

Global listed infrastructure

A safe harbour for investors?

For financial advisers and qualified/professional/institutional investors only

September 2022

Infrastructure describes the physical assets that provide basic services to modern society, including utilities, transport and communication assets. The fundamental, essential nature of the services provided gives global listed infrastructure qualities that can be beneficial to an investment portfolio.

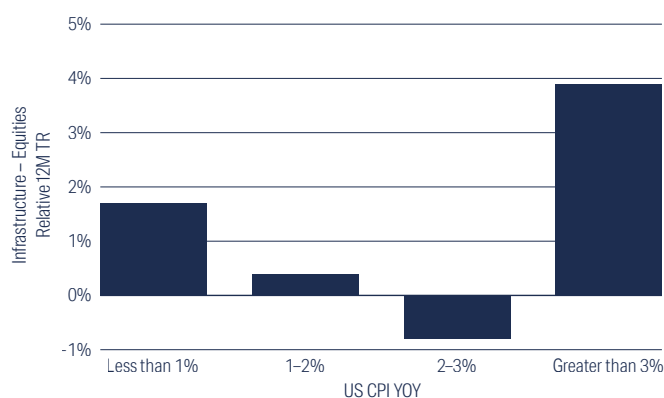
A hedge against inflation?

Global listed infrastructure has outperformed global equities as inflation has risen over the past year. This is a reflection of listed infrastructure being a price maker, not a price taker. Infrastructure's tangible assets provide essential services, using contracted or regulated business models. These assets consistently demonstrate the ability to pass through the effects of higher input costs and inflation to the end user. This can be achieved through regulated real returns for utilities, or through contracts which explicitly link tolls or fees to the inflation rate.

Infrastructure's capital intensive nature provides high barriers to entry which have allowed incumbent operators in other sectors, such as mobile towers and freight rail, to achieve similarly robust pricing results even without explicit inflation links.

An analysis by First Sentier Investors' listed infrastructure team has found that more than 70% of assets owned by listed infrastructure companies may have effective means to pass-through the impacts of inflation to customers, to the benefit of shareholders. The following chart illustrates how listed infrastructure has outperformed global equities when inflation was higher.

Infrastructure performance during periods of inflation



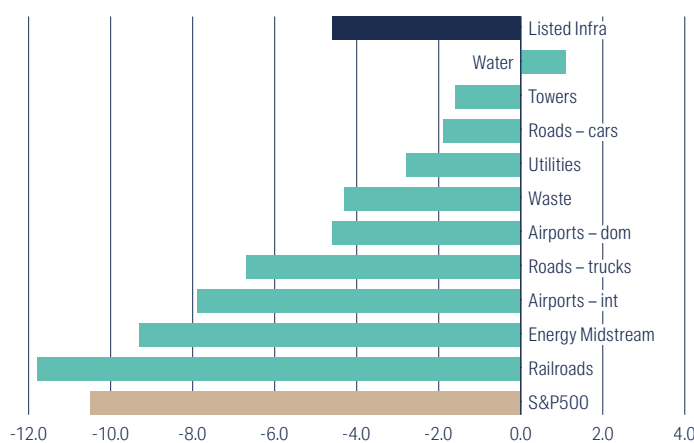
Infrastructure FTSE Global Core Infrastructure 50/50 Total Return Index in USD
 Equities MSCI World Total Return Index USD
 CPI US CPI Urban Consumers SA
 Source: Bloomberg and First Sentier Investors Quarterly time series from 2002-2022

Is listed infrastructure recession proof?

Listed infrastructure has also demonstrated an ability to provide most of the upside in rising equity markets, while offering protection from falling ones. This pattern of performance is underpinned by global listed infrastructure's consistently strong pricing power, predictable cash flows, and relative immunity to economic cycles. This ability to hold up in falling markets has enabled the asset class to generate higher returns than global equities over the past 20 years, with less risk, as measured by standard deviation of returns¹.

First Sentier Investors' listed infrastructure team have undertaken modelling to estimate the potential impact of a recession on different sub-sectors within the asset class. This modelling assumes a -3% change in GDP (from a previously-assumed GDP growth rate of +2% to a decline of -1%), with associated multiplier effects on industrial production, housing starts, commodities etc. This analysis suggests listed infrastructure may suffer less than half the earnings impact relative to broader markets in this scenario, represented by the S&P 500 index.

Expected change in earnings from recession scenario



Source: First Sentier Investors as at 30 June 2022.

1. As at 30 June 2022, comparing the FTSE Global Listed Infrastructure 5050 Index with the MSCI World Index.

Structural growth drivers

Providing further support to infrastructure as an investment is the extent to which it positively aligns to structural growth themes occurring across the globe. Decarbonisation, the electrification of transport, and ever-growing demand for online connectivity all require unprecedented investment in supporting infrastructure. These themes are not transitory and will not be derailed by an economic downturn.

For example, we are optimistic about the substantial investment opportunities associated with the decarbonisation of the world's energy needs. Utilities, which represent about a half of the listed infrastructure opportunity set, are positioned to derive steady, regulated earnings growth by building solar and wind farms, and by upgrading and expanding the networks needed to connect these new power sources to the end user.

US utility companies Entergy, NextEra Energy and PPL Corp recently increased their earnings guidance as a result of additional investment in these areas – a welcome contrast to the turmoil seen elsewhere in financial markets. The roll-out of electric vehicles is expected to provide an additional boost to utilities in the medium term – first from investment opportunities associated with linking EV charging stations to the grid; and then from higher overall demand for electricity.

Digitalisation is another key theme for the asset class. Structural growth in demand for mobile data (underpinned by an ever-growing reliance on digital connectivity) continues to support

steady earnings growth for Towers and Data Centres, insulating them from the ebbs and flows of the broader global economy. The adoption of 5G technology over the medium term will require networks to handle increased data speed, and a much higher number of connected devices.

Statistics from the 2022 Ericsson Mobility Report² highlighted the continuation of this theme. Key points including global mobile network data traffic growing by 40% during the March quarter of 2022, compared to the same period a year earlier; and the forecast that mobile network traffic will increase at a compound annual growth rate of 29% through to 2027. This bodes well for well for continued capital expenditure into mobile networks, to the benefit of Towers.

Conclusion

Listed infrastructure offers a relatively safe harbour for investors navigating an increasingly uncertain and volatile world. Across a range of economic environments and world events, the asset class has shown an ability to out-perform many other asset classes over the medium to long term.

There is no reason to believe this enduring quality is less today than it has ever been. We believe listed infrastructure remains a compelling opportunity and should be considered a core component within investors' portfolios.

2. <https://www.ericsson.com/en/reports-and-papers/mobility-report/reports/june-2022>

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