



A new age of infrastructure

Ingrid Edmund

Senior Portfolio Manager, Infrastructure Investments

Investors are embracing infrastructure assets like never before. In 2018, they look likely to set a record for unlisted infrastructure fundraising at the time of writing.¹ Why? Infrastructure assets can offer relatively high yields that investors with regular income needs, such as insurance companies and pension funds, find difficult to come by in today's persistently low-interest rate environment.

Investors are finding a plethora of opportunities, as the private sector steps in to fill a funding gap left by governments. Europe, where we invest, needs €2 trillion of investment in infrastructure by 2020 just to stay competitive, according to estimates by the European Commission. In straitened economic times, this is a bill that most governments simply cannot afford.

Europe's infrastructure needs renewal, but in ways that are sustainable over the long term. For example, ports are being upgraded to make supply chains more effective, ensuring that goods can move around the world more efficiently. These modernisations will improve the capacity of ports and mean that customers receive better service. Conversely, the need to meet a new, stricter cap on sulphur in marine fuel could force down port revenues as shippers may start negotiating harder on price. An ever-changing landscape means that infrastructure investors must weigh up opportunities and challenges carefully.

In many ways, this growing emphasis on sustainability and new technology represents a new age of infrastructure investing. Investors are more focused on environmental, social and governance (ESG) issues than ever before. We think that ESG and infrastructure investment are a natural fit. Much of Europe's ageing infrastructure needs renewing to ensure it is sustainable.

When investing in infrastructure, we believe it is important to take a long-term view, to build projects that are sustainable and ecologically responsible, and to be prepared to continually make improvements. Ultimately, this will result in better returns and lower risk, as politicians and regulators are much less likely to intervene.

¹ Preqin Infrastructure Capital report, October 2018: <http://docs.preqin.com/reports/Preqin-Infrastructure-Capital-October-2018.pdf>.

Powered by sustainability and technology

2019 looks likely to be another year of impressive growth for infrastructure as it enters a new age, driven by technological disruption and the growing importance of sustainability. As investors, we think it is important to select from the right set of opportunities. Instead of joining the queue of competitors who are keen to participate in high-profile mega deals, we are looking to the mid-market, where there are more prospects which often offer better value and less competition.

Sustainability is an increasingly important theme. In recent years, there has been enormous growth in renewable energy infrastructure, notably solar parks and wind farms. The pace of change has been so rapid that power grids have not necessarily kept up: even more opportunities will arise in this area as it develops. Around 30% of Infrastructure investments are in renewable sources.² Smart cities are much talked about; when they are realised, they will be powered by smart, technology-enabled infrastructure.

Energy distribution generally is becoming more efficient. District heating, for example, has traditionally been fuelled by gas or oil; these days, alternative sources like water and hydrogen are getting more popular, as is biomass heating. As these systems are upgraded, they will create opportunities for investors.

Technology's role in making infrastructure more efficient is also likely to grow in 2019. This means that, for instance, water utility companies can now hover a scanner over an area and see if there is a leak, where in the past they would have had to dig a hole to locate the problem.

Balancing risk and reward

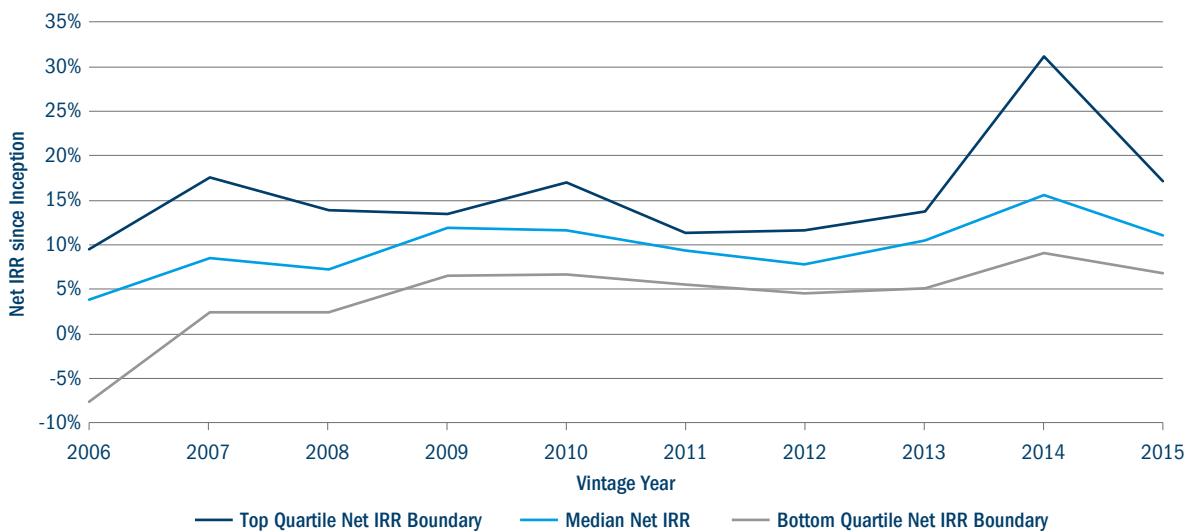
There is a popular narrative that infrastructure is predictable and stable. But it can only offer these characteristics if it is carefully managed. Myriad return drivers fuel infrastructure, and various risk factors could have different effects on different types of infrastructure.

Political and regulatory change can also impact infrastructure's potential returns. For instance, the International Maritime Organisation has introduced a 0.5% cap on sulphur, with which all ships must comply by 2020. This will have seismic implications for how ships are fuelled, and shipping and trade patterns more broadly.

² Preqin Infrastructure Capital report, October 2018: <http://docs.preqin.com/reports/Preqin-Infrastructure-Capital-October-2018.pdf>.

Looking to 2019, it is more important than ever for investors to take a long-term view but also be prepared to follow policy and regulatory developments closely. Long-term asset owners with a commitment to sustainability are much more likely to have the ear of regulators and government than those who are only driven by short-term profit.

Unlisted Infrastructure: Median Net IRRs and Quartile Boundaries by Vintage Year



Source: Pregin 2018.

If a manager buys a host of infrastructure assets in a particular period, they are vulnerable to vintage risk, ie, the risk of buying assets at a particular point in the cycle and then struggling to sell them at a different stage when prices are lower. As the chart above illustrates, infrastructure does not move in a straight line: there are zig zags in performance. For that reason, a long-term view is key to sustained growth over time.

To find out more visit
COLUMBIATHREADNEEDLE.COM



Important information: For investment professionals only, not to be relied upon by private investors. Past performance is not a guide to future performance. The value of investments and any income is not guaranteed and can go down as well as up and may be affected by exchange rate fluctuations. This means that an investor may not get back the amount invested. This material is for information only and does not constitute an offer or solicitation of an order to buy or sell any securities or other financial instruments, or to provide investment advice or services. The analysis included in this document has been produced by Columbia Threadneedle Investments for its own investment management activities, may have been acted upon prior to publication and is made available here incidentally. Any opinions expressed are made as at the date of publication but are subject to change without notice and should not be seen as investment advice. Information obtained from external sources is believed to be reliable but its accuracy or completeness cannot be guaranteed. This material includes forward-looking statements, including projections of future economic and financial conditions. None of Columbia Threadneedle Investments, its directors, officers or employees make any representation, warranty, guarantee or other assurance that any of these forward looking statements will prove to be accurate. Issued by Threadneedle Asset Management Limited (TAML). Registered in England and Wales, Registered No. 573204, Cannon Place, 78 Cannon Street, London EC4N 6AG, United Kingdom. Authorised and regulated in the UK by the Financial Conduct Authority. TAML has a cross-border licence from the Korean Financial Services Commission for Discretionary Investment Management Business. Issued by Threadneedle Portfolio Services Hong Kong Limited 天利投資管理香港有限公司. Unit 3004, Two Exchange Square, 8 Connaught Place, Hong Kong, which is licensed by the Securities and Futures Commission to conduct Type 1 regulated activities (CE:AOA779). Registered in Hong Kong under the Companies Ordinance (Chapter 622), No. 1173058. Issued by Threadneedle Investments Singapore (Pte.) Limited, 3 Killiney Road, #07-07, Winsland House 1, Singapore 239519, regulated in Singapore by the Monetary Authority of Singapore under the Securities and Futures Act (Chapter 289). Registration number: 201101559W. This document is distributed by Columbia Threadneedle Investments (ME) Limited, which is regulated by the Dubai Financial Services Authority (DFSA). For Distributors: This document is intended to provide distributors' with information about Group products and services and is not for further distribution. For Institutional Clients: The information in this document is not intended as financial advice and is only intended for persons with appropriate investment knowledge and who meet the regulatory criteria to be classified as a Professional Client under the DFSA Rules. Issued by Threadneedle Investments Singapore (Pte.) Limited ["TIS"], ARBN 600 027 414. TIS is exempt from the requirement to hold an Australian financial services licence under the Corporations Act and relies on Class Order 03/1102 in marketing and providing financial services to Australian wholesale clients. This document should only be distributed in Australia to "wholesale clients" as defined in Section 761G of the Corporations Act. TIS is regulated in Singapore by the Monetary Authority of Singapore under the Securities and Futures Act (Chapter 289), Registration number: 201101559W which differ from Australian laws. Issued by Threadneedle Asset Management Malaysia Sdn Bhd, Unit 14-1 Level 14, Wisma UOA Damansara II, No 6 Changkat Semantan, Damansara Heights 50490 Kuala Lumpur, Malaysia regulated in Malaysia by Securities Commission Malaysia. Registration number: 1041082-W. This document is distributed by Columbia Threadneedle Investments (ME) Limited which is regulated by the Dubai Financial Services Authority (DFSA). For Distributors: This document is intended to provide distributors' with information about Group products and services and is not for further distribution. For Institutional Clients: The information in this document is not intended as financial advice and is only intended for persons with appropriate investment knowledge and who meet the regulatory criteria to be classified as a Professional Client or Marketing Counterparty and no other Person should act upon it. Columbia Threadneedle Investments is the global brand name of the Columbia and Threadneedle group of companies. columbiathreadneedle.com