Improving and expanding the country’s infrastructure involves more than building roads and bridges. While efficient transport systems are vital, without things like reliable communications networks, safe water and a dependable power supply, the economy simply wouldn’t be able to function. This constant need to improve the country’s infrastructure means that many companies stand to benefit throughout the process.

**Global infrastructure investment needs $49.1 trillion through 2030**

Source: McKinsey Global Institute, Bridging Global Infrastructure Gaps analysis.
Data as at 06/2016

- Infrastructure provides the foundation of our daily lives, while for equity investors it also offers a range of attractive investment opportunities.
- The fact that demand for infrastructure is consistent means it is also largely uncorrelated to the ups and downs of the broader economy. That makes it a useful point of diversification for investors.

HOW SHOULD INVESTORS APPROACH US INFRASTRUCTURE?

Peter Santoro
Portfolio Manager
IT IS BIGGER THAN JUST ROADS AND BRIDGES

The demand for infrastructure applies to much more than simply building and repairing roads and bridges, as important as those aspects are. Trends linked to population growth, increasing urbanisation and industrialisation are spurring demand in many areas of the wider infrastructure sector.

A lot of prospects get missed by public infrastructure funds, which narrowly focus on utilities, energy pipelines and transportation assets. This restricted view doesn’t capture the full scope of potential investments. And, just as importantly, it ignores many of the fastest growing areas.

FIVE MAIN THEMES TO INVESTING

Broadly speaking, we see significant opportunities for investment in five main areas of the market:

- Equipment and materials for road, bridge and transit construction, as well as the construction of commercial and residential buildings. This includes the supply chains associated with them.
- Equipment and services for the control, filtration, transportation and monitoring of water and wastewater.
- Telecom equipment and infrastructure.
- Engineering and service providers that build and support energy and industrial expansion.
- Equipment and services to promote energy efficiency.

These are themes where there is not only consistently heavy demand, but also the ability to pay for it – typically through the private sector or public-private partnerships. People often think of infrastructure as something only municipalities and governments pay for, but there is plenty of room for private-sector financing, too.

THE ROLE OF INNOVATION

Two main things drive demand for infrastructure investment. One is a constant need to repair and replace existing road and bridge networks in a developed market like the US.

The second, more interesting driver is social change and the evolution of technology, which is where we think there are some big opportunities.

A lot of this often goes unrecognised. Cell phone towers are replacing traditional telephone poles. Natural gas pipelines and liquefied natural gas (LNG) facilities are displacing coal trains. Underground utility networks are being built instead of above-ground electricity pylons and cables. All these changes create demand for significant infrastructure investment.
THE TRUMP IMPACT ON INFRASTRUCTURE

One of Trump’s most eye-catching proposals is a plan to spend $1 trillion on infrastructure. Not many of the specifics are known yet, but it’s likely to be based on tax credits to make it cheaper for private firms to finance projects that can generate a positive return. Trump has also decided to press ahead with some energy pipelines, like the Keystone XL project and the Dakota Access pipeline.

But that doesn’t mean infrastructure investment is a fad or a short-term opportunity based solely around the current president’s agenda. This is a long-term secular theme that started well before we knew Trump would be president and which is going to play out over several decades.

In fact, infrastructure investment is one of the few issues with bipartisan support in Washington, which means it is a strong growth opportunity regardless of who is in office. President Obama signed the US Highway Transportation bill in December 2015, which provides for $305 billion of investment over five years. Hillary Clinton also ran on a platform that advocated greater infrastructure investment, so this is something that politicians on both sides of the aisle can agree on.

INVESTMENT TIMEFRAMES

There are often short-, medium- and long-term winners in infrastructure projects. For example, when it comes to building a highway, cement makers should benefit in the short term. The big winners longer term will be the companies that will benefit from those better roads and bridges. In terms of energy projects, it takes a long time to build a pipeline. But in the short term, the ditch diggers, the services companies and contractors will gain from more activity. In the longer term, some energy companies will benefit from using the pipelines to reach their customers.

This means there are both short- and longer-term opportunities for investors. Another attractive aspect is that a lot of infrastructure projects are long-dated – they can take years to build and generate revenues for decades – and they also have heavy cash components. These factors mean they can be useful inflation hedges.

BOTTOM LINE

Infrastructure investment provides a unique combination of above-average secular growth and long-dated investments with stable cash flows and income streams. This powerful combination of capital appreciation and sustainable income provides a basis for long-term investment success.

The need for continued improvements to the country’s infrastructure is widely recognised, which means that investment is constantly happening. The fact that demand for infrastructure is consistent means it is also largely uncorrelated to the ups and downs of the broader economy. That makes it a useful point of diversification for investors.
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