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Context for Private Capital Investment

TRANSCRIPT

Energy Open-Ended Funds on the Horizon
With Nadia Sager of Latham & Watkins

Nadia Sager, Latham & Watkins:

I think the real question is "Are open-ended funds the next frontier in energy and infrastructure?" They certainly are in real estate. We have seen an increase in the popularity of the open-ended fund vehicle as a tool for fundraising for real estate fund managers. We haven't seen as much of that in the energy and infrastructure space. I believe the open-ended fund could be the next wave in energy and infrastructure and presents a really attractive opportunity for fund managers to take development assets once they've stabilized and become cash-flowing assets that they like and would like to hold on a long-term basis and put those in vehicles that they can continue to manage and control.

Privcap: **What are the attributes necessary for an open-ended vehicle to be successfully structured?**

Sager: Those do need to be long-term hold assets that cash flow. It really doesn't work to use an open-ended fund structure with something that doesn't generate a cash flow, because you need to be able to offer your investors liquidity and it's always the important question as to how you're going to manage that liquidity.

What specific types of energy assets would work well in an open-ended format?

Sager: Certainly, once you've got a power plant that's operational and is cash flowing, that's a great asset for an open-ended fund. You could think about critical infrastructure that generates ongoing cash flows. There's all sorts of things—pipelines as well—that really are assets and can be very attractive in an open-ended fund in long-term hold assets.

Might open-ended funds be used as an exit route for private equity firms?

Sager: An open-ended fund is a great exit route for private equity firms to use for their closed-end vehicles. In fact, you do see firms doing that in the real estate space, where they have a fund whose mission was to develop assets or to buy and aggregate assets. Once they've gotten those assets into the value-creation stage where they are a stabilized, cash-flowing asset, they then move them into their own managed open-ended fund vehicle so they can move them from one part of the complex to another part that that sponsor manages.

Are these funds generally more accommodating to smaller investors?

Sager: In the real estate world, where you see a number of open-ended funds now, they do tend to take smaller investments from a large number of retail investors and you have to be set up to manage that many investors. You can very successfully take in a wide variety of investors into your open-ended vehicle and really open up part of the market that you might not be fundraising in today with your closed-end funds.

How does liquidity work in these funds?

Sager: There are a whole variety of ways that you can set up your liquidity for an open-ended fund. You can start with an initial lock-up period of, say, one or two years. Usually, there's some sort of a lock-up for those coming in of a short or medium duration. Then, you can have quarterly or annual exits or, in some cases, you set up exit windows every four or five years. There are really a variety of ways to set that up.