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From deglobalisation to decarbonisation

Global mega-trends are transforming the transport infrastructure opportunity, our four industry professionals tell Amy Carroll and Kalliope Gourntis

Transport infrastructure, and the global passenger movements and supply chains that underpin it, has been hit by a series of existential shocks over the past five years. Firstly, the covid pandemic caused unprecedented levels of disruption, then war in Ukraine sparked a reworking of supply chains along geopolitical lines. Now, President Donald Trump's rollercoaster trade war is threatening to upend the sector once again.

The ultimate impact of US tariffs remains unclear, of course, with the battle still being played out in intergovernmental negotiations and the courts. But infrastructure investors are certainly watching developments closely.

"The vast majority of our transport portfolio is in Australia and so has experienced no effects so far. Given the three-month freeze on US tariffs, global GDP hasn't been impacted yet. However, we're watching closely," says Nicola Palmer, partner and head of transport at QIC. "If China is hit badly, that will immediately flow through to Australian GDP and Australian ports, airports and road investments. Australia is a commodity driven economy connected to the Chinese economy. But for now, most of the volatility has been restricted to the US."

Uncertainty, in itself, is a challenge. But as long-term investors, infrastructure managers are used to preparing for the unknown.

"If you're investing in a transport infrastructure asset, you need to assume that there will be a downturn at some point in your 10-year-plus ownership period and plan appropriately," says Palmer. "If we're investing in a port, for example, we will always ensure we have customer diversification in order to mitigate macro risk. Having said that, if there's a material global recession, your ability to drive goods through a port or passengers through an airport is limited, so you need to make sure that the deal is structured in such a way that it's able to weather any storm."

"I completely agree. Of course you need to anticipate blips over time, but as long as you have a strong, underlying thesis, transport assets should not be overly vulnerable to an economic downturn," adds Infracapital managing director Thomas Crawley. "We're currently investing heavily in rail leasing, for example, which is relatively uncorrelated. We're also invested in rail freight, which has the benefits of underlying diversification at a customer level, and in EV charging and the broader electrification of mobility, which is supported by the mega-trend of decarbonisation."

Furthermore, any form of dislocation also spells opportunity. Trump's tariffs are intensifying a nearshoring trend that originated during the pandemic, creating investment need around the reconfiguration of the global supply chain.

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Thomas Crawley

Managing director, Infracapital

Thomas Crawley joined Infracapital in 2015. He has more than 17 years' infrastructure investment experience across multiple sectors and jurisdictions. Crawley previously worked at Ontario Teachers' Pension Plan and Map Airports, beginning his career at Macquarie.

Matthew Norman

Global head of infrastructure and EIG advisory, Crédit Agricole CIB

Matthew Norman has more than 20 years' infrastructure and energy industry experience. He previously worked in the investment banking and wealth management divisions at Banque Indosuez.

Roland Kaufmann

Head of transport and senior investment manager, Reichmuth Infrastructure

Roland Kaufmann joined Reichmuth Infrastructure in 2020. He leads all relevant investments in the transportation sector. He previously worked at Aurelius Growth Equity and Prime Capital.

Nicola Palmer

Partner and head of transport, QIC

Nicola Palmer joined QIC in April 2022. She leads transport origination for the firm and has more than 30 years' experience of infrastructure investment across Australia, the UK and Europe.

uncertainty may ultimately create further opportunities in the transport and logistics sector," says Matthew Norman, global head of infrastructure and EIG advisory at Crédit Agricole CIB. "This is particularly apparent given the trend around nearshoring and enhancing supply chain resilience, which started during covid and is now gathering further momentum given current geopolitical complexity. That will be a major theme for investment going forward."

Roland Kaufmann, head of transport and senior investment manager at Reichmuth Infrastructure, agrees. "Reshoring or nearshoring has become a priority for most companies in Europe and that's having implications for the way that transport infrastructure is configured. For example, we're seeing a move away from harbour links and towards transcontinental assets, as businesses prepare to shift more product across Europe, instead of shipping it to or from overseas."

US transport and Trump

While the US is feeling the impacts of tariff uncertainty more acutely than other markets, the region still offers interesting opportunities for investment

One of the continuing US projects is the Managed Lanes programme, which is creating opportunities in the toll road sector. It began life in Texas, California and Virginia and now is expanding to other states.

"Historically, it's been hard for private investors to access traditional transport assets in the US because so much has remained under state or local authority ownership. The Managed Lanes programme is providing the private sector with interesting greenfield opportunities," says Crédit Agricole's Matthew Norman. "Ports is another area where we've been active in the US."

Furthermore, the US airports sector is also starting to attract attention. "The model is different to Europe and Australia in that airport investment in the US tends to be done in discrete or bespoke assets and not full privatisation of operations. But there have been one or two deals that have taken place, and I expect to see more in the future."

Tariffs could disrupt momentum here but there are long-term drivers at play. "There's a huge need for enhanced transport capacity in the US. Just look at the congestion that exists around many of the very large cities," says Norman. "Irrespective of what happens in the short term, I think the long-term thesis for investment in US transport remains strong."

Traditional transport

The transport infrastructure growth story remains highly attractive on a global basis, despite macro volatility. "Traditional transport assets offer a compelling combination of dividend yield and growth. Growth is being driven by GDP and population growth, as well as opportunities to invest capex in warehousing, wharfage, dredging, land acquisition, and runway and road extensions," says Palmer. "Our airport, ports and road assets typically double EBITDA every 10 to 15 years."

Norman adds that quality transport assets also have a scarcity value. "These assets are hard to come by when you compare this to the abundance of assets in the energy sector, for example. That means there tends to be a favourable backdrop for sponsors considering their strategic options," he explains. "There's also a huge need for investment. Take the airport sector, for example. There's a significant capex backlog after an almost four-year pause, post-covid. That, combined with a strong traffic recovery profile and an interesting sustainability story, makes for some very interesting dynamics."

Similarly with ports, there is a significant investment need, both to tackle emissions and to boost capacity. "The electrification of port infrastructure is a key theme, as is investment in low carbon fuels and increased automation," says Norman. "Investment in port infrastructure simply hasn't kept up with the increase in global shipping and container demand, as well as the decarbonisation mega-theme, which means there's a huge opportunity that exists today."

Meanwhile, the rail sector, which has historically sat on the cusp of core infrastructure, is also commanding a lot of attention. "There's a significant opportunity on the rail freight side where we're invested in operators that are moving critical goods around the country. That transportation network is the backbone of the economy," says Crawley. "At the same time, we're playing into the decarbonisation drive, by moving goods – and people – off road and onto rail, while also replacing diesel locomotives with bi-mode trains."

Transport adjacencies

While core transport infrastructure remains attractive, the reality is that assets are few in number. A lot of managers are therefore exploring opportunities in adjacent sectors.

Reichmuth Infrastructure has invested in a helicopter leasing platform, for example. Kaufmann says that Sentinal, which focuses on missions related to public infrastructure

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Infracapital

such as search and rescue, firefighting and supply related services, falls firmly within the firm’s definition of infrastructure.

“We don’t define infrastructure in terms of bricks and mortar but rather by investment characteristics. We look for assets that are backed by long-term contracts and that have high cashflow visibility and inflation protection, together with high barriers to entry,” Kaufmann explains. “Helicopter leasing may not be traditional infrastructure, but if you have a long-term lease or concession with a strong counterparty, providing essential services in terms of emergency medical services and firefighting, for example, it certainly fits the bill.”

Infracapital has also recently acquired a mission-critical aerial services business called SAF Aerogroup. “From our perspective, this certainly

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> **ROLAND KAUFMANN**
> **Reichmuth Infrastructure**

represents essential infrastructure. Firefighting, for example, is becoming increasingly critical in Europe against the changing climate backdrop. SAF Aerogroup is also providing emergency medical transport services, addressing changing healthcare needs driven by demographic changes, and facilitating search and rescue operations. This is a business that has long-term, inflation-linked contracts backed by public authorities, while a need for specialised helicopters is a barrier to entry," says Crawley.

Palmer agrees with the premise: "If you have a monopoly position, strong pricing power, long-term contracts and high levels of asset ownership, then the cashflows you're likely to generate will be as high as those from core transport infrastructure, whilst the returns are likely to be even higher.

"We're also looking at the emergency services sector, as well as electric buses, electric depots and containers and logistics equipment. It's important to remember, however, that while some of these assets will have appropriate infrastructure characteristics, not all will. You can have one ferry business that has a monopoly position and long-term contracts, for example, while another might be operating on a highly contestable route."

Norman says: "I would add that some of these adjacent sectors may actually be more resilient than certain core assets. Airports were hit hard by covid, but certain critical services within airports demonstrated less volatility, for example. Service transportation vessels in the offshore wind sector is another interesting area worth mentioning, where the bank has been active."

LPs also seem to be on board with investment in transport adjacencies. There are some isolated exceptions, however. "Investors may be concerned about high levels of GDP exposure when it comes to investments such as container or wagon leasing, but the reality is that these are long-term contracted assets, with good counterparties," says Palmer, who has invested extensively in the space with a previous GP. "I think it's only a matter of time before investor concerns are allayed."

EV charging focus

Another area that's dividing opinion, meanwhile, is EV charging. Some managers are embracing the sector, while others are deeply sceptical.

Infracapital is a firm believer. "From our perspective, EV charging is essential infrastructure. We were a relatively early mover into the sector and have invested in the Nordics, one of the most developed EV markets, and in GRIDSERVE in the UK. It's crucial for meeting decarbonisation objectives, which means that government support is in place to drive EV take-up," says Crawley.

"It's true that the path has not always been smooth. There have been some changes around the edges to government policy in both the UK and the EU, but the end goal remains the same."

Crawley explains that more than 20 percent of all new UK car registrations in May involved battery electric vehicles. "That's an increase of around 25 percent on last year. This isn't the world of regulated utilities and long-term contracts, but there are business models out there that offer the risk profile that we look for."

Palmer is less convinced. "I would say that the jury is out on the vast majority of EV charging infrastructure. This is an industry that's susceptible to overbuild and low levels of utilisation and, when it comes to street level charging, there are no real barriers to entry," she says.

Infracapital, however, ensures high barriers to entry, through a combination of premium enroute locations, and a focus on locations where there is a need for rapid and ultra-rapid charging technologies, according to Crawley.

"Location is key, but you can also mitigate risk in other ways. There are operators that have moved from a B2C to a B2B model, for example, to diversify and de-risk their business models," adds Norman.

Kaufmann, meanwhile, adds that technology risk is significant in this sector. "Charging technologies still exhibit a steeper technological learning curve, potentially being replaced every two to three years. That's why we are currently staying away from this space. We're not precluding it as an area for investment, but only if the investment characteristics are right," he says.

"We really like the tailwinds driving the low carbon mobility sector but let's be clear, while there's some level of regulatory support, the EV charging landscape remains early in its life cycle and is largely evolving as a commercial proposition with full market risk in Europe," adds Norman. "Discipline is therefore essential but, as we have seen in other similar situations – notably fibre – that discipline is not always applied."

The decarbonisation journey

EV charging is only part of the transport infrastructure decarbonisation story, of course. "There's a huge need for decarbonisation spend across the transport infrastructure space and that represents a vast investment opportunity," says Crawley.

Decarbonisation investment serves the dual purpose of greening the transport network while generating cost savings. "At the moment, the focus is primarily on the electrification of light vehicles. This involves capex, of course, which is good for infrastructure investment. Opex costs for fuel and maintenance, meanwhile, are often lower, resulting in higher EBITDA margins," says Palmer.

There's a revenue enhancement angle as well. "We're seeing a lot of customers proactively seeking out counterparties that can demonstrate strong ESG credentials," says Crawley. "Our inland terminal business, Inland Terminal Group, has a contract with Nike, for example. It was really important to Nike that they had a low-carbon shipping option available."

The decarbonisation story becomes more complex, however, when the focus moves to the heavy vehicle and long-haul sectors. "There, you need biodiesel or sustainable aviation fuel, which remain inherently more expensive," says Palmer. "The decarbonisation of those sectors will come, but the economic benefits are not there in the way that they are with the electrification of light vehicles today."

Kaufmann, however, says that with up-to-date propulsion systems and ship designs, opex costs are already lower than older diesel-powered alternatives. "There's also obsolescence risk to take into account."

Infrastructure investors' social contract is also at stake, says Palmer. "We need to provide facilities to enable airlines to switch from traditional fuels to SAF, otherwise we risk losing our social license to operate."

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