

One catch: popularity of the asset class in this crisis could mean demand outstrips supply

Infrastructure, that solid and safe refuge

MARKET WATCH
STEPHEN BARBER



There is something very attractive about infrastructure as an asset class. It is real for a start, funding sizeable projects from rail to roads, bridges to tunnels, public services to communications, ports to airports, power to water. It is also truly international, encompassing not only Europe and North America but also – and more importantly – the rapidly growing emerging economies of India, China and Brazil. But despite its somewhat defensive nature, economic conditions can still worry investors.

In these lean economic times, with price rises eating into investment performance everywhere, infrastructure is inflation-busting and a haven against weak equity markets: it combines income and growth and offers solid, durable, predictable returns over the longer term. These funds enjoy returns from projects irrespective of what is going on in the stock market or indeed the economy. After all, even in recession police stations still function, children go to school, airports remain open and drivers cross toll bridges. These reasons alone make the sector suitable for inclusion in most diversified portfolios, but only partially explain the clamour to invest.

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While infrastructure funds themselves tend to suffer from early underperformance (because the cash takes time to find its way into projects) and it has to be said that fund prices have risen considerably over the past year or more, there is a very big reason for the interest. China alone, which has seen economic growth in double digits for a decade, is spending 10 per cent of its GDP on infrastructure and it is estimated that more than \$20trn (£11.4trn) will be spent worldwide in the sector over the next decade. Meanwhile the OECD has predicted that a whopping \$53trn is needed by 2030 to keep pace with development goals. That is a lot of investment with solid, foreseeable returns.

But the news isn't all rosy. Infrastructure has not entirely avoid-

ed the effects of the credit crunch, with some funds divesting to reduce the average weighted cost of capital. That is, feeling the squeeze, they are reducing debt. That said, throughout 2008 infrastructure has continued to raise cash relatively successfully despite the otherwise hostile funding environment and this year might indeed turn out to break records for the sector.

The economic environment is something of a double-edged sword for infrastructure because it has two contradictory effects. The first is that it makes the sector more attractive as risk-conscious investors eschew the more volatile alternatives in favour of good, solid long-term returns. This is especially true of the mighty pension funds in Europe and the US, which have shown particular interest, but it can also be seen among retail investors and private equity.

However, slowing economic growth in East and West alike inevitably applies pressure to the brakes of some of these projects. The result could well be demand for the asset class outstripping timely supply of projects. That's something we see little of these days: too much liquidity.

Stephen Barber is head of research at Selftrade