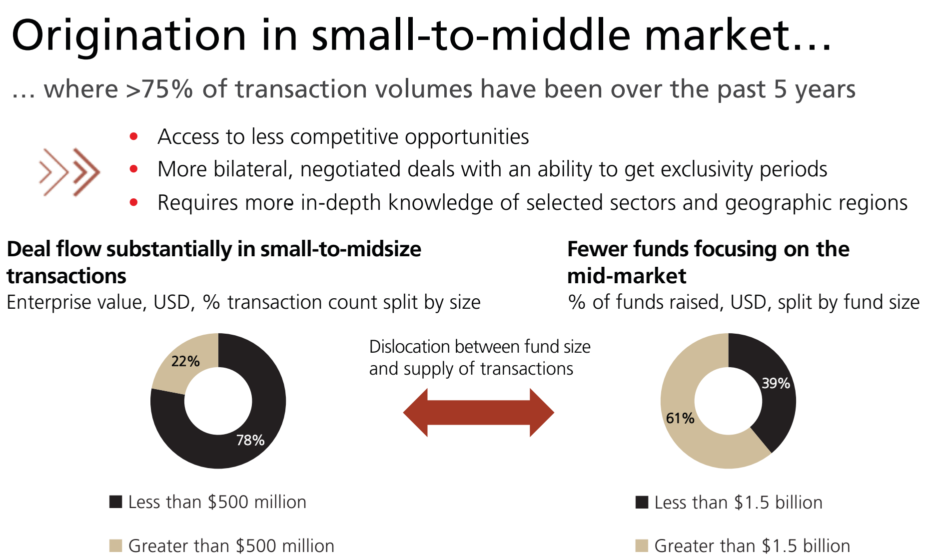
UBS Asset Management

A fork in the road ahead

A Q&A with Perry Offutt

Given the rise in asset values, where are the best opportunities in infrastructure?

While the relative resilience of infrastructure assets, coupled with a low-interest-rate environment, have led to higher valuations, we continue to find significant opportunities. In short, managers either focused on smaller-scale or extremely large investments within infrastructure have the ability to avoid competitive auctions, which often leads to better risk-adjusted returns.



Sources: UBS Asset Management, Real Estate & Private Markets; Preqin, average size 2014 to August 2018

Specifically, we believe that there is currently a compelling opportunity in the lower-middle market, given the number of investment targets that we have identified relative to the capital raised for this segment of the infrastructure market. We have found that by building relationships with developers, who are interested in partnering, or corporations interested in divesting small, noncore assets, bilateral discussions are often preferable for both sides. As a result, each party can focus on bespoke transaction terms and maximize execution certainty, which is difficult via a standard auction process. For example, there are numerous smaller renewable platforms that are seeking capital to build out their pipeline. A partnership between infrastructure capital and these developers at the project level can address each party's goals in the short term, as well as create a longer-term relationship for future projects.

How will the COVID-19 crisis continue to affect the infrastructure sector?

First, we believe in the importance of diversification within an infrastructure portfolio. The COVID-19 crisis has affected specific subsectors in very different ways, which differ from a typical recession. Pre-crisis, we had strong conviction that energy transition and digitalization were positive tailwinds for the sector, and COVID-19 has only helped to reinforce those views.

Specifically, we are focused on the three Ds — decarbonization, digitalization and demographics — which, when combined with the key attributes associated with infrastructure investments such as high barriers to entry and imbedded inflation protection, can lead to long-term growth opportunities with predictable cashflows. Therefore, we expect telecommunications, renewable energy and social infrastructure to continue to perform well in the years to come.

Is transportation a sector to avoid, or are there opportunities?

Clearly, the transportation sector was at the center of this crisis. However, the subverticals are recovering at different rates. Airports, which lost 95 percent of their traffic volume during the lockdowns, mass transit and cruise lines have all struggled to recover. Meanwhile, roads, rail and ports have fared much better, with many assets operating at or close to pre-COVID-19 levels.

Over the long term, we believe that traditional transportation assets belong in an infrastructure portfolio to create the appropriate level of portfolio diversification. However, in the shorter term, it is difficult to predict when and if historical usage will return to certain areas of transportation, such as airports and managed lanes. Therefore, these areas are not a primary focus of ours at this time.

Despite being unpopular now, however, these assets have historically had high, stable EBITDA margins and will continue to be essential post-COVID-19. For example, we think that investors taking a blanket unfavorable view of airports may miss opportunities to secure attractive risk-adjusted returns. For most of the transportation sector, these continue to be essential assets, even in the short term, and have shown to be resilient during this crisis. These assets are exposed to further lockdowns, but they should rebound quickly once restrictions are eased, as demonstrated to date.

How can private capital best partner with government entities to rebuild an aging infrastructure?

It is well documented that trillions of dollars are needed to repair the aging infrastructure in the United States (e.g., transportation, water/wastewater or social infrastructure), at a time when most municipalities are experiencing budget shortfalls. As a result, there should be significant opportunities for private capital to help fund a portion of this need. However, historically it has been a challenge to execute on public-private partnerships within the United States.

We believe the best way for this to change is to focus on true partnership opportunities between the private sector and governmental organizations, where there can be a win-win-win situation — a win for the end-user, for the governmental agency and for the private investor. Once political will is in place, it would be up to the infrastructure capital, teamed with construction/operating firms, to build or replace critical infrastructure in a more innovative and cost-effective manner to demonstrate the value that the private sector can bring.

Fortunately, infrastructure is one area that tends to get bipartisan support, given the potential to create jobs and improve local economies. This gives me hope that the U.S. federal government will find ways to encourage the involvement of private capital.

UBS is a leader in sustainable investing. How does that focus translate to infrastructure investing?

The 3 "Ds" to drive future infrastructure pipeline

The sector has evolved significantly over the past 10 years. But what will it look like in the next decade?

Decarbonization

"The unprecedented stimulus program — along with a revised budget for the next seven years — aims to **accelerate the transition to clean transport, increase energy savings** and boost the production of **renewable energy.**"

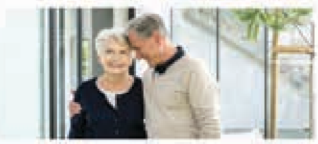
Ursula von der Leyen, President of the European Commission

Digitalization

"There will be almost 30 billion connected devices by 2023, **more than 3x the global population** and up from almost 13 billion in 2018."

World Economic Forum, "Data is the new gold. This is how it can benefit everyone — while harming no one," July 2020

Demographics



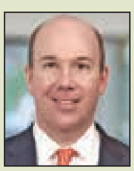
"At present just under 11% of the world's 6.9 billion people are over 60. Taking the UN's central forecast, by 2050 that share will have risen to 22% (of a population of over 9 billion), and in the developed countries to 33%. To put it another way, **in the rich world one person in three will be a pensioner; nearly one in ten will be over 80.**"

***The Economist*, "A slow-burning fuse," August 2018**

Our firm's sustainability strategy is guided by our goal to be the financial provider of choice for clients wishing to mobilize capital towards the achievement of the United Nations' Sustainable Development Goals (SDGs) and the orderly transition to a low-carbon economy. We work toward this goal by integrating sustainability into our mainstream offerings, through new and innovative financial products with a positive effect on the environment and society, and by advising clients on their philanthropic works.

These principles clearly also apply to our infrastructure strategies. Further, our focus on environmental, social and governance (ESG) factors reduces risk at our portfolio companies and for our investors. ESG is firmly embedded into our processes from origination through to asset management. Infrastructure assets are esoteric in nature, and, therefore, it is difficult to apply standardized reporting and measurement frameworks to them. This is why we have engaged an external consultant for our newest infrastructure equity offering. Our ESG consultant measures the carbon footprint and helps to identify measurable KPIs for each investment. We make a commitment to improve these KPIs over the holding period for our investments.

CONTRIBUTOR



Perry Offutt

Managing Director

Head of Infrastructure Americas

CORPORATE CONTACTS

Pat Cunningham
Head of Infrastructure Investment Specialists Americas
+1 (212) 713-3908 | pat.cunningham@ubs.com

Kate Greene
Senior Capability Specialist
+1 (212) 821-6557 | kate.greene@ubs.com

UBS Asset Management, Real Estate & Private Markets
1285 Avenue of the Americas, New York 10019
www.ubs.com/repm

CORPORATE OVERVIEW

UBS Asset Management

UBS Asset Management's Real Estate & Private Markets (REPM) business actively manages investments of more than USD 114 billion globally and regionally within Asia Pacific, Europe and the United States, making it one of the largest asset managers in real assets worldwide. Our capabilities reach across the risk/return spectrum, ranging from core to value-add and opportunistic strategies. We offer both direct real estate and infrastructure equity and debt investments, or indirect exposure to leading real estate, infrastructure and private equity managers. Investors can access our diverse product range across open- and closed-ended private funds, investment trusts, listed funds, REITs, and bespoke separately-managed accounts.