I Squared Capital invests in the APAC 'growth engine'

A big win in April's Japanese capacity auction is the latest sign of I Squared Capital's commitment to investing in the region, with more to come, senior partner Harsh Agrawal tells Daniel Kemp

In late April, the Japanese government announced the winners of its Long-term Decarbonization Power Source Auction – and among the list of winners were a few surprises. As well as the local developers that have tended to dominate renewable energy auctions in the country were a host of foreign players – among them Actis, Equis and Stonepeak.

But the most eye-catching of all was Hexa Renewables, the APAC renewables platform established by I Squared Capital in 2020, winning 11 contracts, all for battery energy storage systems. The firm was the biggest single winner of any organisation, foreign or domestic, all the more impressive given some of the recent history in Japan.

"We started preparing [for the capacity auction ahead of time] and we had 11 projects that were ready with interconnections and had development done," I Squared senior partner Harsh Agrawal tells *Infrastructure Investor*. "So, because of that, and our team on the ground, we were able to prepare, with 11 projects ready to tender into the auction – and that's one of the reasons we ended up as the largest winner."

Agrawal says I Squared has long had interactions with Japanese investors, with institutions there becoming LPs in its funds and acting as co-investors in portfolio companies in Asia and elsewhere. And through its Hexa platform, it spied an opportunity in the country as its grid begins to open up for the first time in such a way that third-party corporate power-purchase agreements have become viable.

"The team has been focusing on a shift in how corporate consumers procure power in Japan… which is something we've seen happen in other

markets globally. We wanted to get a bit ahead of the curve and start developing projects targeted to those large corporate consumers," he says.

But the story of I Squared in Asia-Pacific goes beyond Japan, with the firm operating out of four offices across the region and targeting opportunities in both developed and emerging markets.

Across Asia

Agrawal points out that I Squared has invested in APAC through its flagship global funds for many years, making them truly global strategies. The firm subsequently launched a vehicle, the Growth Markets Fund, that was explicitly designed to give investors exposure to emerging markets in the region – with roughly 75 percent of its capital ending up deployed here (the other 25 percent going to Latin America).

Agrawal is keen to emphasise that the firm is guided by the opportunities that present themselves in each market. "[Asia is] not one market – there are so many different markets within it. You have to take a slightly different approach in each market and decide what makes sense."

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"If you look at emerging markets versus developed Asia, for example – in emerging Asia, you really want to back infrastructure that is ultimately tied to consumer demand, because that is the macro theme you are getting behind. That means assets where consumers are the offtake, rather than the state – like toll roads, logistics, or utilities.

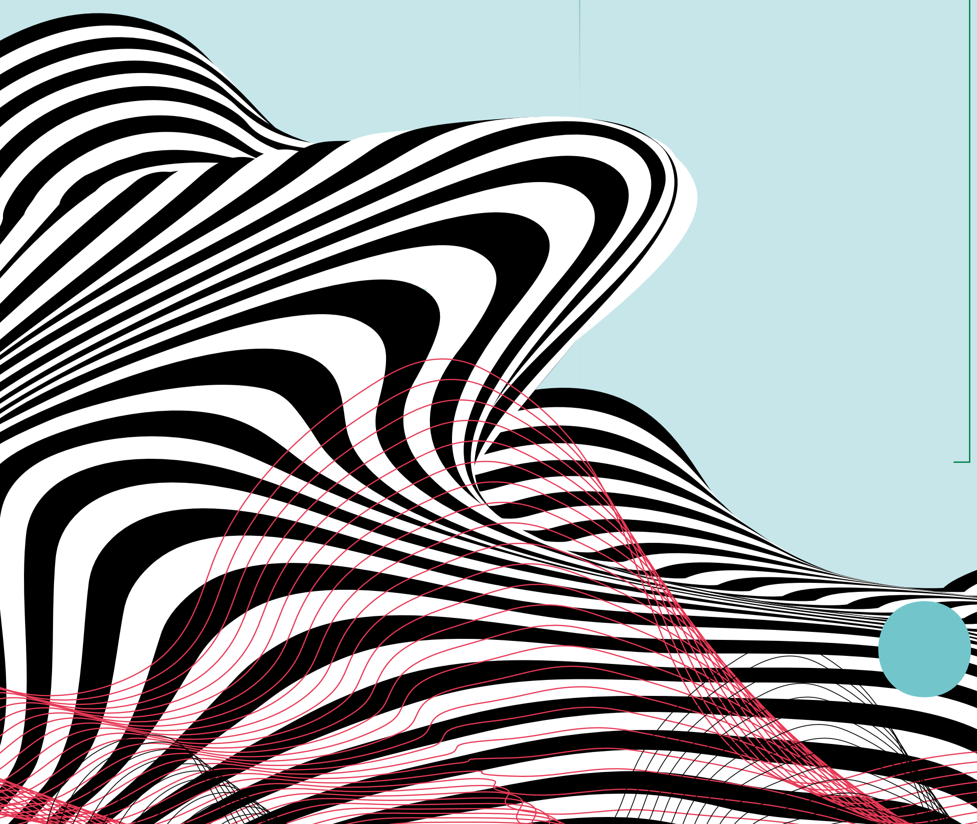
"In developed Asia, you're trying to find sectors where your cost of capital is still relevant. There is a lot of competition in many of these markets from incumbent players who can price things at much finer rates of return than us, so we have to hunt harder for things where we can add value. That means we tend to look at platform-orientated approaches where we can start small, or in the mid-market, and grow organically or through acquisitions over time."

It's that platform approach that I Squared has taken to renewables across the region through Hexa, with multiple markets in the firm's sights already.

As well as Japan, Agrawal says the firm sees other opportunities in north Asia. "We still see a good opportunity in Taiwan – they are actively looking to increase the amount of renewable energy in the grid while reducing the amount of nuclear, so that is attractive. And in the future, there will be opportunities to deploy on the battery side as well.

"In Korea, projects tend to be smaller scale because land is a constraint. So, the strategy is to aggregate multiple smaller-sized projects into a bigger portfolio."

Meanwhile growth markets are also of interest, with the Philippines recently changing regulations to allow 100 percent foreign ownership of some renewable energy projects, and Malaysia enacting policy that will allow it to export power to Singapore.



"Indonesia is also a market we want to do more in, but the pace of change is not as fast as in Malaysia and the Philippines. But hopefully there will be more opportunities there."

Another market Hexa is looking at closely is Australia, although it is taking what Agrawal describes as a "slightly different approach".

"Our existing business here [Clean Energy Fuels Australia] is focused on the energy transition for mining companies. The investment we're looking to make will be under the same theme – empowering mining companies to find greener alternatives for power, moving away from diesel towards a blend of natural gas and renewable energy.

"Our thesis for Hexa in Australia will include a large component where we supply power to some of these off-grid customers through renewables. Australia is a competitive market, but I think our entry point is a differentiator."

Beyond decarbonisation

I Squared is also targeting investments beyond renewables, of course, with digitalisation a prominent thematic, as it is for most investors in the current environment.

The approach will differ from market to market, Agrawal says, but the firm has already set up a pan-Asia data centre platform called BDx that has made investments in Hong Kong, Singapore, Taiwan and Indonesia so far.

"On the fibre side there will continue to be opportunities [too]," says Agrawal, "especially as incumbent operators look for platform investors like us to invest in common shared infrastructure, so that not everybody has to roll out their own fibre networks."

Transport and logistics will continue to be focus areas, with logistics an attractive area in growth markets especially. The firm has had success in transport in multiple markets in the region, too, especially in India where it built a significant portfolio of toll road assets through its Cube Highways platform.

Overall, Agrawal says Asia has been "very competitive" in terms of returns compared with the rest of the firm's portfolio, with I Squared poised to continue raising and deploying capital in the region for the foreseeable future.

Local investors, too, are starting to become more interested in the opportunities in their own back yard. "We still see a lot of desire from Japanese and Korean investors to invest in the US, Europe and Australia, because they tend to favour more developed OECD markets. But they are now investing more in emerging Asia.

"Strategic investors from Japan and Korea have always been very active in the region – but institutional investors may still take a bit more time, it's fair to say."

On the strength of returns, Agrawal says I Squared has been able to achieve "a fair amount" of realisations in the region, despite the more challenging exit environment being experienced by asset managers globally.

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And as to why exits have been possible in APAC, Agrawal believes it is a combination of the fact that there are more willing buyers as capital shifts towards the region – but that it is "also about what you have to sell".

"When people started investing in this region 15-20 years ago, a lot of the deals were minority transactions behind large local groups. So you couldn't really control the exits. But over the last few years, we've taken the approach of pursuing controlling buyouts, or looking at building up companies from scratch, or buying existing companies and scaling them up. Once you have a professionally managed company like that, an incoming strategic buyer may like it.

"The growth engine for the world over the next few years is Asia-Pacific – so a lot of strategic buyers want exposure to that. But they want exposure to companies that have the same ethos as them from an ESG perspective, as well as ones that they can control and make part of their own business, as an extension."

And as with the example of the recent Japanese capacity auction, it's clear there will continue to be an abundance of opportunities in the region, especially in digital infrastructure and the energy transition. ■