A formidable friend in turbulent times

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Infrastructure debt is now an established alternative asset class. While it broadly refers to the debt component of an infrastructure asset's or company's capital structure, it is by no means homogeneous, with the market covering a range of sub-sectors and risk profiles.

PATRIZIA specifically targets transactions generating spreads of 400 to 600 basis points, known as the "high-income" segment. Such investments are typically subordinated to senior debt, have a BB/Ba rating profile and issued by the private holding companies ("HoldCo") of infrastructure assets.

In a relatively short period of time, private, high-income infrastructure debt has matured considerably as an investable asset class. Its appeals are by now well established – it tends to exhibit low volatility backed by stable long-term cash flows, lower default risk versus broader corporate credit, typically robust inflation insulation, and favourable portfolio construction benefits. Additionally, the current uncertain yet pessimistic economic backdrop plays to its cyclical resilience.

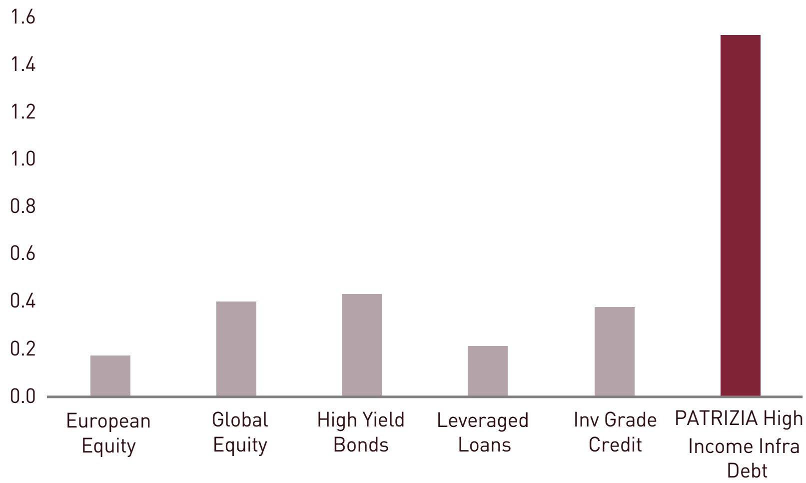
That said, the benefits of high-income infrastructure debt are not exclusive to contemporary conditions; the class can help play a pivotal role in a key secular trend - generating decarbonisation and broader sustainability outcomes. This is by way of lending to assets designed and built to adapt and be resilient to climatic impacts and which provide communities with reliable, essential services. Regardless of the direction the global economy takes in the coming years, high-income infrastructure debt's ability to generate superior portfolio construction outcomes and contribute to sustainability targets is likely to ensure its investment rationale remains strong in the years to come.

Increasingly compared to direct lending by investors, high-income infrastructure debt is typically secured against businesses or assets with long-term stable cash flows; by comparison, direct lending is generally secured against small to mid cap businesses, including in sectors which exhibit material cyclicality.

We consider the investment rationale for the high-income segment of the infrastructure debt market a compelling one for a number of reasons.

Compared with other fixed income asset classes, high-income infrastructure debt can possess structural complexity. As a niche market, it requires expert knowledge and entails technical lending terms. Accordingly, lenders with greater scope to undertake their own credit analysis are better able to identify attractively priced opportunities and capture additional return premia.

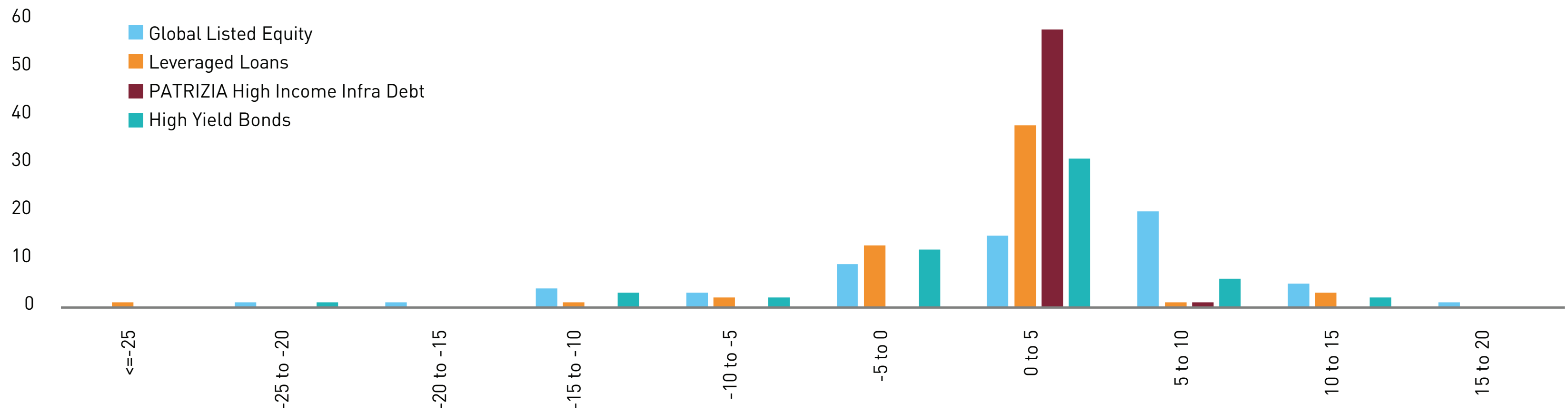
Long term Sharpe ratio^



Long term asset class correlation^

	European Equity	Global Equity	High Yield Bonds	Leveraged Loans	Inv Grade Credit	PATRIZIA High Income Infra Debt
European Equity	1.0					
Global Equity	0.9	1.0				
High Yield Bonds	0.7	0.7	1.0			
Leveraged Loans	0.6	0.6	0.8	1.0		
Inv Grade Credit	0.5	0.5	0.6	0.5	1.0	
PATRIZIA High Income Infra Debt	0.1	0.1	-0.1	-0.1	0.2	1.0

Quarterly return distribution (euro hedged) since 2008^



The class has also benefitted from significant and ongoing bank disintermediation. With post- global financial crisis regulations rendering banks' regulatory capital treatment of sub investment grade debt more punitive, a funding gap for high-income infrastructure debt has emerged, reducing lender competition.

These traits are reflected in the relatively high returns offered, which tend to be superior to other fixed income classes with similar credit ratings, such as high-yield bonds and leveraged loans.

However, it is not just return premia that renders high-income infrastructure debt attractive; its low volatility can offer both insulation during bouts of economic uncertainty and portfolio construction benefits.

Infrastructure assets tend to be supported by a combination of regulatory stability, offtake agreements via long-term contracts – including inflation linkage - and inelastic demand. This can provide long-term cash flow stability for the assets underpinning high-income infrastructure loans, leaving them well-placed to weather economic headwinds. By contrast, other forms of private debt are less equipped to withstand periods of looming downturn. For example, middle-market lending tends to benefit more in economic upturns, when deal activity is elevated and liquidity favourable.

> "High-income infrastructure debt's typically long-term cash flow visibility, inflation protection, economic resilience and market dynamics all place it in a particularly strong position to weather the choppy waters ahead."

The low volatility of the class has also historically imparted a low return correlation with both equities and other fixed income classes, generating favourable diversification traits within a multi-asset portfolio. Indeed, the strong risk-adjusted return profile is reflected in PATRIZIA's high-income infrastructure debt strategy track record, which has exhibited a historical Sharpe ratio (using 3-month EURIBOR as the risk free rate) that is considerably higher than both equities and fixed income classes of similar credit quality.

While high-income infrastructure debt can be subordinated to senior debt, it often still benefits from long-term cash flow stability, robust security and strong covenants. This contrasts with other alternative credit classes such as leveraged loans, which in recent years have been overwhelmingly skewed to covenant-lite issuance. It also benefits from the equity cushion atop the capital structure; the typical equity buffer for PATRIZIA's infrastructure debt portfolio is around 35% to 50% – that is, the enterprise value of the borrower would need to decline by nearly half before lenders were impacted in the event of a default. Additionally, its creditworthiness reflects the underlying assets – often capital-intensive with high barriers to entry and monopolistic traits - against which the loans are secured.

As a result, non-performance, defaults and credit losses have been lower compared to other types of corporate debt at equivalent credit ratings. As a gauge, PATRIZIA Infrastructure has invested in a portfolio of over fifty assets over the past 20 years* and has not experienced a single default or any credit loss.

With more than 1,000 professionals and 28 offices globally, PATRIZIA has been active as a real assets investment manager since 1984. The firm manages more than €58 billion of assets for more than 500 institutional clients in real estate and infrastructure across the risk spectrum.

** As at 30 June 2023.*

PATRIZIA

^Data from 2008 to 2022. Data series used in analysis: European Equity – MSCI Europe Index (EUR Hedged); Global Equity – MSCI World Index (EUR Hedged); High Yield Bonds - Bloomberg Pan-European High Income (Euro) TR Index (EUR Hedged); Leveraged Loans – Credit Suisse Leveraged Loan Index (EUR Hedged); Investment Grade Credit – Bloomberg Global Aggregate Credit Index (EUR Hedged), PATRIZIA High Income Infra Debt – strategy history.