GLOBAL LISTED INFRASTRUCTURE
Market Commentary Q1 2018

EXECUTIVE SUMMARY

- Despite weak performance in Q1, we maintain a constructive outlook for listed infrastructure to deliver 10-12% returns in 2018.
- M&A activity is accelerating - one of the key factors we highlighted that would draw attention to the >20% discount listed infrastructure companies are trading at relative to their asset values.
- Our total return forecast is underpinned by a 4% dividend yield and 8-9% dividend growth.

OUTLOOK AND STRATEGY

The secular drivers for infrastructure remain in place, namely the inflation sensitivity of the assets and the need to invest in aging infrastructure in developed markets for efficiency, safety and reliability purposes. Other regional and sector-level themes are driving increased infrastructure investment, including the transition towards clean energy, connecting abundant U.S. natural gas supply with global demand, and the explosion in data and digital information.

Our return outlook is the build-up of stable dividends and visible growth driven by the above themes: 4% recurring (60% payout) dividend yield, plus the inflationary growth of 1-3% plus 3-4% growth from investment in existing and new infrastructure projects (funded by the 40% of retained earnings). Our upside case could see another year of 15-20% returns driven by multiple expansion. Interaction with our private market infrastructure team at CBRE Caledon Capital leads us to surmise that the listed infrastructure market trades at a significant discount to the value of its underlying assets. On average, listed infrastructure trades at an 11.2x EBITDA multiple, well below private values (14-16x) for similar core infrastructure assets.

Many M&A announcements and private market transactions support our view that the gap in valuations will lead to rising multiples for listed companies. Interest in infrastructure as an asset class continues to rise, with increasing allocations among sizable sovereign pension funds and new allocations among smaller institutions. The scarcity of these essential assets combined with increased fund flows is in stark contrast to the discounts implied in the valuations of the listed companies. We expect M&A activity to accelerate this year leading to a re-rating in the value of the listed market, but our outlook is positive for infrastructure even in the absence of such a catalyst, underpinned by visible, secular investment trends.

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MARKET REVIEW[1]

Listed infrastructure finished down 4.5% in the first quarter of 2018. After a relatively flat January, infrastructure stocks sold off in February and rebounded modestly in March, up 0.8% in the month. All regions had negative returns in Q1, although Continental Europe was the leader and closed slightly below break-even. Developed Asia outperformed global infrastructure while the Americas and the U.K. were the biggest laggards. Generally, most global treasury yields rose in the quarter and peaked in mid-February putting some pressure on bond proxy equities. Crude oil stayed in a $60-65 per barrel range and the USD depreciated against most major currencies.

Continental Europe benefited from positive economic developments broadly as well as lessening political risk. Transportation outperformed as the stocks were supported by M&A activity as well as fundamentals continuing to drive solid operating results. Negative returns from regulated electrics and gas distribution utilities were muted, while renewable and integrated electric companies generated positive returns. Similarly, U.K. regulated electric and water utilities traded down while integrated utilities were up in the quarter. Satellite companies in Europe continued to lag as secular changes in their market continue to drive profit warnings.

Every country in Developed Asia outperformed except Australia. Australia sold off in every sector highlighted by the 10% fall in toll roads and discussion around Transurban's Citylink concession acquisition. While Hong Kong, New Zealand, and Singapore outperformed, Japan was the clear leader in the region finishing up 5.8%. Helped by an appreciating yen, Japan had strong returns from utilities driven by positive news on nuclear restarts.

In the U.S. and Canada, Midstream/Pipelines experienced a large sell-off after the regulator changed a tax allowance rule on certain MLP pipelines. While some pipelines owned by MLPs will recover less with this new ruling, sentiment on the entire space deteriorated. Integrated utilities and renewable companies outperformed whereas the more interest rate sensitive regulated and water utilities did not fare as well. Towers closed higher as organic growth expectations remain solid. U.S. railroads outperformed while their Canadian counterparts lagged.

IMPORTANT DISCLOSURES

[1]All discussion of performance of infrastructure stocks refers to the UBS Global Infrastructure & Utilities 50-50 Index through 02/28/2015 and FTSE Global Core Infrastructure 50/50 Index from 03/01/2015-03/31/2018.

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The FTSE Global Core Infrastructure 50/50 Index provides exposure to infrastructure as defined by the Industry Classification Benchmark (ICB) and adjusts the exposure to certain infrastructure sub-sectors. Company weights are limited to 5%. The UBS 50/50 Index is an unmanaged market-weighted index which consists of infrastructure and utility companies from developed markets whose floats are larger than US $500 million. PA05142018