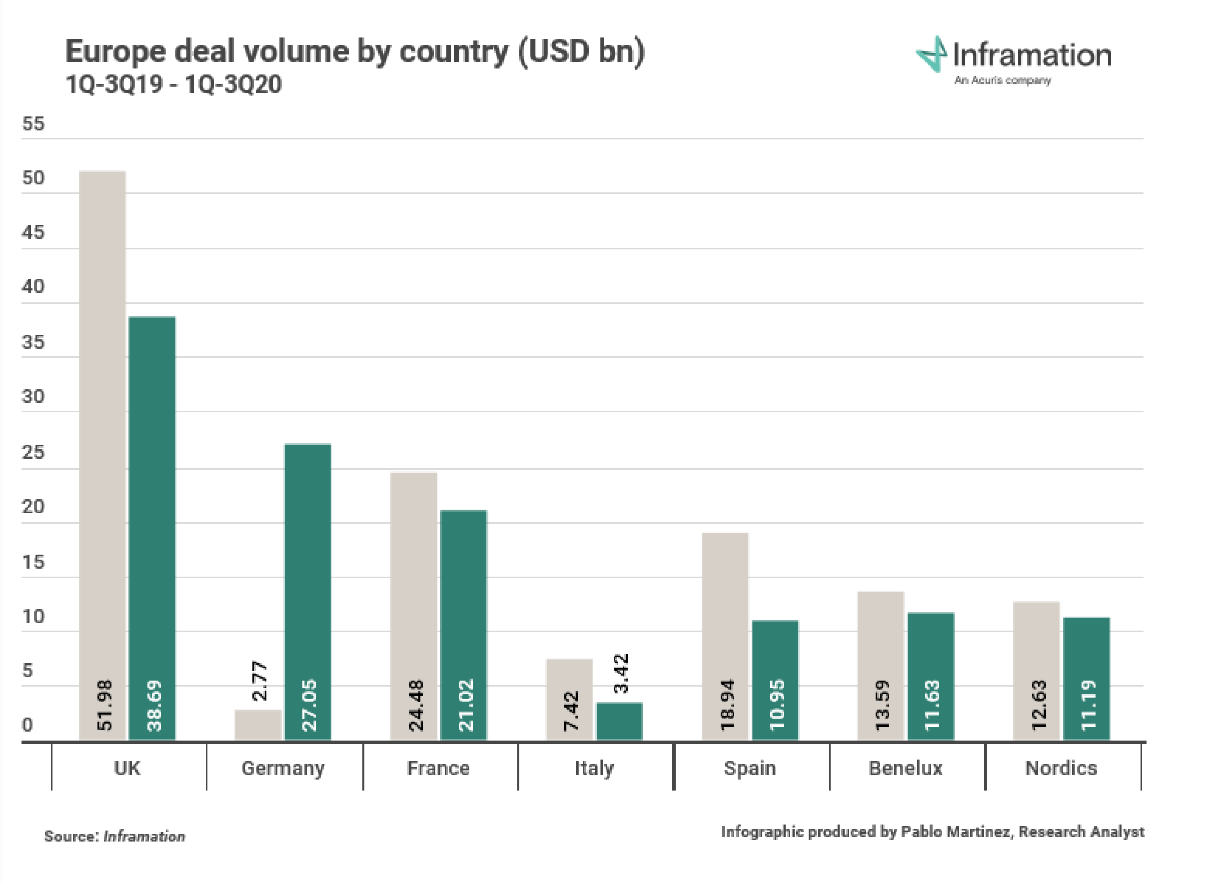
The energy and power markets are also experiencing some ups and downs.

The district heating sector is remaining reliably busy on the back of strong activity in Scandinavia. More than EUR 2.4bn of deals have closed so far and valuations are rising comfortably above 20x, indicating growing interest from buyers. In some cases, they jumped above 30x, with an Infranode-backed team paying 34x to buy a Finnish network from Fortum this quarter. More deals are set to close, such as JP Morgan Asset Management's acquisition of heating group Adven, estimated to have an equity value above EUR 1bn.

On the other hand, far fewer gas transportation and distribution M&A and financing deals closed this year compared to 2019 (down 60%). The next few months could see a reversal of this trend, however, with big-ticket sales coming up. Galp's sale of its Portuguese gas network is in its final phases. The privatisation of Greece's gas distribution company DEPA Infrastructure is progressing, albeit slowly, and First State Investments, now renamed First Sentier, is putting its German gas company Ferngas on the block. Uniper is also selling a stake in German gas pipeline Opal.

Electricity distribution and transmission deals continue to account for two-thirds of the power sector, a stable market share over the past three years. Orsted closed the USD 3.4bn sale of its Radius power grid in August and M&A prospects are brightened by the ongoing sale of UK electricity grid company Western Power Distribution (WPD), which has a GBP 8bn regulated asset value.

There has been strong activity in smart meters (representing 17% of total power deals so far this year) across a variety of transactions – from IPOs and refinancing (Calisen) to M&A (Mapleco). More money from infrastructure investors and lenders is also flowing into the expanding electric vehicle value chain. The first-of-its-kind structured financing for an electric battery Gigafactory – Northvolt Ett in Sweden – was closed in July.



Capital raising and consolidation

Despite the uncertain backdrop, infrastructure fund managers continue to eye bigger funds. EQT recently set its fifth flagship infrastructure fund's hard cap at EUR 15bn, while KKR is targeting over USD 12bn for its fourth global vehicle. Renewables-focused Copenhagen Infrastructure Partners is also scaling up and could reach EUR 7bn for its latest vehicle after reaching second close in September.

But some are also tracing back their steps – Antin is preparing a new middle-market fund after reaching EUR 6.5bn for its latest flagship fund.

Among infrastructure corporates, there are signs that consolidation is afoot. French environmental giant Veolia's bid to take over its water and waste competitor Suez is perhaps the clearest sign of this trend. But other big deals are in the making, including Vinci's bid to take over EUR 5bn worth of concessions and industrial business from fellow construction heavyweight ACS.

The renewables market is also ripe for consolidation as small renewables developers are being gobbled up by big energy groups. German solar groups IB Vogt and BayWa are on the block, while RWE took over Nordex's European wind development platform in July.

On the debt side, banks have seen the European infrastructure loan market shrink by 17% so far this year as the number and size of refinancings remained subdued in Q3 after a fall documented in the H1 league tables.

But infrastructure lenders have weathered the COVID-19 crisis much better than the global financial crisis, managing to keep debt funding flowing. They are being helped by regulators. One senior infrastructure banker said the European Commission is expected to introduce measures known as "infrastructure supporting factor" in Q4 to reduce capital requirements for infrastructure and energy lending, which will enable banks to price loans more cheaply.

The Q3 lending league tables continued to see the top three French banks and Santander as the four largest lenders, with the Spanish bank replacing Societe Generale at the top of the tables. All four increased the amount they lent year-on-year.

The loan market held up better than capital market financing, which has shrunk by a third so far this year. But change is afoot here too, with plenty of new infrastructure debt funds being raised that will soon look for a home for their capital.

Swiss Life AM and HSBC AM are among the latest to enter the sector, launching platforms seeking to raise EUR 1.5bn and USD 1.5bn, respectively. Others have stepped up their debt fund offerings, including DIF. Junior debt is also finding new champions, including UBS AM, which launched its first high-yield infrastructure debt fund in the last quarter.