Global Listed Infrastructure
Five myths of Infrastructure

First Sentier Investors

First Sentier Investors has built an impressive track record in the Global Listed Infrastructure asset class.

Despite the extraordinary events since its launch in June 2007 – including the Great Financial Crisis, political upheaval in many parts of the world, and the 2020 pandemic – the strategy has delivered strong, consistent returns through a focus on valuation, quality and active management.

This paper discusses **five common myths** associated with investing in global listed infrastructure.

Listed infrastructure is highly correlated to equities

Infrastructure assets are low growth and will be left behind in rising markets

I already gain exposure to listed infrastructure through traditional equity managers

Infrastructure assets are too highly leveraged and therefore less defensive

Infrastructure is reliant on government funding, which is in short supply

The First Sentier Global Listed Infrastructure Fund (the Fund) has outperformed its benchmark by a cumulative 61% from inception to 31 July 2020 (B GBP Acc, net of fees). The Fund has also surpassed the MSCI World Index (GBP) by 16% over that period.

The strategy was founded by Peter Meany and Andrew Greenup in 2007 and now manages over US$8 billion (as at 30 June 2020) on behalf of institutional and wholesale clients. Since inception, the team has engaged with hundreds of investors on the merits of the asset class.

Annual Performance (% in GBP) to 30 June 2020

Period	12 mths to 30/06/20	12 mths to 30/06/19	12 mths to 30/06/18	12 mths to 30/06/17	12 mths to 30/06/16
First Sentier Global Listed Infrastructure Fund B GBP Acc	**-3.3**	**18.2**	**-0.7**	**17.0**	**28.7**
FTSE Global Core Infrastructure 50/50 Index Net TR GBP*	-5.3	19.8	1.1	13.1	28.1
MSCI World Net Total Return Index GBP	5.9	10.3	9.3	21.6	14.4

These figures refer to the past. Past performance is not a reliable indicator of future results. For investors based in countries with currencies other than the share class currency, the return may increase or decrease as a result of currency fluctuations.

Performance figures have been calculated since the launch date. Performance data is calculated on a net basis by deducting fees incurred at fund level (e.g. the management and administration fee) and other costs charged to the fund (e.g. transaction and custody costs), save that it does not take account of initial charges or switching fees (if any). Income reinvested is included on a net of tax basis. Source: Lipper IM / First Sentier Investors (UK) Funds Limited. *The Fund's benchmark has been the FTSE Global Core Infrastructure 50/50 Index (Net TR, GBP) since 1 April 2015. Prior to that date it was the UBS Global Infrastructure & Utilities 50/50 Index (Net TR, GBP).

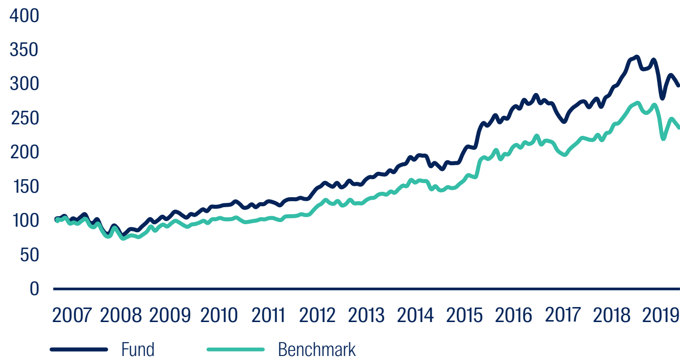
RISK FACTORS

This is a financial promotion for The First Sentier Global Listed Infrastructure Strategy. This information is for professional clients only in the UK and EEA and elsewhere where lawful. Investing involves certain risks including:

- **The value of investments and any income from them may go down as well as up and are not guaranteed. Investors may get back significantly less than the original amount invested.**
- **Currency risk:** The Fund invests in assets which are denominated in other currencies; changes in exchange rates will affect the value of the Fund and could create losses. Currency control decisions made by governments could affect the value of the Fund's investments and could cause the Fund to defer or suspend redemptions of its shares.
- **Single sector risk:** Investing in a single economic sector may be riskier than investing in a number of different sectors. Investing in a larger number of sectors helps to spread risk.
- **Charges to capital risk:** The fees and expenses may be charged against the capital property. Deducting expenses from capital reduces the potential for capital growth.
- **Listed infrastructure risk:** The infrastructure sector and the value of the Fund is particularly affected by factors such as natural disasters, operational disruption and national and local environmental laws.
- **Emerging market risk:** Emerging markets tend to be more sensitive to economic and political conditions than developed markets. Other factors include greater liquidity risk, restrictions on investment or transfer of assets, failed/delayed settlement and difficulties valuing securities.

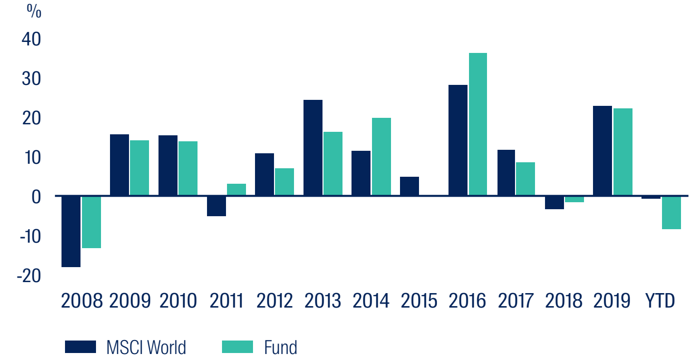
For a full description of the terms of investment and the risks please see the Prospectus and Key Investor Information Document for each Fund.
If you are in any doubt as to the suitability of our funds for your investment needs, please seek investment advice.

Fund Performance vs Benchmark



First Sentier Global Listed Infrastructure Fund (B GBP Acc) after fees and expenses
FTSE Global Core Infrastructure 50/50 Net TR (GBP) from 1 April 2015, previously UBS
Source: First Sentier Investors Monthly data from 8 October 2007 to 31 July 2020

Fund Performance vs MSCI World



First Sentier Global Listed Infrastructure Fund (B GBP Acc) after fees and expenses
^MSCI World Net TR (GBP)
Source: First Sentier Investors Monthly data from 8 October 2007 to 31 July 2020

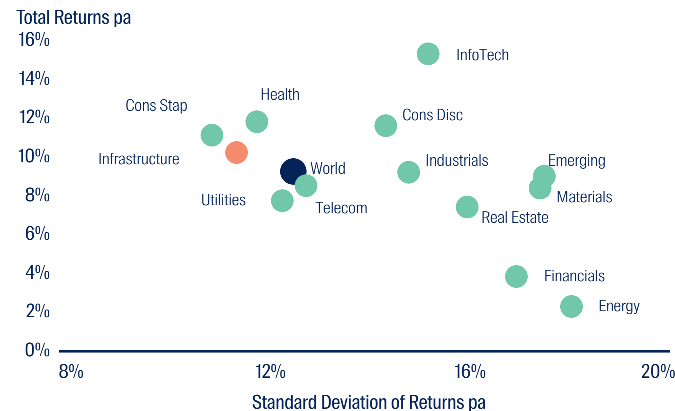
Myth 1:

Listed infrastructure is highly correlated to equities

Infrastructure assets exhibit unique characteristics which have become increasingly relevant in the current economic environment. They provide essential goods or services to society that have a low level of sensitivity to the economic cycle, using contracted or regulated price structures which can provide an inflation hedge.

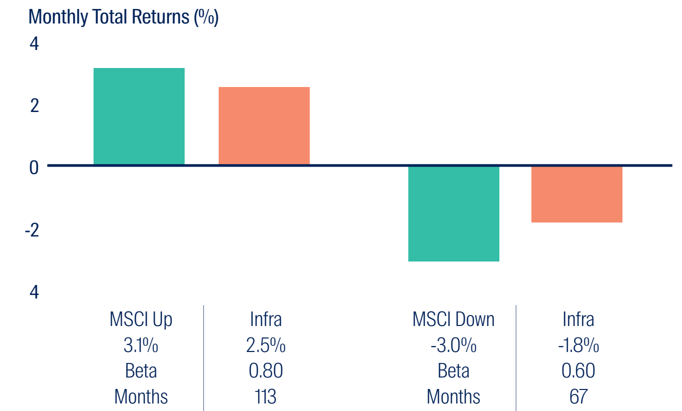
Global listed infrastructure assets tend to complement other typical constituents of an investment portfolio, meaning that allocating listed infrastructure assets to an investment portfolio can improve its risk/return profile. Global listed infrastructure has delivered higher returns with lower risk than global equities over the past 15 years, as illustrated in the chart below.

Global Listed Infrastructure is highly correlated to equities



FTSE Global Core Infrastructure 50/50 Net TR Index GBP from Dec-05, previously Macquarie
MSCI World Net TR GBP
Source: Bloomberg and First Sentier Investors Monthly data for 15 years to 30 June 2020

Global Infrastructure in MSCI World Up/Down Markets



FTSE Global Core Infrastructure 50/50 Net TR Index GBP from Dec-05, previously Macquarie
MSCI World Net TR GBP
Source: Bloomberg and First Sentier Investors Monthly data for 15 years to 30 June 2020

The sector has also proven to be defensive during periods of market volatility. In the past 15 years, the sector has provided 80% of the upside in rising global equity markets but just 60% of the downside in falling markets.

Global listed infrastructure may be suitable for investors who are looking for a more defensive investment during times of market volatility. Global listed infrastructure may also suit investors who are concerned about the impact of inflation and aim to ensure that their investments maintain and grow in real terms.

Myth 2:

Infrastructure assets are low growth and will be left behind in rising markets

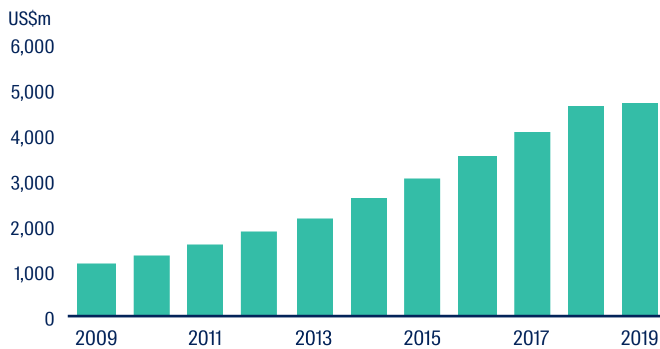
Infrastructure companies often generate growth from structural rather than cyclical drivers. Long-term trends like urban congestion, globalisation of trade, security of energy supplies, and mobility of communications have placed enormous strain on infrastructure networks and will require investment over many decades. Backed by the right business model, this investment has the potential to deliver strong capital growth for investors.

A number of infrastructure sectors are currently delivering double-digit growth due to structural change. Mobile towers have been a beneficiary of the exponential growth in smart phone usage and the resulting pressures on mobile carriers to improve network quality. American Tower has been increasing rental charges, co-locating new tenants on existing sites and building or acquiring new sites. Strict planning restrictions and community opposition to new tower sites represent effective barriers to entry. This underpinned stable earnings growth at a compound annual growth rate (CAGR) of 15% over the 10 years to 2019, with 5G rollout yet to come.

Listed infrastructure also offers exposure to sectors which have the potential to benefit from improving economic growth, such as freight rail. Union Pacific, the largest North American Class I freight rail company, owns and operates a 32,000 mile network of railroads covering the western two thirds of the United States. The company effectively operates as a duopoly in its service territory, alongside Warren Buffet-owned BNSF.

The company was a beneficiary of volume recovery as the US economy improved. Earnings growth was driven significantly by price increases and by improvements in operating efficiency. In total, this combination of cyclical tailwinds and operational improvements enabled Union Pacific to achieve an Earnings per Share (EPS) compound annual growth rate of over 15% pa as markets rose between 2009 and 2016.

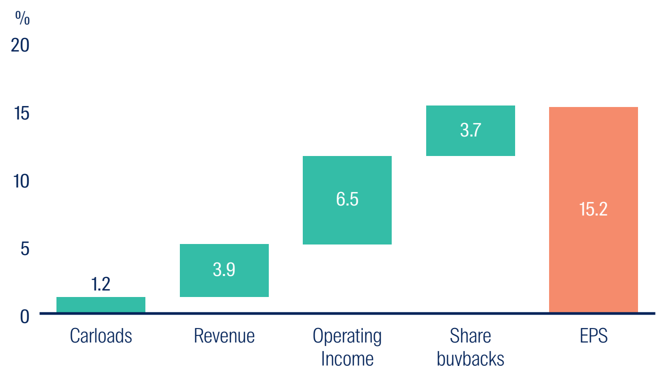
American Tower 2009-2019 EBITDA* growth (US$m)



Source: American Tower, First Sentier Investors

*Earnings before interest, taxes, depreciation and amortization.

Union Pacific 2009-2016 CAGR in EPS



Source: Union Pacific, First Sentier Investors.

Myth 3:

I already gain exposure to listed infrastructure through traditional equity managers

Many global equity managers may hold 2% or less of their portfolio in infrastructure assets, and this exposure could be concentrated amongst a small number of large, well-known utility names. However, much of the alpha generated in our diversified portfolio has come from mid cap stocks, which are under-researched by global equity managers, such as toll roads, oil storage, mobile towers and water utilities.

Listed infrastructure is an emerging asset class that is currently under-researched and not always well understood. This is similar to the situation we saw 20 years ago with listed property trusts, although we believe that the risk/return characteristics of listed infrastructure are superior to those of property, due to long-term structural growth drivers like urbanisation, globalisation of trade, mobilisation of data and security of energy supplies.

It is important to view investments in listed infrastructure from a global perspective. The global listed universe is capitalised at over US$2 trillion, allowing investors to diversify across various infrastructure sectors and geographies and to actively manage key risks.

Infrastructure is a separate asset class for many pension funds, endowment funds, sovereign wealth funds, private banks and multi-managers from around the world. Early movers are typically allocating between 5% and 10% to this asset class.

We have already received strong demand from private investors searching for an alternative to traditional asset classes. They recognise the need to move out of low yielding bonds into equities, but in many cases are wary of volatility. Listed infrastructure, with its combination of possible inflation protected income and the potential of steady capital growth, offers a way of doing this.

Myth 4:

Infrastructure assets are too highly leveraged and therefore less defensive

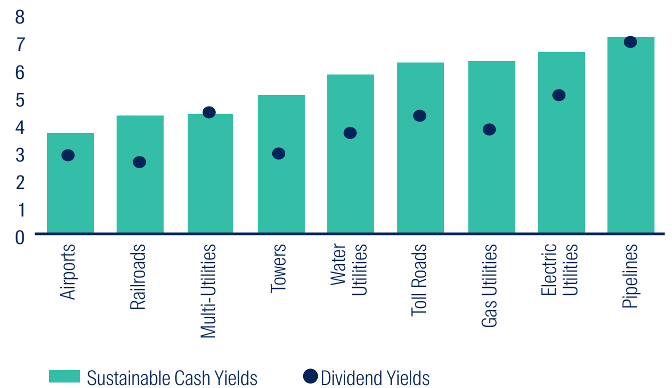
There is no doubt that extreme levels of debt will change the characteristics of equity. A handful of infrastructure stocks, notably in Australia and Spain, created inappropriate capital structures (70-90% leverage) in the mid 2000's when debt was cheap and plentiful. The one thing these companies had in common was poor alignment – investment banks or construction companies were often incentivised on a short-term deal or project rather than on the long-term viability of the investment.

It is important to note that these companies represented less than 5% of our global investment universe. The vast majority of infrastructure stocks are traditional companies, sensibly leveraged (30-50%) and run for shareholders. In recent years, they have strengthened balance sheets by reducing costs and repaying debt. We have also seen widespread refinancing of existing debt, to lock in reduced rates and diversify funding sources.

Some poorly aligned companies took a back-to-basics approach. Australian toll road operator Transurban is a great example. Following changes in the Board and senior management over the last decade, the company raised equity to repay debt, cut the dividend to sustainable levels, halved corporate costs and refocused on its core assets. Having undertaken these measures, Transurban became a key portfolio holding in 2011 and has delivered double-digit annualised returns to shareholders since then.

Today, global listed infrastructure companies are in relatively sound financial positions. Generally prudent balance sheet management across the asset class, with cash yields of infrastructure sectors remaining higher than their respective dividend yields, is illustrated by the following chart.

Infrastructure Yields by Sector



Source: First Sentier Investors

As at 30 June 2020

Myth 5:

Infrastructure is reliant on government funding, which is in short supply

Following years of underinvestment, a significant amount of infrastructure investment is now needed globally. Rough estimates from the Organisation for Economic Co-operation and Development (OECD) suggest that annual investment requirements for road, rail, electricity (transmission and distribution), telecommunications and water are likely to total around an average of 2.5% of world GDP (roughly US$53 trillion to 2030)[2]. Economic growth for a number of nations has been hindered in by critical infrastructure bottlenecks, particularly in the transport sector.

However, while scarce government funding is problematic for societies in need of infrastructure upgrades, it is less of an issue for listed infrastructure companies.

The listed infrastructure investment universe consists of mature, established businesses. These companies provide essential services and generate predictable cash flows underpinned by regulated or contracted business models. Regulatory frameworks often encourage infrastructure companies to invest to maintain or improve their existing assets, and allow them to earn a return on money spent in this way. Under this model, infrastructure companies are incentivised to provide better and more efficient services; with no reliance on government help.

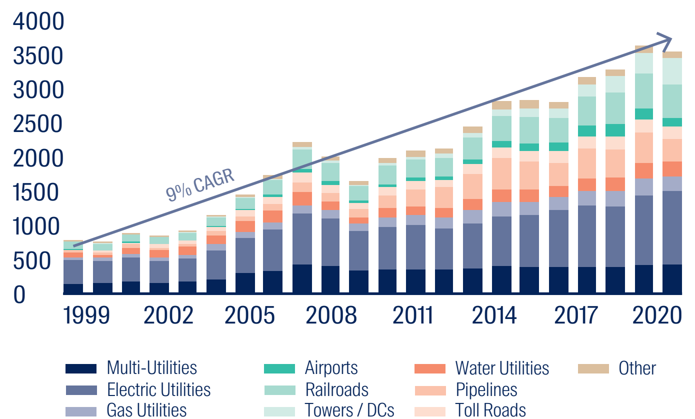
We have seen a lack of government funding lead to promising investment opportunities for listed infrastructure investors. Financially distressed governments have felt the need to divest assets, including valuable infrastructure, to help maintain financial stability. Airports have been listed on public markets or sold to listed companies in Japan, France and Spain; as have ports in China, Germany and Greece. Australian state governments have sold port, toll road and electricity transmission assets to private operators.

A good example of this theme is AENA, the world's largest airport operator. The company handles approximately 200 million passengers per year, primarily at 46 Spanish airports including hubs at Madrid and Barcelona. Previously wholly owned by the Spanish government, a 49% stake was IPO'd in early 2015. Since then the stock has risen strongly as robust passenger growth, limited capital expenditure requirements and improving commercial earnings have propelled its share price higher.

Looking ahead, many infrastructure assets remain in state government hands. The partial sale of WestConnex to a consortium led by Transurban offers a roadmap to the recycling of these assets. Brazil is in the midst of a major privatisation program of toll roads, ports, railroads, airports and utilities.

In addition to this, the listed infrastructure investment universe is benefitting from a wave of corporate restructurings. Many infrastructure assets reside within large, vertically integrated corporations and conglomerates. Companies are increasingly looking to streamline and optimise their capital structures. This has often led to the divestment of infrastructure assets - highly valuable in their own right, but deemed peripheral by a larger entity.

Market Cap $bn



Source: Bloomberg, First Sentier Investors

Combined, these themes of government privatisation and corporate restructuring have resulted in significant expansion, as well as improvements in quality and diversification, for the listed infrastructure asset class in recent years.

[2] OECD 'Infrastructure to 2030' Report.

For further institutional enquiries contact institutionalenquiries@firstsentier.com
For wholesale enquiries contact enquiries@firstsentier.com

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