FINANCIAL NEWS – 4^{TH} to 10^{TH} of July 2016

Investors scramble for illiquids as Brexit floors yields

ByMark Cobley
04 July 2016

Investors' enthusiasm for long-term, illiquid assets such as infrastructure and renewable energy is to increase still further as a result of the referendum result, investors and consultants say, as they seek more profitable havens than bond markets.

The trend has been boosted by a collapse in bond yields in the days after the June 23 vote, leaving illiquid assets as the least-worst option for investors needing a return.

Phil Edwards, European director of strategic research at Mercer, which advises funds worth $6.7 trillion, said: "More schemes are moving in this direction, and this has created a challenge of increased demand for these kinds of assets – long-lease property, ground rents, infrastructure, and those with a credit focus, such as assetbacked securities, trade finance or bank loans.

"A number of firms are putting together products and strategies in this area, and we have clients that are interested in this and actively looking at it."

Long-term, private investments also do not have to be benchmarked every quarter against the market. In contrast, equities can plunge in days – as shown by the FTSE-250, which lost 7% the day after the ballot, and was still down by 5% on its close on 23 June.

10-year UK government bonds dropped to a fresh record low on Friday July 1, of 0.81%, after Bank of England governor Mark Carney warned of possible further monetary easing to come – a move aimed at stabilising markets spooked by the UK's vote to leave the European Union.

Luba Nikulina, global head of manager research at investment consultancy Willis Towers Watson, said pensionfund investors are "trying to keep risk low while going for something more sensibly priced and focused on income."

The crush of investors for this type of long-term asset meant deals were in short supply.

BlackRock, the world's largest asset manager, is among the firms launching new funds to take advantage of the trend. On July 4 it is launching a UK Strategic Alternative Income Fund to invest in infrastructure debt, renewable energy, property debt, long-lease property and direct lending in the UK, with the aim of generating better income than is available from bid-up bond markets.

The company is also raising money for a direct lending fund, which will lend to corporates, led by Stephan Caron, head of direct European direct corporate financing, who signed up from GE Capital in 2014. A BlackRock spokeswoman declined to comment.

Meanwhile, the BAe Systems Pension Fund and the Swedish state fund AP1 are among investors to have committed to a new $300 million fund from Resonance Asset Management, targeting water infrastructure investments.

Pension funds, one of the largest classes of investors, have been pressed by regulators to shift into government and corporate bond markets in recent years. But rising prices and dwindling yields mean it is becoming harder and harder for funds to get the returns they need to close deficits.

To make matters worse, pension liabilities are valued using bond yields, with lower yields meaning bigger deficits. FN reported last week that the decline in UK gilt yields had propelled the UK's collective pension deficit towards £1 billion for the first time.

Additional reporting by Mike Foster