



Plans for an innovation district north of Oxford in the UK

# Innovation districts – an emerging asset class?

Georg Inderst examines the benefits and pitfalls for investors in this growing area

Innovation districts are a growing feature in cities across the world. Their main purpose is to boost a region's economic and social development by concentrating high-tech companies and research institutions in one place.

Governments try to seed 'the next Silicon Valley', while the private sector can find a modern and publicly supported business environment. Institutional investors are also becoming interested in this area. So what are the opportunities and what are the challenges them? Is there a new asset class in the making?

Clusters of innovative enterprises are nothing new in history. Since the 1990s, dedicated science and technology parks (STPs) have been set up in the US and Europe, across

developed Asia and China, and also in other emerging markets.

These days, the term 'innovation districts' indicates a wider sectoral focus, including all sorts of R&D, life-sciences, biotech, fintech, education, communication, media, and other entities.

## Enormous variety

There is no clear count of STPs and innovation districts. The hundreds of examples are very different, all with their own legacies and political objectives. They vary in location, size and population, legal and regulatory frameworks, shareholders and stakeholders, funding and financing arrangements, development stage, and more.

For example, is it urban regenera-

tion or a greenfield project near universities or airports? Who drives the project? Who owns the land? Are housing and leisure facilities planned in addition to working spaces?

Some innovation districts are dominated by the public sector, some more privately run, and others are formal public-private partnerships (PPPs) – international studies have shown the heterogeneous nature of innovation districts.

In Europe, for example, @22 Barcelona is an early and well-known example of an innovation district, with urban and industrial regeneration, as well as social revitalisation and extended housing capacities. A quite different example is WISTA Adlershof at Berlin's periphery, a post-GDR project for universities and

tech companies, run by the Berlin state via a fiduciary agency. In contrast, Thess INTEC, outside Thessaloniki, is a greenfield project with a combination of public (including universities) and private shareholders (including international companies).

Three key players are traditionally involved: (local or central) government, universities/R&D institutions and the private sector. The local community is an increasingly important fourth pillar of 'innovation ecosystems'. For politicians, the case is easily made. However, it is often less clear what sort of policy interventions are needed for such clusters to evolve – if any. How are the (technological, economic, financial, social) benefits measured? How is

success or failure assessed?

The private sector can offer opportunities both for entrepreneurs and investors:

- There is the traditional role in STPs for entrepreneurs, start-ups, business incubators and accelerators, as well as other service providers. This is also well-explored territory of interest for venture capital and private-equity firms.
- Private companies are called in for the development of land and the construction and operation of commercial and residential buildings. This area has seen a growing involvement of institutional real estate managers.
- Transport, energy, water and communication networks need to be built or upgraded. Much of this is undertaken by the public sector, but private companies can also be contracted. This can be attractive for investors in infrastructure.
- Social-infrastructure investors can be interested in financing student accommodation, affordable and social housing, health facilities, entertainment and cultural venues, and so on.

**Institutions come to the fore**

The rise in institutional investors engaging in innovation districts is noticeable – not only real estate managers but also large asset owners that are starting to take direct stakes in them.

GIC, the Singapore sovereign wealth fund, bought a stake in Oxford Science Park from Magdalen College in 2021. UK insurer L&G General is developing a district with the university in that area. French insurance company AXA has gained exposure to several science parks across Europe.

The Canadian Pension Plan Investment Board and the Australian property group Lendlease are in a joint venture for MIND, an innovation district developed on the 2015 World EXPO site in Milano. Several large pension funds in the Netherlands, the Nordics and Canada have also become active in this area.

There are several attractions for real estate investors looking at

innovation districts. For example, investors can expand their real estate portfolios beyond the traditional sectors into ‘alternative’ segments such as technology and life-science properties, digital infrastructure and communication, logistics, hotels and leisure, residential, and others.

Innovation districts can offer stable returns and inflation protection. Pension funds and insurance companies look for investments with predictable returns over longer periods. Preferred assets ideally offer some inflation-hedging characteristics, either by contract or by having sufficient pricing power.

There are diversification benefits, too. Some segments of innovation districts tend to be less affected by the business cycle, including medical and R&D facilities, student residences, university and public tenants. Less-correlated returns are welcome, especially in difficult times.

And finally, innovation districts often receive government support, either directly, via long-term lease and management contracts with public institutions, or via the provision of public infrastructures.

**Challenges for infra investors**

One less explored area – at least so far – is institutional investing in the infrastructure of innovation districts. Governments often lack the budgetary funds or the management capacity at local level.

All sorts of economic and social infrastructure around these districts could do with strong, long-term institutional financing:

- Public transport networks such as trains, trams, sky trains, cable cars;
- Other transport infrastructure such as bridges, tunnels, toll roads;
- Renewable-energy generation and distribution;
- Water and wastewater network;
- State-of-the art district heating systems;
- Digitalisation – security and cybersecurity systems;
- Affordable and social housing; mixed living areas;
- Schools and training places; student accommodation;
- Medical and emergency facilities;



Georg Inderst: we are some distance away from a reasonably standardised approach to institutional investing in innovation districts

- Cultural and entertainment halls, recreation areas such as parks.

For investors, the challenge is that such portfolios can be laborious to set up and cumbersome to manage because of the broad range of stakeholders. The small size and the lack of scalability of projects is another issue.

Furthermore, experiences with one district are not easily transferable to other districts.

**Impact investing at work**

For asset owners, there is an opportunity here to invest not only in a sustainable way but also to invest with a clearly visible impact.

In a localised context, impact may be more easily visible and measured – for example, in jobs creation, rising education levels, newly built living spaces, improving energy efficiency, carbon footprint, biodiversity, social inclusion, lower crime rates, and so forth.

Of course, impact investing this way is not without hurdles and controversies, and definitely open to the temptations of green-washing, social-washing and all sorts of dubious public relation stunts.

In reality, climate/nature objectives and social objectives easily conflict in high-density areas. Finally, there can be positive (or negative) spillovers into neighbouring regions. For example, do smart cities generate new ways of social exclusion?

**Single asset or an entire park?**

An important distinction must be emphasised: is the investment in a single asset or in an entire innovation park? At the lower, asset-specific level, investing in companies or real

estate within innovation districts is not much different from investing in other locations.

However, getting involved at the upper level, ie, the development and operation of a whole technology park, is another matter. Much depends on the specific ownership and governance structures in place.

Investing in an entire innovation district comes with more complexity and a distinct set of opportunities and pitfalls.

Many investors feel uncomfortable with too many players in the room. Also, generous public commitment can evaporate with the change of political parties or people in power. How stable is the support of community groups, and how will the media look at PPPs when something goes wrong? These are potential reputational risk factors, especially for asset owners.

Last, but not least, there is competition between locations, and innovation districts might themselves face disruption from technical progress, and changing consumer preferences or supply chains.

Innovation ecosystems require the capacity to co-operate with politicians, the local administration, educational institutions, associations, local communities. A consistent, and yet dynamic, partnership is required. What is the concrete funding proposition, and how can revenue from users or governments be secured over longer periods? What are appropriate investment vehicles and what could the expected risk-and-return profile be? Finally, things can go wrong at some stage; what can be re-negotiated, and is there a breakup clause?

To conclude, the potential for broader institutional investing in this field is certainly there. Innovation ecosystems worldwide can generate more interesting opportunities for private equity and real estate, and increasingly also infrastructure investors and impact investors.

However, when it comes to entire innovation districts, they can have very different institutional set-ups.

We are some distance away from a reasonably standardised approach to institutional investing in innovation districts, and it can certainly not be decreed by governments or international institutions.

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