



## Sourcing excellent value-add infrastructure opportunities in the middle market

**Chase McWhorter**, Institutional Real Estate, Inc.'s managing director, *Institutional Investing in Infrastructure*, recently spoke with **Chris Beall** and **Allison Kingsley**, both founders of NOVA Infrastructure. Following is an excerpt of that conversation.

*Why has NOVA Infrastructure focused on the mid-market? And how do you think the mid-market competes with the increasingly larger funds and their portfolio companies?*

**Chris Beall:** There are really three factors that influenced us to start in the middle market. First, that is where the bulk of our experience has been. I have been in the middle market my whole career, looking at transactions between \$50 million and \$300 million. Second, when we were starting NOVA, it was our view that the middle market was a significantly less crowded space, and the bigger funds were getting bigger. That's even easier to see now. Finally, we were confident because of the network of relationships and senior advisers we have, all of whom have experience as operators and executives.

**Allison Kingsley:** Chris brings up these three factors — experience, attractiveness of the segment and deal sourcing — and if you continue on with our data points around those factors, they have all proven themselves out. We have ended up in a situation with significant deal flow, the vast majority of which is proprietary — our relationships in the middle market really have brought deals to us. For the right type of investors, the segment must be attractive, given the size and the nature of the deal flow we are seeing. Sometimes you hear larger funds talk about how their portfolio companies are able to compete in the mid-market, but what we have typically found is that founders/owners/operators who are in the middle market and looking for institutional capital are not indifferent about where they get capital — the idea of working with a team where you are partner to partner, principal to principal, is a different proposition than becoming one of the many subsidiaries of a large portfolio company of a mega-fund.

**Beall:** Founders/owners/operators are picky about the capital they want. They don't just want to be part of a big machine, but rather they are looking for a strategic partner who wants to grow with them.

*2020 has been a challenging year, but it has also created opportunity. What sectors do you think are interesting heading into 2021?*

**Kingsley:** We have thought about this a lot because sector selection is quite important to the strategy. Here at NOVA Infrastructure, we have an advantage in understanding how the sectors interact and being able to pivot as necessary. Right now, we are spending considerable time and capital in environmental services. It is a significant area of our focus, together with waste and water, two sectors that are doing relatively well right now because of their essential nature.

### CONTRIBUTORS



#### **Chris Beall, Managing Partner and Founder**

Chris Beall has more than 20 years of experience in infrastructure, private equity, investment banking, and operations and engineering. At NOVA, Beall originates and leads the execution of infrastructure investments, with a particular focus on the environmental services, energy transition, and communications sectors, and serves as chair of the Investment Committee. Beall also serves on the Board for Integrated Waste Solutions Group, a vertically integrated waste platform that he co-founded that is a current NOVA portfolio company. In addition to his responsibilities at NOVA, Beall serves on the Board of Directors of the National Passenger Rail Corporation (Amtrak), the largest provider of passenger rail service in the United States.



#### **Allison Kingsley, Partner and Founder**

Allison Kingsley has 20 years of experience working in infrastructure, project finance, investment banking and risk. At NOVA, Kingsley originates and leads the execution of infrastructure investments, with a particular focus on the environmental services (water and wastewater), transportation, and energy transition. Kingsley sits on the Investment Committee and additionally functions as chief risk officer. Currently, Kingsley serves on the Board of Directors for Bold Ocean, a maritime logistics business serving the U.S. government, and Jaguar Transport, a short-line railroad platform.

**Beall:** Let me put it in simple terms: If you are sequestered at home, you definitely want someone picking up your trash. You definitely want someone providing you water and electricity, so while there are sources of commercial demand for those, things that focus on people and their homes are important. Telecommunications and media are also very popular now, and for good reason. There are tailwinds behind those sectors as people value connectivity more. Data is growing very quickly. These are popular sectors, and we are watching values go up in concert with that increased popularity, but when people talk about what sectors are interesting, they rarely talk about the commensurate value of getting into those sectors. Even though sometimes sectors seem out of favor, there may be some niche opportunities because out-of-favor sectors may have better values, so you have to look at both sides of the coin.

*What do you think about the increasing importance of digital and communications?*

**Beall:** You really need to separate out the subsectors, because they are not all homogenous. For instance, cell towers are very popular. They have good business models, there is increasing demand, but they trade at very, very high values. If you talk to the people in the sector, they may talk about yields as low

as 4 percent. For telecom opportunities, if you think about fiber to the home, that is strong downside protection because if you are the first mover into a region, you have locked up the good neighborhoods and then you can really do well there. You do have to be very cognizant of valuation, and you have to know something about the sector — you have to have a view of technical risk and technology development. Technology developments are an important part of all infrastructure, but relatively less in a water utility and relatively more in digital and telecom. But it is really important that you have people on your team who have genuine experience. We have a senior adviser who has more than 35 years of experience as a telecom engineer. That gives us great comfort as we are evaluating opportunities.

**Kingsley:** One of the things we have noticed in watching some of the niche players compete for transactions, particularly in the telecom and digital communication space, is that they are very exposed to overall increases in sector valuation. Sometimes it almost seems that they can't afford to lose a deal because it is such a core part of their focus, whereas we are evaluating what are the best opportunities in any one sector relative to all the other sector opportunities.

*So because you are across different sectors, you can be a little bit more selective when it comes to transactions?*

**Kingsley:** Our relationships in the mid-market have allowed us to generate a wide funnel of opportunities, not just in terms of the number of deals, but also in terms of the diversity of those deals. That helps us choose wisely and selectively across the categories that matter to us, valuation being one. We can afford to bypass a deal because we have other sectors with other attractive opportunities.

*Given NOVA's sizable deal flow, what criteria does your team use to evaluate deals?*

**Kingsley:** We don't just evaluate deals. Frequently we are *creating* deals. That creating deals requires market knowledge, judgment, relationships and creativity. It also depends on due diligence and real understanding of the market and opportunity, which only comes from detailed, bottom-up due diligence.

**Beall:** Creative structuring is one of our most important capabilities. It is an interesting time to think about structure because, in the post-COVID-19 world, many people who own assets that they purchased pre-pandemic are not ready to declare value is impaired, and they haven't written things down. Maybe they won't have to — we will see how the market develops. The question is, how do you bridge the gap between buyers and sellers to get deals done? Structure is a key tool you can use to do that, so you can do things that potentially have structural downside protection, like preferred investments, but still have upside exposure — and that may be a way to bridge value. As for leverage, as a value-added manager, our goal is to earn returns by operating assets better than they are currently operated or partnering with good operators to build businesses. We don't want to just crank leverage up a turn or two. Finally, in terms of valuation, there is a lot of capital in the market, and seeking opportunities we can enter into at better attachment points for valuation is one of the main reasons we like the middle market. There are people who have said: "Smaller infrastructure is by necessity inferior;" "Infrastructure is a big-ticket game;" "You need big capital to do the big deals." There are certainly big pieces of infrastructure, but I don't think the smaller pieces of

infrastructure are necessarily inferior just because they are smaller. The only regional airport in a mid-size city is a much smaller airport than LaGuardia, but that doesn't make it an inferior opportunity. It doesn't mean that it has less downside protection. However, it requires experience, judgment and due diligence to know which opportunities are inferior and which are just smaller.

*How do you think about meaningful ESG activity?*

**Kingsley:** People use "ESG" to mean lots of different things. Some think of ESG as a definition of how you report versus how you act. We believe it is how you act, and your reporting flows out of that. You should be embedding ESG values into the culture, and it should be more than just stapled onto your marketing. We think ESG is about asset selection and supporting ESG-friendly practices of NOVA's portfolio companies. For instance, when one of our portfolio companies needs to buy new equipment, are they choosing electric over diesel? Or when hiring contractors for construction, is there a responsible-contractor policy? How do you employ and report on the SASB standards? ESG is about what activities flow out of those, and how we show our commitment to ESG in our actions.

**Beall:** To Allison's point, it is about what you do, but also what you don't do. We looked at a very interesting waste-recycling business, and we quite liked the locations and thought the market was attractive. But when we performed due diligence on the operator, they had a history of releases into waterways. After that review, we didn't feel comfortable that they would be an appropriate partner, even though maybe in other aspects they were operating in an environmentally friendly way. This type of activity is not necessarily going to get captured on a report for us, but it is in the culture — and that is what we focus on. If all you are doing is capturing ESG in your reporting data and it is not showing up in your day-to-day decision making, then you are not really promoting ESG activity.

## CORPORATE OVERVIEW

**NOVA Infrastructure** is an infrastructure investment firm that targets middle-market opportunities in environmental services, transportation, energy and energy transition, communications, and other infrastructure sectors, primarily in North America. NOVA structures investments with significant downside protections characteristic of infrastructure investments and then capitalizes on its expertise to catalyze operationally focused upside generation for its investors. NOVA builds value by combining creative deal sourcing and efficient operations with extensive industry experience and relationships to optimize the long-term cashflow. NOVA's focused hands-on approach, unique strategic focus, significant experience, and market connectivity provide a competitive advantage sourcing bespoke opportunities and monetizing the investment at exit. Central to NOVA's mission of catalyzing value creation in infrastructure is the trust that NOVA strives to cultivate among its team, as well as its partners and investors, through an unwavering commitment to NOVA's values.

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