Eight benefits of listed over unlisted infrastructure

Investors who can see the benefits of holding global infrastructure assets face an early decision; choosing between listed and unlisted infrastructure assets. While the benefits of unlisted infrastructure are well known, this document highlights eight benefits of listed infrastructure, a universe of more than 350 companies worth more than US$4 trillion at prevailing market prices.[1]

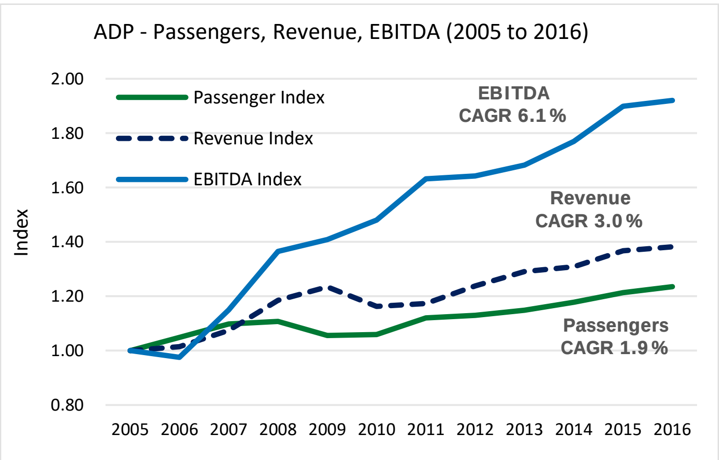
While the ownership structure does not change the characteristics of the underlying infrastructure assets (stable and reliable real returns and income over the business cycle), listed offers additional benefits that complement unlisted global infrastructure investments.

1 Some of the world's best infrastructure is listed

If investors want to own holdings in the world's best infrastructure companies, they are forced to turn, in part, to listed markets because some of the best infrastructure businesses can only be accessed this way. Paris's Charles de Gaulle international airport, Melbourne's CityLink, and the high-voltage electricity transmission network in England and Wales, for example, are owned by listed infrastructure companies. Investors have been well rewarded as these companies have achieved rising returns on equity and higher earnings per share.

CHARLES DE GAULLE AIRPORT (PARIS)

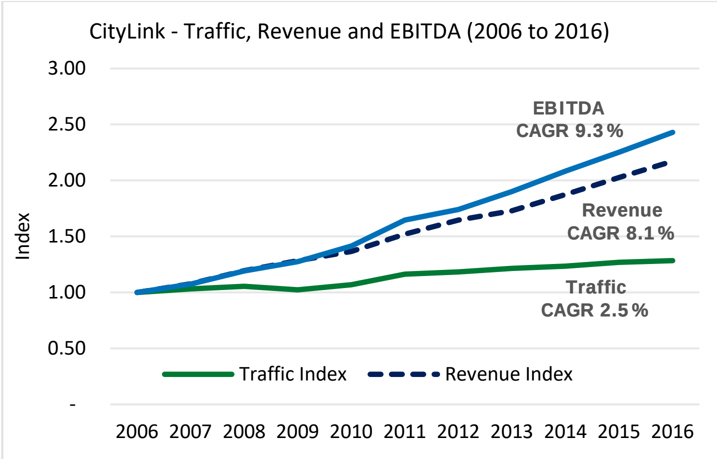

Source: parisinfo.com



Source: Magellan.

MELBOURNE'S CITYLINK


Source: transurban.com



Source: Magellan.

Table 1: Examples of high quality assets within the listed infrastructure universe.

COMPANY	COMMENTARY
Sydney Airport	Sydney Airport is Australia's largest airport and is one of the busiest 40 in the world as it handles about 41 million international and domestic passengers a year. Sydney Airport enjoys a mix of businesses from which it earns revenue, including international and domestic aeronautical services, retailing and property.
nationalgrid	UK-based National Grid owns and operates regulated electricity and gas networks in the UK and the northeast US. These networks are monopolies because most of National Grid's consumers have no other way to receive electricity or gas.
Atlantia	Atlantia of Italy operates Europe's largest motorway network while managing more than 5,000 kilometres of toll motorways in Italy, Brazil, Chile, India and Poland. In addition, Atlantia manages five airports in Italy and France.

[1] Source: Bloomberg, Magellan, as at December 2017.

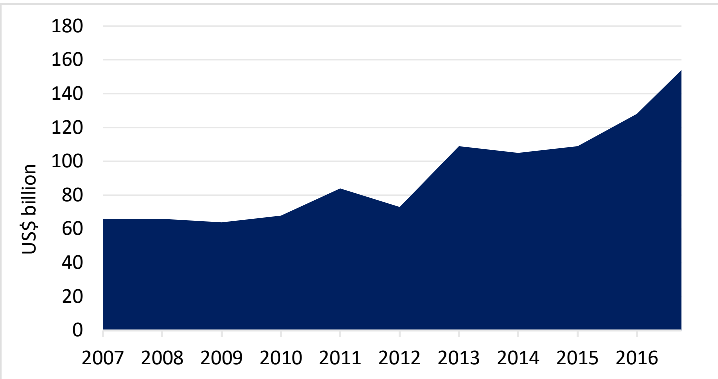
AMERICAN TOWER	American Tower is a communications tower infrastructure company that provides co-location space to wireless carriers across its more than 140,000 communication sites globally. The company operates in 15 countries and five continents.
ENBRIDGE	Enbridge of Canada owns and operates the world's largest crude oil and liquids transportation system across Canada and the US. Enbridge's assets are dominated by a petroleum pipeline network that transports more than two million barrels of crude oil per day. The company owns a network of natural-gas-related transmission and midstream assets in North America, as well as Canada's largest natural gas distribution utility.

Source: Magellan.

2 An ability to invest quickly

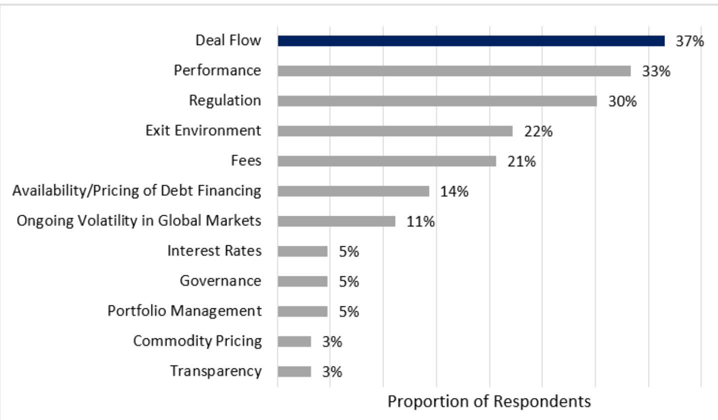
The liquid nature of the listed infrastructure universe enables investors to achieve their desired strategic allocation in relatively short order. We estimate that an investor can deploy US$500 million in the world's best listed infrastructure assets within a number of weeks while it can take investors in unlisted infrastructure a number of years to invest their capital. A recent Preqin infrastructure survey noted 37% of infrastructure investors are concerned with the lack of deal flow that has contributed to the growing levels of 'dry powder' to unlisted infrastructure funds. Chart 1 below shows the growing 'committed but not deployed' capital has exceeded US$100 billion since 2013.

Chart 1: Growing 'committed but not deployed' capital has exceeded US$100 billion since 2013.



Source: Preqin.

Chart 2: Investor views on the key issues for the infrastructure industry in 2017.



Source: Preqin.

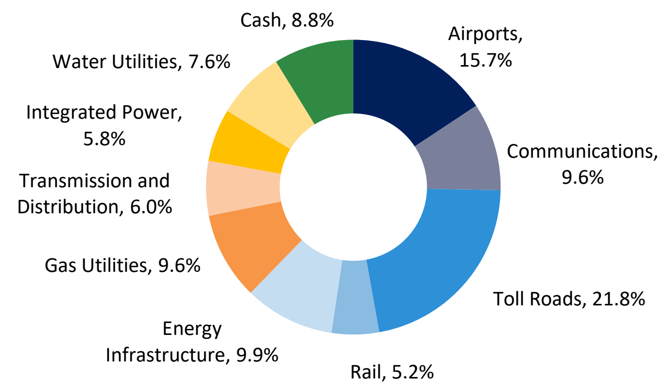
3 Diversification across sectors and regions

Listed infrastructure companies own and operate assets located around the world (developed and emerging countries) and across the spectrum of infrastructure sub-sectors (including utilities, infrastructure and social). This diversity means investors can dynamically build high-quality well-diversified portfolios of infrastructure assets.

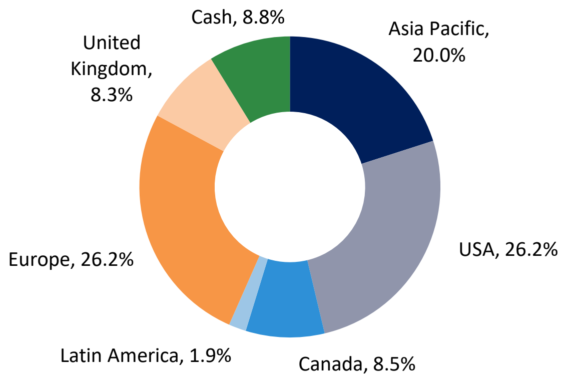
UTILITIES	INFRASTRUCTURE	SOCIAL
Water	Airports	Hospitals
Gas utilities	Toll roads	Schools
Energy transmission & distribution	Pipelines	
	Communication	
	Ports	
	Rail	

Chart 3: Sector and geographical exposure of the Magellan Select Infrastructure Strategy as at 30 September 2017.

Sector Exposure*



Geographical Exposure*

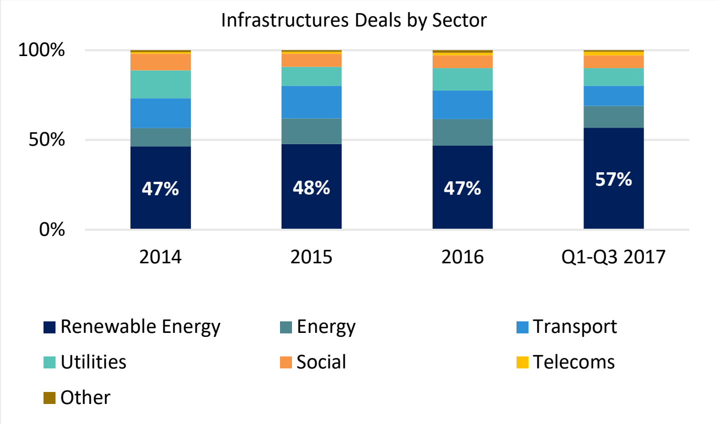


Source: Magellan.
*Sectors are internally defined. Geographical exposures are by domicile of listing.

This compares with the unlisted world where funds typically hold a concentrated portfolio of between five and 15 assets with a bias to a sector or region depending on available assets, during the Funds investment period.

More recently, as illustrated in chart 4 below, approximately 50% of completed infrastructure deals were focused on renewable energy assets[2], resulting in most unlisted infrastructure funds having a bias to the renewable energy sector. Achieving portfolio diversification can be challenging with an unlisted-only approach.

Chart 4: Representative sector allocation amongst 2015-2017 private-market infrastructure funds.



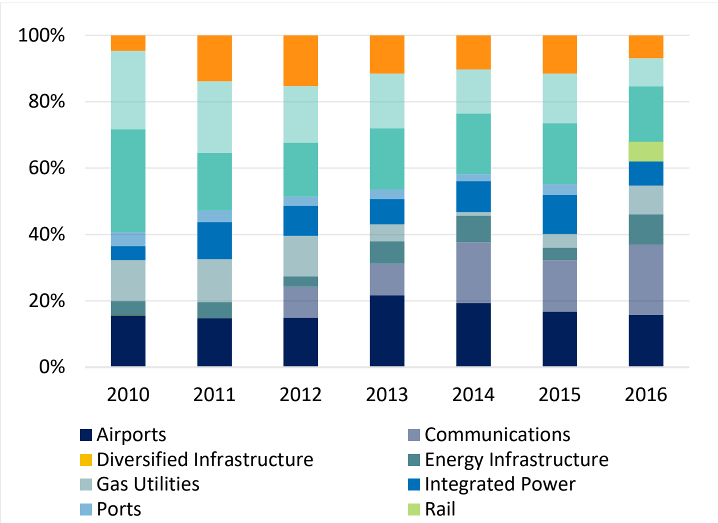
Source: Preqin.

An ability to tilt across regions and sectors

Once investors have built a well-diversified portfolio of global listed infrastructure stocks, they can readily adjust holdings across sectors and regions to take advantage of different pricing conditions across markets. This ability can enhance the risk-return profiles of portfolios.

Unlisted infrastructure funds are generally unable to make medium-term tilts across regions and sectors during the life of the fund to take advantage of pricing opportunities.

Chart 5: Active sector tilts across the Magellan Select Infrastructure Strategy 2010-16.



Source: Magellan.

Live prices reduce illusionary risk reduction

The intrinsic value of any long-dated asset (including infrastructure assets) is simply a function of its future cash flows and their associated risks. Because of the predictability of their cash flows, the intrinsic valuations of infrastructure assets tend to be stable over time. Despite this, stock prices fluctuate above and below this intrinsic value, presenting investors the opportunity to achieve superior risk-adjusted returns.

The more infrequently asset valuation takes place, the less accurate the accounting value of an asset is likely to be. As a result, less-frequently valued assets (such as unlisted infrastructure assets) present risks to certain institutions such as defined contribution plans. For these, the liquidity mismatch created by offering members the ability to transact (by switching investment options or joining/departing the plan) more regularly than assets are valued increases the risk of such a plan's assets' values being misrepresented to investors, which can lead them to join the plan at an inflated price (or depart at an artificially low price). As defined contribution funds generally allow their members daily liquidity, even quarterly valuations present significant risk for members to transact at inaccurate prices.

The counter-argument often put forward is that listed investments contain 'beta risk'; i.e., are subject to the volatility of the broader equities market because they are listed on an exchange. The merit of this argument is rather difficult to follow. For example, in the event that an asset is 50% privately traded and 50% publicly traded, it is difficult to make the case that the publicly traded portion of the same asset carries higher risk.

Given the above, it is rather surprising that many institutional investors deem private-market assets lower risk than their publicly traded equivalents. In the eyes of rational investors, asset valuation frequency has no bearing on an asset's fundamental business risk; however, the more frequently an asset is valued, the lower the investment risk it presents.

More mispricing opportunities

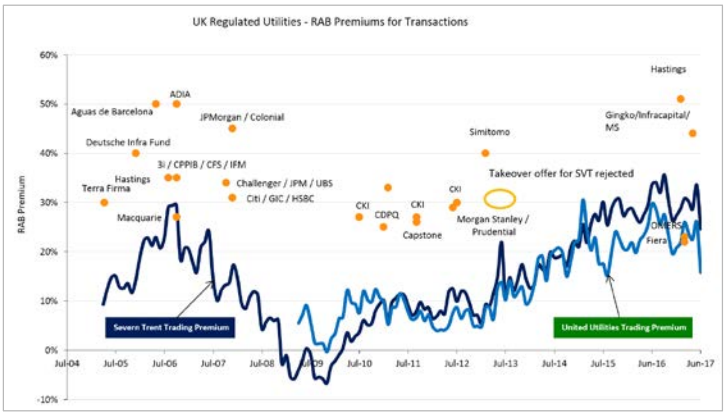
The nature of listed markets provides skilled investors with the opportunity to purchase assets at a material discount to their intrinsic value or to sell them at material premiums.

In recent years, demand-and-supply dynamics for private-market infrastructure have shifted such that many of these assets have been acquired at valuation premiums to their publicly traded alternatives.

As shown in Chart 6, within the UK utilities sector, valuation differences have been pronounced. Despite the country's sophisticated regulatory regime that permits utilities to earn a set, fair return on their regulated asset base (which can be thought of as net tangible assets), and regardless of ownership, valuation premiums have persisted over the past decade. The chart shows private-market transaction valuations have exceeded trading multiples by between 20% and 50% to the underlying net tangible assets. The mispricing opportunities are also available within global airports.

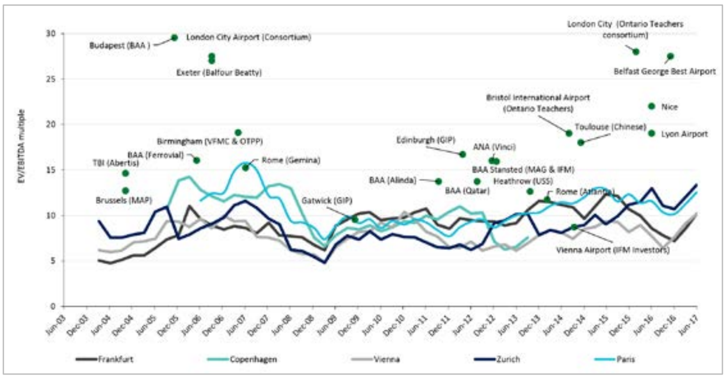
[2] Preqin.

Chart 6: Relative pricing opportunities within UK water utilities.



Sources: Company accounts, Magellan research.

Chart 7: Relative pricing opportunities within global airports.



Sources: Company accounts, Magellan research.

Transparency of assets from the outset

Another benefit of listed securities is that investors are well informed and aware of the likely assets that will form part of a listed infrastructure portfolio. This contrasts with private infrastructure funds that can often involve a 'blind commitment' to a fund that may, at the end of the investment period, hold lower-quality non-core assets than promised at the outset.

No forced asset sales

Another factor in favour of listed securities is that there are no forced asset sales. The closed-ended nature of private infrastructure funds can result in redeeming assets at sub-optimal market conditions. The open-ended nature of listed assets means exposure can be held indefinitely.