Hamilton Lane

2022 Real Assets Market Oveview

# Fundraising and Investment Highlights in Real Assets

**July 2022** | Pete Larsen, Managing Director, Real Assets

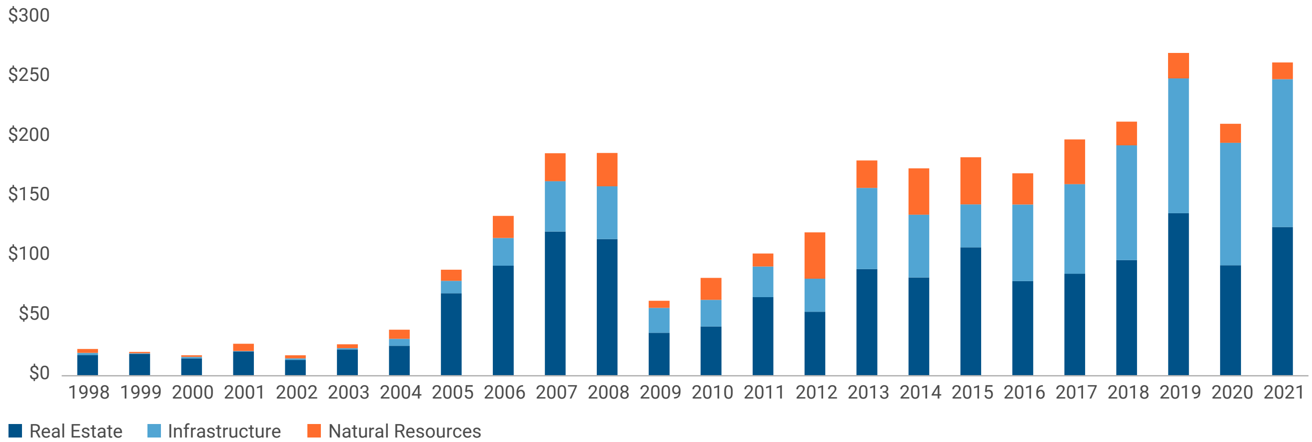
## Fundraising is like a box of…ice cream?

### Let's talk ice cream! Given his druthers, my father would eat ice cream for three meals a day.  I'm no different, although modern science and pesky things like lipid panels suggest this is ill advised.  But I digress…

Why ice cream?  Well, if you know us you know we love an analogy. And in searching for something to appropriately and simultaneously capture the three distinctly different dynamics of real estate, infrastructure and natural resources, I landed on ice cream. Or more specifically, Neapolitan ice cream.  Before the days of fancy Ben & Jerry's  flavors sold in pints, Neapolitan by the gallon box was a freezer staple.  But there was only one problem – strawberry.  Tucked neatly alongside the other two flavors, strawberry was usually in much lower demand and consumed even more slowly.

Seem like a stretch? Indulge me: Fundraising and investor activity in real assets is like that gallon of Neapolitan.  Three distinctly different dynamics are dominating the landscape.  Looking at real assets exposure between 1999 and 2021, we see substantial growth in real assets overall as a percentage of investors' portfolios.  In fact, it's grown by 25.3% annually, outpaced only by growth in private credit.  But since the Global Financial Crisis, and even more so in recent years, different patterns have emerged among the three sub-asset classes.  And sorry, natural resources, as far as fundraising is concerned, at least for now, you're strawberry.

**Closed-End Fund Fundraising by Strategy**
USD in Billions




Source: Hamilton Lane data via Cobalt as of September 30, 2021, for all sectors through 2016 and natural resources through 2021; PERE and Inframation data for real estate and infrastructure, respectively, from 2017 to 2021 Note: 2021 natural resources data represents an annualized figure using Q3 Hamilton Lane data via Cobalt

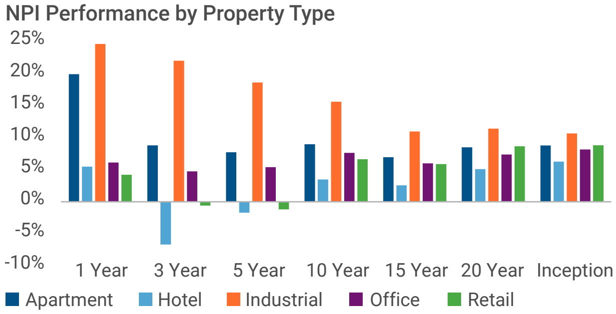
Let's look more closely at the dynamics:

## Real Estate: Vanilla

Looking at real estate, it continues to attract capital and is in relatively steady demand. A bit like vanilla – always there, always consumed, but its audience isn't necessarily expanding by leaps and bounds. It continues to push forward, with relatively few changes in the fundraising landscape.

One trend that we do see, however, is more and more specialist funds being raised to focus on specific markets and/or property types. This has been driven by investor desire to take a more active role in weighting their real estate allocations, no doubt being influenced by the increasing dispersion of returns between property types. As shown, in more recent periods, both multifamily and industrial have shown outperformance relative to other property types.

**NPI Performance by Property Type**

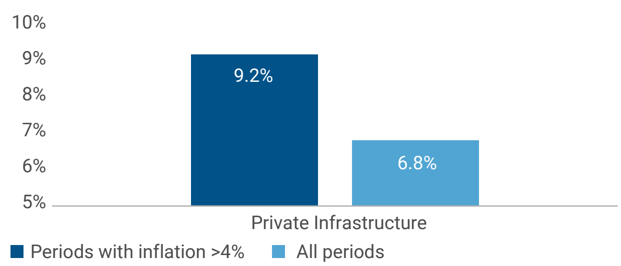



Source: NCREIF as of December 31, 2021

## Infrastructure: Chocolate

Infrastructure, by contrast, has been growing steadily. In 1999, infrastructure comprised only about 1% of private markets portfolios. By 2021, this had grown almost eight-fold (or "octupled" as we like to say). Part of this interest, particularly in more recent quarters, has been the desire for investors to seek both an inflation hedge and potential downside protection in a volatile market. As shown, infrastructure tends to outperform during periods where inflation is above 4%.

**Average Performance During Periods of Elevated Inflation (>4%)**
1999 - TTM Q3 2021




Source: Hamilton Lane Data via Cobalt as of September 30, 2021

### Emergence of Middle Market Infrastructure

But while the amount of capital raised in the asset class has increased more quickly than other types of real assets, the actual number of funds in market has returned to levels last seen around 2015. Huh?

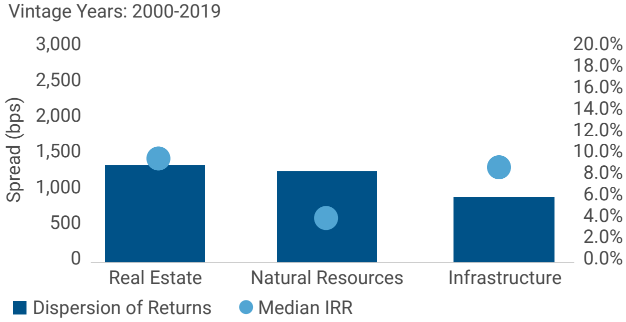
Yes, the mega funds have arrived. From a macro standpoint, this demonstrates a healthy appetite for infrastructure exposure. But as managers have increasingly focused their attention on larger deals due to larger funds, transactions over $2.5 billion account for only 5% of the market by number.

This has given way to the other trend we see in infrastructure – emergence of middle market-focused funds. Perhaps taking a page from their private equity brethren or perhaps in search of higher returns, but recognizing an opportunity, more managers have created funds to focus on these 'smaller' transactions. We expect this trend to continue as investors seek to balance the exposures within their infrastructure portfolios.

## Natural Resources: Strawberry

As mentioned, natural resources fundraising has retreated. This has been led by an obvious contraction of fundraising in energy, primarily upstream E&P-focused funds, due to volatility in the sector and possibly also related to ESG-related concerns. However, there has also been a contraction among funds focused on agriculture and timber, likely led by a reduction in returns within these sectors over the last decade. And natural resources as a sub-asset class tends to show lower overall returns than infrastructure or real estate, but with similar or higher dispersion of returns (read: not a good look).

**Dispersions of Returns by Strategy**
Vintage Years: 2000-2019

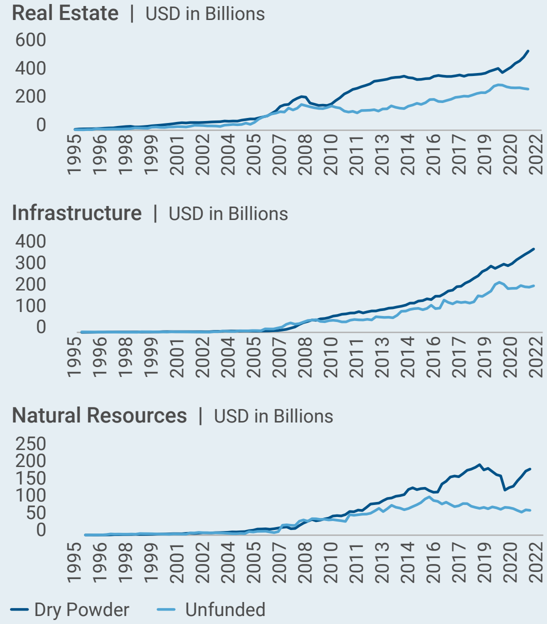



Source: Hamilton Lane Data via Cobalt (December 2021)

But don't ignore natural resources all together. Some investors have begun to consider the asset class once again, particularly within upstream energy, identifying the fact that reduced competition can provide opportunities for the brave. And let's face it, although strawberry sometimes looked a little odd sitting there next to the monochromatic favorites, it was still pretty tasty.

## Final Note on Investor Sentiment

Turning to some of our favorite metrics of dry powder and unfunded commitments as a proxy for investor sentiment, we see similar trends among the three sub-assets classes. Infrastructure has had the steepest increases in both metrics, followed by real estate. In both these cases, both dry powder and unfunded commitments have grown for the most part in tandem over the observed period. On the other hand, dry powder in natural resources has stagnated. Even worse, unfunded commitments to natural resource funds have steadily decreased since 2015, suggesting a pullback from the sub-asset class.




Source: Hamilton Lane data via Cobalt as of September 30, 2021

## STRATEGY DEFINITIONS

Infrastructure –An investment strategy that invests in physical systems involved in the distribution of people, goods, and resources.

Natural Resources –An investment strategy that invests in companies involved in the extraction, refinement, or distribution of natural resources.

Real Assets –Real Assets includes any PM fund with a strategy of Infrastructure, Natural Resources, or Real Estate.

Real Estate –Any closed-end fund that primarily invests in non-core real estate, excluding separate accounts and joint ventures.

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