How focussing on long life infrastructure can help investors meet their goals

Adrian Mucalov
Partner, Head of Long Life Infrastructure

Infrastructure has long been known for producing solid, risk-adjusted yields over a significant timeframe. The sector's strong, consistent, predictable returns which exceed those available in the fixed-income class have meant it has become a valuable source of resilience and diversification within many portfolios. Meanwhile recent global events have thrown light onto another characteristic - its help in protecting investors from inflation.

Long life infrastructure funds – funds that invest in assets for a decade or longer – have a particular role to play in meeting investor needs. They typically invest not in greenfield businesses but in established companies with proven yielding cashflows, and undertake moderate capital expenditure and optimisation strategies to improve the assets. By holding on to investments for longer, they can better match the liabilities investors face. The longer timeframe also gives a manager the opportunity to build greater sustainability into a portfolio, and drive technical and commercial improvements, as well as allowing the fund's own investors to take advantage of the cashflow for longer.

Such an approach can help attract a wider investor base. A longer-term perspective can for example attract more global insurers, sovereign wealth funds or institutional pension funds who seek regular cash distributions, and who often prefer a lower-risk approach than investing in newer businesses typically involves. This lower-risk style may be particularly important for those who are seeking to invest in geographies that are new to them.

Long life investing can focus on a number of sectors. Sustainable energy assets for example such as wind farms, solar energy plants and transmission systems can play a critical role in growing economies and delivering electricity to local communities, as well as helping the world meet its net-zero goals. Investing in transport systems such as toll roads can lead to more efficient road usage, reduced car idling and pollution, and lead to quicker journeys with lower emissions.

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Meanwhile digital infrastructure such as data centres are vital when it comes to managing the world's seemingly insatiable appetite for technology. The growth of Artificial Intelligence and 5G are only two of the trends which are likely to support such centres in the future.

What characterises all these investments is the length of tenors and the stable yields they tend to deliver. But where in the world can the most compelling risk-reward opportunities be found? Typically, these are in markets where the need for sustainable long-term infrastructure is at its highest, but where the amount of capital available to invest is relatively scarce. That means examining business opportunities in some of the less mature, faster growing economies of the world such as Asia and Latin America, as well as in Central and Eastern Europe. In CEE for example, while there are a number of important existing east-west transport links due to the need to access the region from western Europe, there are fewer networks linking the north and south. Energy security is also a huge issue in this region. This area is likely therefore to be a significant investment opportunity in the years ahead.

Meanwhile India is already one of the largest markets in the world for renewable energy and toll roads; nearly all of the required capital now comes from private investors. The transition from coal to renewables is a top government priority, and the demand for quality transport infrastructure is growing relentlessly to support the country's roughly 7% annual GDP growth.

For a successful investor it is vital to have a robust attitude to risk. This can be mitigated by focussing on countries which are already comfortable with foreign direct investment and have a long, successful track record of regulation. It is also important to assess macro risk in each market on a regular basis, and work with a manager with experience in a particular country, one who can help ensure the right balance between risk and reward is attained.

Investing sustainably is also key in these sectors and regions. Being a sustainable long-term investor who takes time to build a portfolio company's ESG credentials is, of course, critical in supporting the global energy transition. In addition however, integrating any infrastructure investment into a community – so that its members can see the benefits it is bringing - is vital in creating a licence to operate, both at a local and national level. Having a robust and proven commitment to governance is also important in ensuring the successful operation of an asset. Commitments like these do not just support sustainable development goals - they also create a more valuable business that can lead to higher exit values when it comes to selling a portfolio company.

How do investors identify the right partner? In any region, it is vital that investors work with managers with a deep and specialised knowledge of the target investment regions. This is especially true if focused on faster-growing economies such as Asia, Latin America and elsewhere. They should work with a firm with an on-the-ground presence, one with experience in investing there and knowledge of the local nuances. It is also important to find someone with the mindset of a builder-operator, with a strong portfolio management team whose focus is on optimising assets.

Long life infrastructure assets are also important in meeting what has become a recent challenge for many: the current environment of high inflation. Many investments in core, long life infrastructure can be structured in a way that revenues are linked to price indices. Many markets outside of the United States also continue to offer contracted returns that are not denominated in local currencies, but in US dollars. The long-term nature of contracts means investors can index to inflation resiliently and safely for decades.

Investors have always valued the high-yielding, predictable returns that long life infrastructure provides. Many are now finding the current global environment means protecting their portfolios from inflation has never been more important. What was formerly a useful additional characteristic has now become one of the core reasons to invest. For those seeking stable, inflation-protected returns, the attractions of long-term infrastructure are now more compelling than ever.

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