



Infrastructure Investing

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September 8, 2009

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With global markets improving, liquidity returning to the credit markets, and valuations improving, the infrastructure market looks promising. Infrastructure assets, when chosen correctly, can diversify an investor's portfolio because of their low correlation with other asset groups, their consistent returns coupled with lowered levels of risk, and their potential for inflation-linked returns.



What is listed infrastructure?

Infrastructure assets represent a broad mix of the large-scale public systems, services, and facilities of a country or region that are necessary for economic activity to function. Some examples of infrastructure include power generation and transmission, water supplies and wastewater treatment, public transportation, rail, roads, bridges, tunnels, ports, airports, telecommunications, and finally, basic social services such as schools and hospitals. The global listed infrastructure securities market represents a market value of roughly \$1.79 trillion. (Source: S&P Listed Infrastructure Assets - A Primer 2009)

Infrastructure has emerged as a differentiated asset class that provides unique investment characteristics. Infrastructure assets provide a necessary good or service to society, and they have high barriers to entry for competitors. Because of the pricing power that results from their favorable market position, regulators typically limit the revenue growth from these assets to the rate of inflation. As a result, infrastructure investments are able to offer long-term stable cash flows that have the potential for inflation hedging.

Infrastructure investments also exhibit a hybrid nature of both fixed income cash flows coupled with capital gains. They behave somewhat like a bond with stable cash flows, but these assets can be improved upon and their capacity can be expanded, allowing for their principal value to grow over time.

Finally, infrastructure investments offer a variety of risk and return profiles. Infrastructure investments range from low-risk regulated assets to moderate-risk loosely regulated



entities such as energy production. The assets offer varying amounts of inflation protection and different levels of vulnerability to economic cycles. It is important to note that, while these assets are all considered the same asset class, not all of them will exhibit the same risk and return behavior.

What are the benefits of listed infrastructure investments?

In response to a recent survey conducted by Capital Innovations LLC, high net-worth investors listed the attributes they consider most important in an attractive investment: diversification, liquidity, reasonable fees, valuation/ daily market pricing, transparent corporate governance and active management.

Listed infrastructure can provide these key attributes to your clients in a straightforward and easy to understand framework, differentiating it from many other complex, unlisted (private equity type) investments.

Diversification: There are a series of risk and return elements to any investment strategy. Listed infrastructure permits investors to diversify across “sectors,” which may help to ameliorate some of infrastructure’s inherent risks (i.e., regulatory risk, demand risk, interest rate or refinancing risk). Diversification across regulatory sectors, physical assets, currency exposure and political risks (countries or regions) helps investors construct a portfolio that achieves their desired risk/return profile. A global diversified portfolio of holdings can accomplish this.

Large Investment Universe that Provides Liquidity: Investors may access investment vehicles, separately managed accounts, and mutual funds, all of which have liquidity that is not available in direct project finance deals. This liquidity feature allows investors to easily put money to work and conversely trim their listed infrastructure exposure to maintain their asset allocation models.

Reasonable Fees: Fees that are assessed on an investment portfolio represent an obstacle, for investors and portfolio managers alike, to investment performance. An actively managed separate account portfolio of listed infrastructure investments whose pricing is negotiated can be more attractive than buying a mutual fund or ETF.

Valuation and Daily Market Pricing: In the current market environment, transparency is at a premium. Listed infrastructure securities are exchange-traded and market-priced, providing investors with the level of disclosure they need.

Transparent Governance: Listed companies are subject to scrutiny from regulatory authorities, governments, investor advocacy groups, labor unions and the media.

Active Management: Active portfolio management in the listed infrastructure sector can generate significant returns while avoiding unwanted sector concentration in the



benchmark. Stock market volatility has risen, creating a greater dispersion of returns among individual stocks and expanding the possibility for active managers to distinguish themselves from a benchmark.

What is the infrastructure opportunity?

Global demographic trends are driving a need for infrastructure construction in the world's developing economies. Populations are shifting from agrarian to industrial, urban societies. These geographic regions require new, modern infrastructure to facilitate the expansion of industry, urbanization, and to accommodate continued population growth and an expanding middle class. In the developed markets, basic infrastructure is old and dilapidated, having been constructed in the middle of the twentieth century. The percent of GDP that most developed countries spend on infrastructure has been steadily declining for decades, leaving them with a crumbling legacy. This entire supply of old infrastructure needs to be either repaired or replaced.

The amount of investment that will be required to fix or upgrade existing infrastructure in the developed economies is truly stunning, especially when one examines our own situation in the U.S. The American Society of Civil Engineers has estimated that the United States needs \$2.2 trillion in infrastructure funding over the next five-year period!

Recently, the commitment to building America's future through stimulative infrastructure spending and project development has provided a much-needed boost to job creation. In addition to the long-term trends at work that favor this asset class, the stimulus package recently enacted by the U.S. government will benefit infrastructure investors directly in the near term.

If history is an indicator, stock market recoveries have come in relatively short bursts, and outperformance has occurred in a select number of sectors; infrastructure has been one of these sectors. As the markets continue to rebound from their lows, listed infrastructure securities are well positioned to capitalize.

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