

KEYNOTE INTERVIEW

Riding the digital growth curve



Even accounting for recent blips in some markets, digital infrastructure continues to create substantial investment opportunities, explains 3i's Oscar Tylegård

Broadly speaking, digitalisation is a trend that has been embraced right across the investment landscape – but even so, there are certain industries that seem to be further along the curve than others. And yet while some players have been faster to jump on board the digital bandwagon, the direction of travel is clear. Even macroeconomic volatility has been unable to derail investment in digital infrastructure.

As 3i partner Oscar Tylegård explains, the momentum around digital infrastructure means that investment opportunities look set to be in abundance over the next few years. With artificial intelligence and cloud adoption

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showing little signs of abatement, it is up to investors to funnel capital towards the right areas to ensure the wave of digitalisation delivers solid returns.

Q What are some of the key trends you are seeing in digital infrastructure?

The rise of AI, as well as an increasing focus on the infrastructure needed to facilitate it, is the obvious answer. Aside from that, we continue to see strong momentum across the board. We see a

lot of interest in B2B, data centres and applications that will enable companies to take the next step in their digital journey.

Broadly, there is also a “same-as-usual” approach. In some markets, you may have seen investment in digital infrastructure slowing a little, especially with regard to, say, B2C fibre, but this is likely just a blip in the growth curve. Overall, it is very much a continuation of what we have seen in previous years.

There are, of course, trends within the macro market worth keeping an eye on, such as those relevant to deal-making. Even though there has been a slowdown in transactions between

portfolio company owners, investors are still investing in their portfolio companies to support their digital development. This trend is continuing or even accelerating.

We are also seeing that, within the broad digitalisation movement, several technologies are attracting the most investment. For instance, data centres continue to attract a lot of capital. There is also a handful of very large investors backing AI and the cloud in a big way. Additionally, we are seeing a lot of movement around the applications companies are building on top of digital infrastructure to offer extra services to customers, for example developing fibre businesses or helping customers set up private networks.

Finally, there is also technology like 5G that cannot be dismissed. We may have been talking about this technology for a long time, but I think there will be a lot of investment in this space from traditional telecommunication companies in the coming years.

Q How is digital infrastructure helping other industries digitalise?

This is a topic we think about a lot. Where are certain industries in terms of their digital maturity? It is clear that a lot of the traditional, heavy industries are perhaps a bit behind compared to the leaders.

For example, a lot of people are currently thinking about what to do with their data, which creates opportunities, especially for asset-intensive businesses. Using data more effectively could open up a number of improvements – everything from lowering emissions to boosting health and safety and accessing efficiencies. We are entering a period of huge opportunities stemming from further digitalisation.

Even though not all industries are utilising AI directly, the focus on this technology in the media and investment community is facilitating a change in thinking. Infrastructure investors will undoubtedly benefit from

“A handful of very large investors [are] backing AI and the cloud in a big way”

this mindset shift. But it will also pose a question for providers of digital infrastructure: namely, what should you be offering along the value chain?

Meanwhile, several industries that historically have been lagging using data as a way to drive value, are now starting to embrace digitalisation. The energy sector is one. If you take renewables, for example, there has been a focus on managing construction and financing among renewable developers over a number of years, but if you can now use data to generate, say, 1 percent



Part of ESVAGT's fleet of service operation vessels for the offshore wind industry

IMAGE: 31/ESVAGT

Q How is the digitalisation of different industries creating advantages from a customer perspective?

There are customer benefits to be found in all areas, to be honest. You simply have to find the best place to start. You can add value across most areas through digitalisation, particularly if you, as an infrastructure provider, own a lot of data which you can utilise.

As a case in point, a company we own, ESVAGT, is a leading provider of service operation vessels (SOVs) to the offshore wind industry. Together with the ESVAGT team, we helped to plan and manage the operation and maintenance of these vessels using data. We have by far the largest fleet of these assets in the market and, as such, we generate a huge amount of data. In addition, we have upgraded connectivity on the SOVs so there is now 5G on board.

The improvements we have made to ESVAGT's fleet have unlocked other benefits that will be felt by end users. For instance, we are now working on an AI tool to manage operations better. First, we collected data on how we maintain and operate wind farms. Then, we developed an AI maintenance plan for its customers. This is just one example of an industry that is quite asset-intensive, traditionally relying largely on manual resources, which is adopting a new approach. This was all made possible by those connectivity improvements and greater awareness of the importance of data.

more uptime, that is real money. Now that the sector is maturing, moving into digital represents the obvious next step.

Q In what way does digital infrastructure enable progress on key global themes such as sustainability or the rise of AI?

I think digital infrastructure is absolutely vital here. To some extent, I think the general public may have taken the role played by infrastructure in digital transformation projects for granted in the past. But during the covid pandemic, we saw the first signs that this was changing. With supply chain disruptions and other bottlenecks, it became clear just how important infrastructure was.

We now see interesting situations emerging around the globe. In certain pockets, I think you will start to see more bottlenecks caused by a number of factors. First, some regions have faced underinvestment. Also, today we live in a different market setup compared with pre-covid, when we basically enjoyed a zero-interest rate environment. Access to capital was plentiful and inflation was low. This meant we saw large hyperscalers investing heavily across the board, whether it was in subsea fibre or data centres.

We are now in a different macroeconomic environment. We are seeing large players promote capital discipline. Investment decisions are perhaps not as easy to make as they were previously. This is creating a situation where you will see certain areas facing underinvestment, certainly in the short term. This presents an opportunity for infrastructure investors like us to help mitigate bottlenecks and do good business at the same time.

Q Are there any challenges or risks that investors in the digital space should be aware of?

A lot of investors have come to realise the importance of never

underestimating the challenges that surround scaling a business, including how to go from small to medium and then to large. Previously, firms may have been supercharged by an abundance of capital. This capital could be harder to come by now.

Another challenge concerns whether businesses can show the discipline required in our new macroeconomic climate. Perhaps we saw some investors lose a bit of this discipline in the past and overcommitting in certain areas.

Cybersecurity is also set to become more important for infrastructure owners. How you manage this security as an infrastructure owner is a theme

that will increase in prominence as we move further along the digital journey. These challenges are all manageable, of course, but they are certainly areas that investors should keep in mind.

These themes are particularly interesting in light of the changing macroeconomic climate. To some extent, our digital assets are supporting the energy sector, which has, in certain regards, benefited from recent events. For instance, people are focused more on security of energy supply. We also own subsea fibre cables that go from the US to Europe, and also to the Middle East and Asia. Here, as well, you can see that existing assets are attractive, with people being otherwise reluctant to invest in these areas.

In general, what has happened for asset owners today is that if you think about the value of those portfolios that were built out over the past 10 to 15 years, recent rises in inflation and interest rates mean that your existing asset book is worth more today than it was previously. To replicate it today would prove more expensive and more difficult. So, if you invested in the right areas, you are probably sitting quite nicely today.

Q Looking ahead, what does the investment pipeline look like for digital infrastructure?

The future looks very positive for digital infrastructure. It is clear that there has been a slower M&A market over the past 18 months, but the need for investment has not disappeared. Significant pent-up demand remains because of macro themes like AI and cloud adoption.

Regarding the investment pipeline, there are a number of positive signs for the rest of 2024 and beyond. We are confident that digital will remain a space with ample opportunity to invest in the coming years. There has been a small shock to the system recently but perhaps that has actually made digital more attractive to invest in. ■

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