Research Blast

US election and the impact on infrastructure – November 2020

Under a Biden presidency, the next wave of infrastructure investments will have greater emphasis on ESG issues

The extent of this will depend on the outcome of the Senate race, although historically, there has been more bipartisan support for clean energy than headlines suggest

Private infrastructure funds, equipped with over USD 200 billion of dry powder, will likely play an important role, especially given government budget constraints

Revival of US infrastructure under Biden?

Former Vice President Joe Biden has been declared the next President of the United States. Assuming that the current results hold despite President Donald Trump's legal challenges, Biden will push for his USD 2 trillion climate plan that he touted during his campaign. Infrastructure spending is the tried-and-true way to alleviate unemployment and kick-start stagnant economies. How *green* the next wave of infrastructure spending is will depend on the final outcome of the Georgia Senate runoff elections scheduled for 5 January 2021.

For many years, infrastructure has been something that politicians like to talk about. But when it comes to actually putting federal dollars to work, it is often overshadowed by other topics such as healthcare, defense, social security, education and social issues. The current economic crisis has provided a rare opportunity to hit the reset button, and reprioritize long-term development goals. Unlike past infrastructure spending plans, the next wave of investments will have a greater emphasis on ESG issues under a Biden presidency.

However, if Republicans retain control over the Senate, they will pose a challenge to Biden's ambitious plans. The silver lining is that there has historically been more bipartisan support for clean energy than what the political headlines suggest. As we are currently experiencing a second COVID-19 wave, there is also more urgency to reach political consensus. Either way, given strained government finances, private investors will likely have an important role to play.

President-elect Joe Biden's climate change plans

Traditionally, federal infrastructure policy is heavily based on surface transportation such as highways, roads and water infrastructure, with little mention of renewable energy and emerging technologies. This can be seen in the recent legislative bills and proposals such as the FAST Act renewal (Fixing America's Surface Transportation), the Build USA Infrastructure Act, the America's Transportation Infrastructure Act, and the America's Water Infrastructure Act of 2020 etc.

However, during Biden's campaign trail, he touted a USD 2 trillion climate change plan that looks to invest across the energy, transportation and building sectors. The plan promises to create millions of new jobs, build a more resilient economy, eliminate carbon emissions, and tackle environmental injustices. Details include:

- Invest in energy efficiency, clean energy, electrical systems and transmission (100% clean electricity by 2035)
- Innovate on technologies such as grid-scale storage, modular nuclear reactors, zero net energy buildings, green hydrogen, carbon capture and storage etc.
- Reduce greenhouse gas emissions from transportation, including railroads, aviation, cars and trucks
- Support communities of color and low-income who have typically been disproportionately harmed by pollution
- Deploy more than 500,000 new public electric vehicle charging outlets by the end of 2030
- Implement methane pollution limits for oil and gas operations

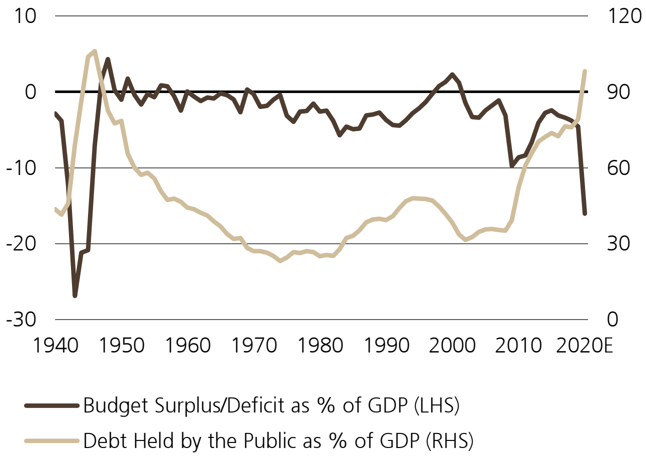
Role of private infrastructure investors

The sticking point for Biden's climate change strategy is the price tag. To fund these investments, he plans on raising taxes on individuals with an income above USD 400,000, and increasing capital gains tax, payroll tax, and the corporate income tax rate. If Republicans retake the Senate after the 5 January runoff elections, the likelihood of these tax raises will become relatively low.

However, this does not mean that there will be no infrastructure spending bill. Based on the dire situation of the economy, infrastructure spending is still the best method to immediately deploy large amounts of capital to stimulate the economy and create jobs. Without significant tax raises, it will be difficult to fund any stimulus bills.

Currently, the US federal government budget deficit and public debt levels have already climbed to the highest levels since World War II (see Figure 1). The situation is equally grim at the local government level. The National League of Cities (NLC) announced in a survey of over 1,100 municipalities that 65% of cities are delaying or cancelling infrastructure projects in response to severe revenue loss from COVID-19.

Figure 1: 2020 budget deficit and public debt have climbed to their highest levels since World War II



Source: Congressional Budget Office, September 2020

Similarly, according to a report by the American Road & Transportation Builders Association (ARTBA), more than USD 9.6 billion of infrastructure projects have already been delayed or canceled by states and local governments due to shrinking revenues.

Private capital will therefore need to play an increasingly important role. Although Republicans are ideologically more supportive of private sector investments, Biden has also highlighted the importance of the private sector in his climate change plans. He mentioned several times how he will enable private investments in clean energy, increase cooperation with the private sector, and support private entrepreneurs in researching new technologies.

Regardless of who wins the Senate race, the private infrastructure industry, equipped with over USD 200 billion of dry powder, will likely play a critical role in the next wave of infrastructure investments.

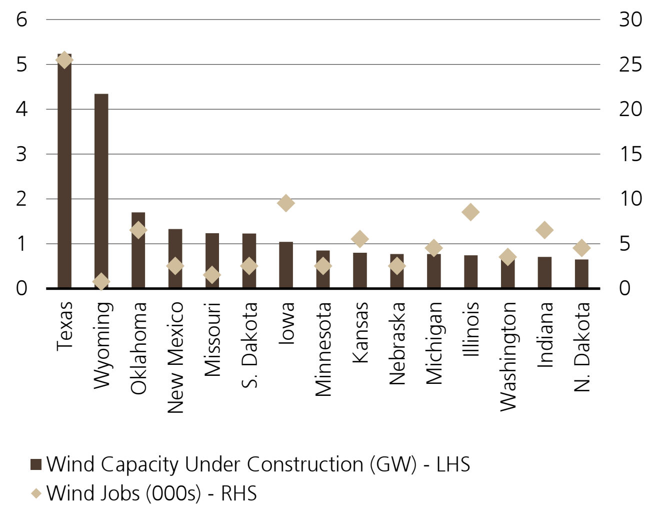
Bipartisan support for renewable energy?

Beyond the political rhetoric and headlines, the renewable energy sector has generally seen bipartisan support, and has shown resilience regardless of who is in the White House or Congress.

For example, under Trump's presidency, coal-fired power generation in the US still declined 35% since January 2017, while wind plus solar power generation increased by almost 60%. Continued cost declines, technological improvements, and widespread support from consumers mean the growth of renewable energy will continue.

Investors must also remember that red states such as Texas and Oklahoma actually have the highest amount of wind capacity in the US. Even if we look at the construction pipeline for wind farms in the following years, red states dominate the top spots (see Figure 2).

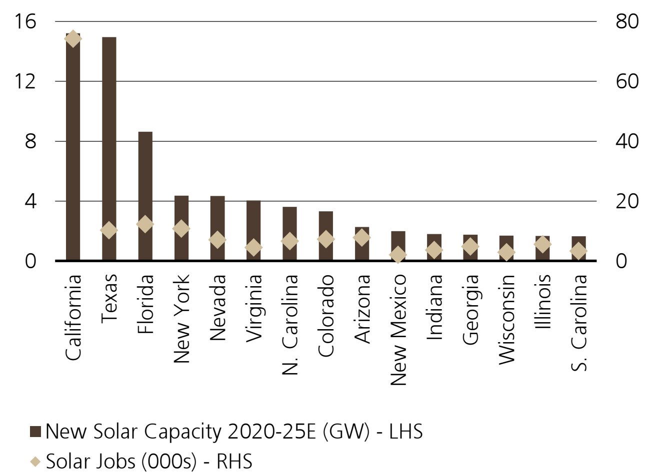
Figure 2: Red states dominate the top spots among states with the most wind projects under construction



Source: American Wind Energy Association, September 2020

There is a view that Republicans favor wind over solar due to the geographic distribution of these resources. In the past, there is certainly some truth to this. However, if we look at where new solar capacity is being built in the next five years, red states and politically important swing states actually make up the majority (see Figure 3). Moreover, even though the US solar industry is less than half the size of the wind industry, it employs twice the number of people, which means it has significant local job creation potential.

Figure 3: Red states or swing states make up a majority of the new solar capacity in the next five years



Source: Solar Energy Industries Association, June 2020

Finally, there could also be some interest in new electricity grid projects, which tends to receive more bipartisan support. Transmission lines typically fall under the more traditional definition of infrastructure, and are therefore less politicized than renewables. Yet new transmission lines actually directly benefit renewables by linking distant and remote resources to demand centers.

What happens to oil and gas?

The shale oil and gas industry has significant economic and political value, and thus a complete ban is unlikely in the short to medium-term. Biden recognizes this and therefore publicly stated that he does not want to ban fracking.

However, Biden's plan to restrict drilling on federal lands and increase regulation on methane could still increase the cost of business. Methane has been shown to be more potent than CO_2 as a greenhouse gas, and there is now more pressure to limit methane leakages at oil and gas wells.

Regulation is not necessarily bad for everyone, as it also puts upward pressure on commodity prices and increases barriers-to-entry. This creates more differentiation between efficient and inefficient operators, good and bad locations, rich and poor shale geologies etc. This may not be positive for the industry as a whole, but it means that savvy investors should still be able to find good investment opportunities.

Telecommunication is another sector to watch

The telecommunication sector has received significant attention during the COVID-19 pandemic. High speed internet has enabled working-from-home and remote-learning. However, rural areas and low-income neighborhoods generally have poor access to high speed internet, and have essentially been deprived of these essential services during lockdowns. In March, Microsoft estimated that 157 million Americans do not have access to broadband internet.

In a recent poll by the Internet Innovation Alliance, 90% of respondents support Congress using federal funds to expand broadband internet network infrastructure to areas that currently do not have access, and 88% support Congress increase support to those who cannot currently afford broadband internet, including students from low-income families.

Therefore, the next wave of telecom infrastructure investments will need to address the current digital divide. Biden has already included affordable broadband services in his USD 2 trillion plan. In addition, rural communities tend to be Republican-leaning, making broadband internet access a relatively bipartisan issue.

Summary

A Biden presidency will increase the likelihood of a spending bill that emphasizes ESG issues. The extent of this will be determined by the outcome of the Senate runoff elections. Regardless of who wins, there has historically been bipartisan support for renewable energy, so there is reason to remain cautiously optimistic.

In addition, there is now more urgency for congress to spur new investments to stimulate the economy and create jobs despite fiscal constraints. Therefore, private infrastructure investors are well positioned to take advantage of new opportunities under the next administration.

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