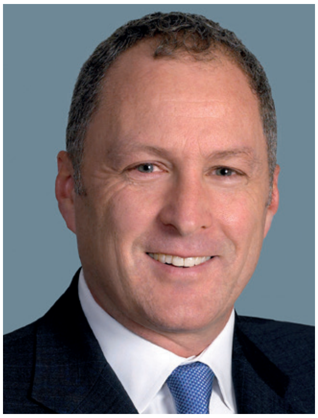
KEYNOTE INTERVIEW

Digitalisation and decarbonisation



Recent macroeconomic challenges have done little to derail the trends driving growth in infrastructure investment, explains Stephen Dowd, CBRE's chief investment officer – private infrastructure strategies

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The Biden administration signed into law the Infrastructure Investment and Jobs Act in November 2021, authorising $550 billion in new infrastructure spending in the US over the next five years. In the months since the bill's passing, excitement continues to build around ways the Act could revitalise infrastructure in the US and the investor returns it could support.

Stephen Dowd, chief investment officer for private infrastructure strategies at CBRE Investment Management, has more than three decades of experience in infrastructure, having invested in assets across Europe, Asia, Australia, South America and the US. *Infrastructure Investor* asked him about recent developments in the asset class, and the investment trends worth keeping an eye on.

Q Where is investment focusing right now?

The biggest themes are around digitalisation and decarbonisation – those run all the way through infrastructure. The growth of digital infrastructure over the last five to six years has been monumental. Investments in data centres and fibre-optic networks have both seen a lot of uptake. These recent investments in new forms of digital infrastructure have joined the ranks of pre-existing assets that have long been popular among investors, like mobile phone towers. As more and more sectors embrace digital solutions, it is likely that digital infrastructure will continue to see greater levels of investment. The hardware and software that are essential to the modern, global economy require new infrastructure developments to support them.

We are also seeing digitalisation become embedded further in more traditional areas of infrastructure. The increased use of data to optimise the performance of infrastructure investment is a prominent trend among investors.

In tandem, decarbonisation has been a priority for some time. Renewables are part of an ever-expanding asset class for investors to consider.

Although in the world of US infrastructure investment, 2021's Infrastructure Investment and Jobs Act remains a focus, the country's more recent Inflation Reduction Act may turn out to be just as impactful. The latter earmarks $369 billion to ease the transition to more sustainable energy sources. This will only increase the attractiveness of renewable infrastructure assets.

All developed markets have very strong tailwinds for renewables. Decarbonisation is also growing in prominence for traditional infrastructure assets in terms of reducing emissions, implementing electrification and introducing carbon footprint measurements. This makes existing assets more compatible with longer-term net-zero strategies.

Q In what way is digital infrastructure set to play a larger role within infrastructure investment?

Investments in data centres, fibre-optic networks and mobile towers represent much larger components of infrastructure investment than they did five years ago. While this may still be a smaller subsector than more traditional infrastructure assets, there is still plenty of activity being generated.

Digital is now well established as part of the infrastructure landscape. Overall, the digitalisation of society is driving the growth of related assets. Pretty much every industry, from healthcare to hospitality, is now data-driven, and so demand for data – whether this concerns storage, transfer, or management – continues to be strong and will be for the foreseeable future.

Electrification is another development that is driving investment in digital infrastructure. Within the electric vehicle market, greater investment in physical charging infrastructure is needed, of course, but digital infrastructure to support the extra data created will also be key, as will new software solutions. These developments, and others like the Internet of Things, smart cities and digital twin technology, will all provide the impetus for investors to support digital infrastructure investment.

Q How prominent a role are ESG considerations playing within infrastructure investment?

A major part of ESG trends is undoubtedly the environmental "E" factor, but there are other elements worth considering from an investor standpoint.

We have seen the number of requests around ESG from investors explode over the last two years; they are looking for more specifics rather than just a general statement around ESG priorities, so partners and managers must embed ESG principles more deeply within their strategies.

Even as environmental considerations grow in importance, investors continue to value social and governance factors as well. Infrastructure investment may not have always been responsive to ESG inputs but changes over the last few years have seen investors become more programmatic about

Q What will the Inflation Reduction Act do for infrastructure?

The Act, signed into law in August, will reinforce clean energy supply chains in the US. It is looking to curb inflation and reduce the federal government's deficit, but its impact on clean energy could be just as important.

The Act guarantees $369 billion of support for clean energy and climate change mitigation initiatives across the US. By 2030, this investment will lead to the creation of 950 million solar panels, 120,000 wind turbines and 2,300 grid-scale battery plants.

The creation of a "green bank" to support public-private partnerships that encourage emission reduction will mean that infrastructure investment in ESG-focused projects is likely to become more attractive in the US.

how they implement their ESG strategies. They are becoming more specific about measuring emissions, social outcomes, governance issues and community relations.

It is worth noting as well that ESG principles are completely consistent with a well-performing infrastructure investment strategy. The prominence of these issues is growing all the time. As a good investor, you should always be focusing on ESG factors, but this focus is definitely becoming more pronounced.

Q What sort of challenges do infrastructure investors face in meeting their ESG goals?

One of the main challenges for infrastructure investors is the fact that different organisations have different approaches to measuring ESG outputs. This inconsistency can create difficulties for investors as there is no single standard. However, at CBRE, we focus our measurements on the metrics favoured by the groups we are members of.

There is a bit of an alphabet soup when it comes to measuring the environmental impact of assets. In recent times, a number of different rating providers have emerged, each offering unique approaches and frameworks for measuring ESG impact – these can add another layer of complexity for investors to manage.

For example, ESG scoring might consider emission levels, water usage, environmental management, workplace safety and numerous other factors. They may each also have different levels of importance attributed to them.

However, there are a few recognised standards that organisations and investors have gravitated towards. It is up to partners and managers to choose from a range of respected organisations offering ESG measurements and explain to investors what the benefits of those are. This provides some guidance for investors even if the industry is lacking a global standard.

Q What impact are recent macroeconomic challenges having on infrastructure investment?

The three biggest macroeconomic factors affecting infrastructure investment are energy commodity prices, inflation and interest rates. With regard to energy prices, energy security has become a major issue of late too. The recent energy crisis has left investors, companies and entire industries facing a dilemma: how do they meet energy needs, when the most secure, reliable sources of energy may run counter to their stated ESG goals?

In the short term, energy security is more pressing, so governments and investors may decide to support certain energy sources regardless of their carbon emissions. Looking longer term, they will likely want to create infrastructure that ensures they are not so dependent on problematic energy sources. Diversifying energy with more distributed solutions, such as renewables and battery power, will obviously affect the flow of infrastructure investments.

Recent increases in prices emphasise the importance of inflation resilience for infrastructure investments. Although we have just come out of a prolonged period of low inflation, inflation protection should always be an important part of an infrastructure investor's list of things being looked at before they choose which assets to back.

Looking at the recent rise in interest rates, this will have an impact on refinancing and investor evaluations. How investors and managers put together capital structures for long-term resilience and duration risk will be affected by interest rate movements.

Every manager is paying attention to the three factors of energy pricing, inflation and interest rates. The good news is that the current macroeconomic environment is one where infrastructure should perform well. It actually becomes more appealing to the LP base.

While liquid assets may have retreated somewhat, the appeal of infrastructure has continued to be strong. Whatever we have witnessed within the macroeconomic market, this has only reinforced investors' commitment to infrastructure.

Q What is the global outlook like for infrastructure projects and where do you see the main opportunities residing?

There is certainly an interesting dynamic with regard to power generation. For a while, investors have been very wary of any assets that were connected to fossil fuels, which made it quite difficult for managers to invest in traditional infrastructure.

The recent emphasis on energy security has changed things a little, however. There is still a long-term movement away from fossil fuels, but investors looking for short-term returns are not quite so dismissive as they may have been regarding assets with sizeable carbon footprints.

Having said that, many of the main opportunities within infrastructure investment reside with assets that have decarbonisation as a core focus. Digitalisation will also continue to present interesting opportunities for investors. Both trends are visible across infrastructure generally because of long-term factors that are driving infrastructure growth.

Even the recent macroeconomic challenges that we have been experiencing can be reframed as positives for infrastructure investment. It proves the stability and resilience of the asset class – something that infrastructure has shown over a prolonged period of time. If you were a new investor entering this sector, I think focusing on the long-term trends of decarbonisation and digitalisation would be to your advantage. ■