GRI News and Reports


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INVESTOR'S APPETITE FOR US INFRASTRUCTURE ASSETS

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GRI Club INFRASTRUCTURE

Baker McKenzie

Introduction

On January 21, 2021, the GRI Club held an eMeeting titled "Investors' Appetite for US Infrastructure Assets - Competitive opportunities or scarce success?". The eMeeting discussed investment opportunities in the US Infrastructure and Energy sectors in light of the Covid-19 pandemic, the recent US presidential election and the worldwide drive towards sustainability and decarbonization.

The e-Meeting was moderated by Jose Moran, Partner at Baker & McKenzie LLP, and Jorge Valenzuela, Principal at ARUP, and included the following panelists: Amit Rikhy, President and CEO, Carlyle Airport Group, Helen Newell, Senior Vice President-Infrastructure, GIC, Juan Camargo, Managing Director, OMERS Infrastructure, Olivier Renault, Managing Director, Caisse de dépôt et placement du Québec (CDPQ), and Paul David, Head of Americas, Infrastructure Debt, Allianz Global Investors.

The discussion led to this white paper, which explores current investor opportunities in the US infrastructure and energy sectors.

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1. The Biden Administration, Infrastructure and Covid-19

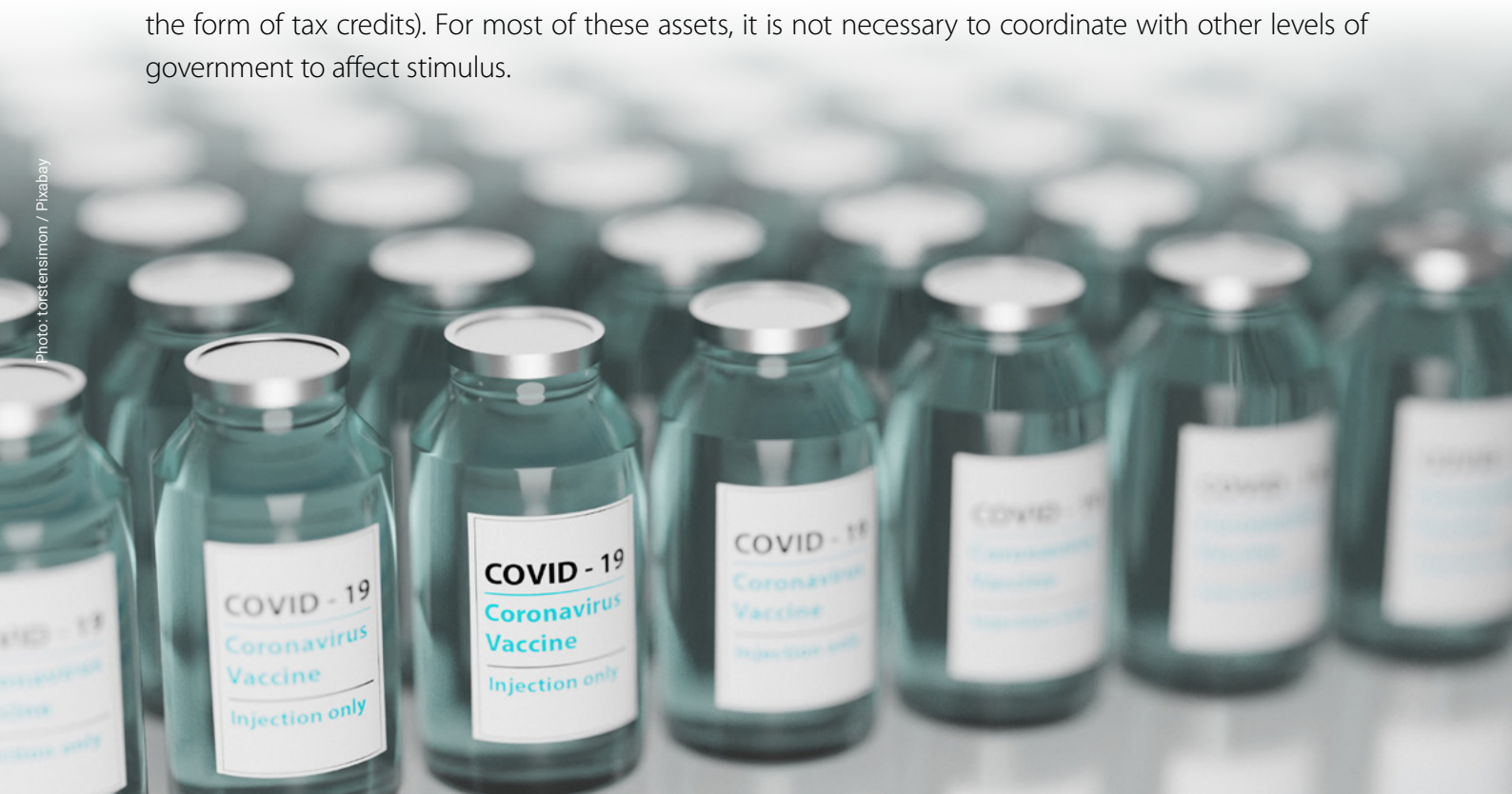
One speaker indicated that infrastructure is a key focus for the Biden administration. The number one priority now for the Biden administration is Covid relief.

The Biden infrastructure policy is a wide ranging policy, which touches every aspect of infrastructure, including assets at the state and local level. The Biden infrastructure policy has a big focus on sustainability: everything that will be done will focus on sustainability. The second big area of focus will be on equity: infrastructure investment will not focus only on wealthy areas, but will focus also on disadvantaged areas to create equitable economic opportunity.

The Biden administration will also focus on healthy travel. Its efforts will aim to rebuild confidence in all modes of travel, and will aim to ensure that such travel is healthy, safe and secure. The Biden administration will aim to provide stimulus to develop and retrofit travel assets consistent with this goal.

Panelists considered several obstacles that the Biden administration may face in effecting its plans. Many assets and procurements lie within the jurisdictions of non-federal levels of US government: at state, regional municipal and other levels of government (such as universities). In the past, big federal plans for infrastructure stimulus have been complicated by this relationship and the need to get approvals at other levels of government for plans to proceed. This is not a new problem. However, for large-scale stimulus to take effect, it is critically important to coordinate between the different levels of the US government.

Renewable energy assets differ, since the main stimulative effect is derived from federal tax policy (in the form of tax credits). For most of these assets, it is not necessary to coordinate with other levels of government to affect stimulus.



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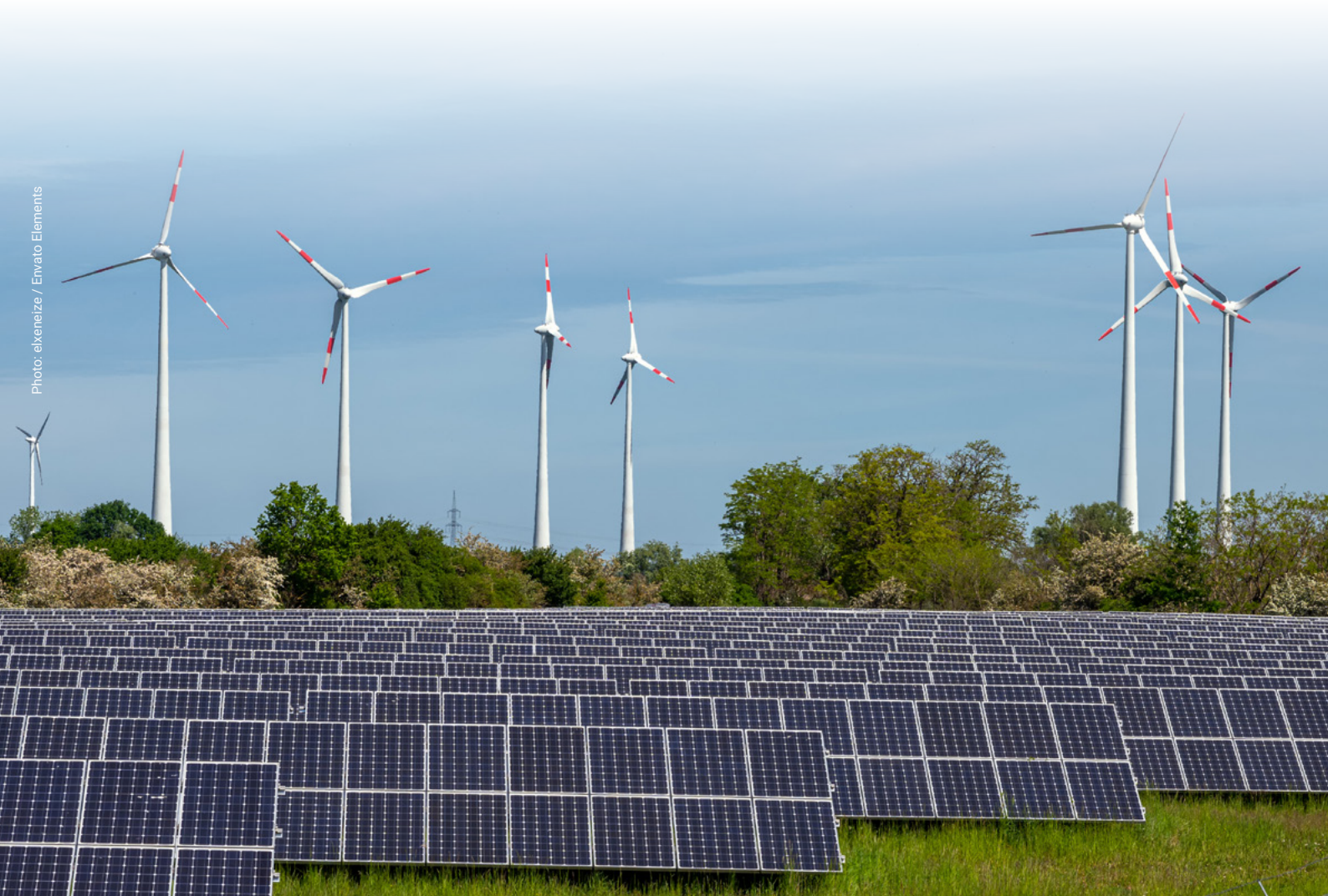
2. Investment opportunities in sources of renewable energy

The panel considered investment opportunities among the different sources of renewable energy.

One panelist noted that energy had been involved in a first wave of transition, to cleaner energy, and was now engaged in a second wave of transition, from fossil fuels to renewables. The investment opportunities in the US include wind and solar, hydrogen and carbon capture, electrolyzing technology (for hydrogen production) and electric vehicles (and charging networks for such vehicles).

A principal challenge for hydrogen is that it is not currently used on a wide scale. The Biden administration may encourage further use of hydrogen by imposing a tax on carbon emission as well as by subsidizing the use of hydrogen assets. A panelist was of the view that a measurable shift to increased use of hydrogen might not occur in the near term.

The panel considered a question from the audience regarding whether the recession had affected the ability of investors to invest in renewables. A panelist responded that the market is tightening, but deals are getting done. The recent extension in the US of the investment tax credit for solar investments through the end of 2022 should increase the number of investment opportunities in that space. Renewables deals may be monetized internally (with existing tax equity investors), rather than with third party debt.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3. Energy transition; Oil & gas companies moving into renewables

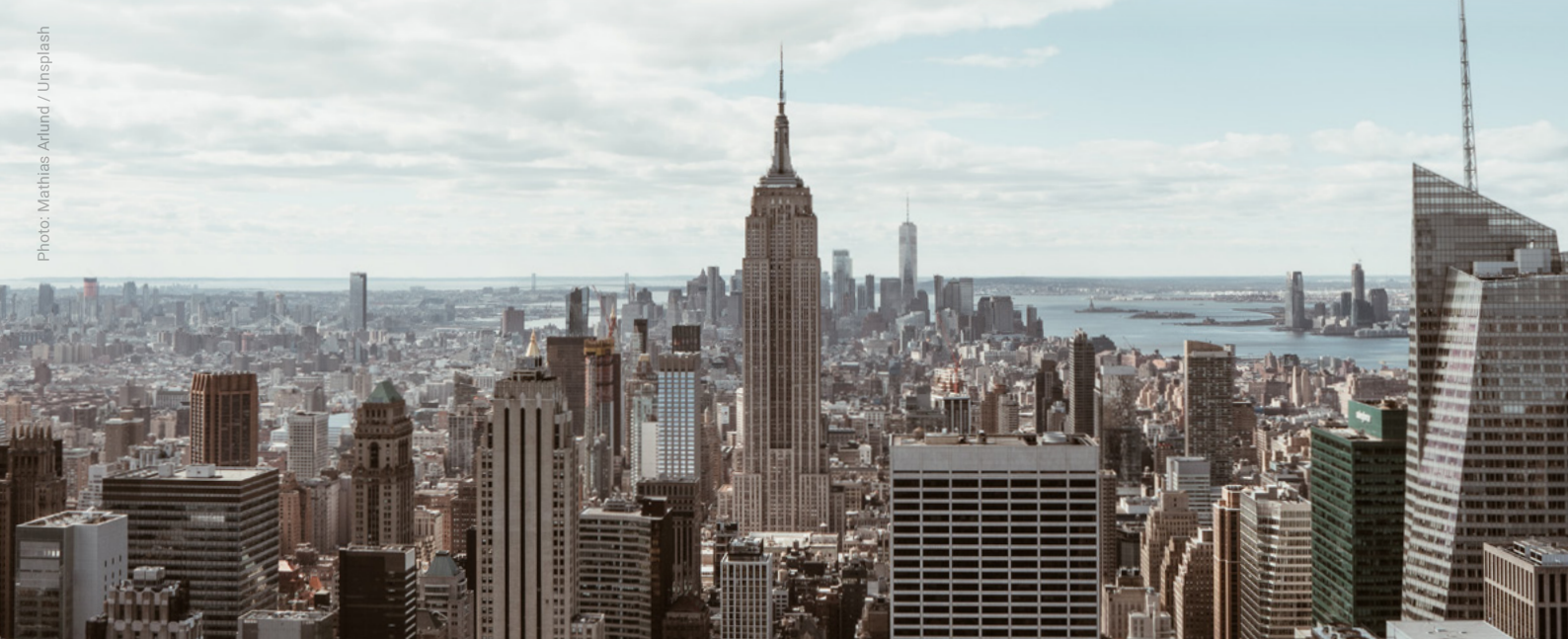
A panelist noted that, while there has been much speculation about traditional oil & gas companies seeking to diversify into renewable energy assets, the panelist had not seen much evidence of this. Private equity and pension funds are currently the big players in this space. Oil & gas companies may come into this market in the future, but have not yet been seen making large investments.

The Biden administration has given a clear message regarding renewables. It has cancelled the Keystone pipeline, and has rejoined the Paris climate accord.

A panelist questioned whether the current US tax equity system was the best way to promote the Biden administration's renewables policy. In the view of this panelist, renewables assets are long term assets, that ideally should be funded with long term liabilities. The panelist stated that there was a currently a degree of uncertainty in financing renewable assets.

4. The prospects for investment by Chinese State-Owned Enterprises (SOEs) in US infrastructure assets

SOEs have made a number of investments in infrastructure around the world as part of China's "belt and road" program, including investments in Latin America. The panel was asked to consider whether SOEs are likely to invest in US infrastructure. Several panelists stated that investment by SOEs in US infrastructure will depend on the nature of the political relationship between US and China. Given the current state of such relationship, such investment may not occur in the near term. The existence of the US CFIUS law, which regulates certain foreign investment in the US, is also a factor.



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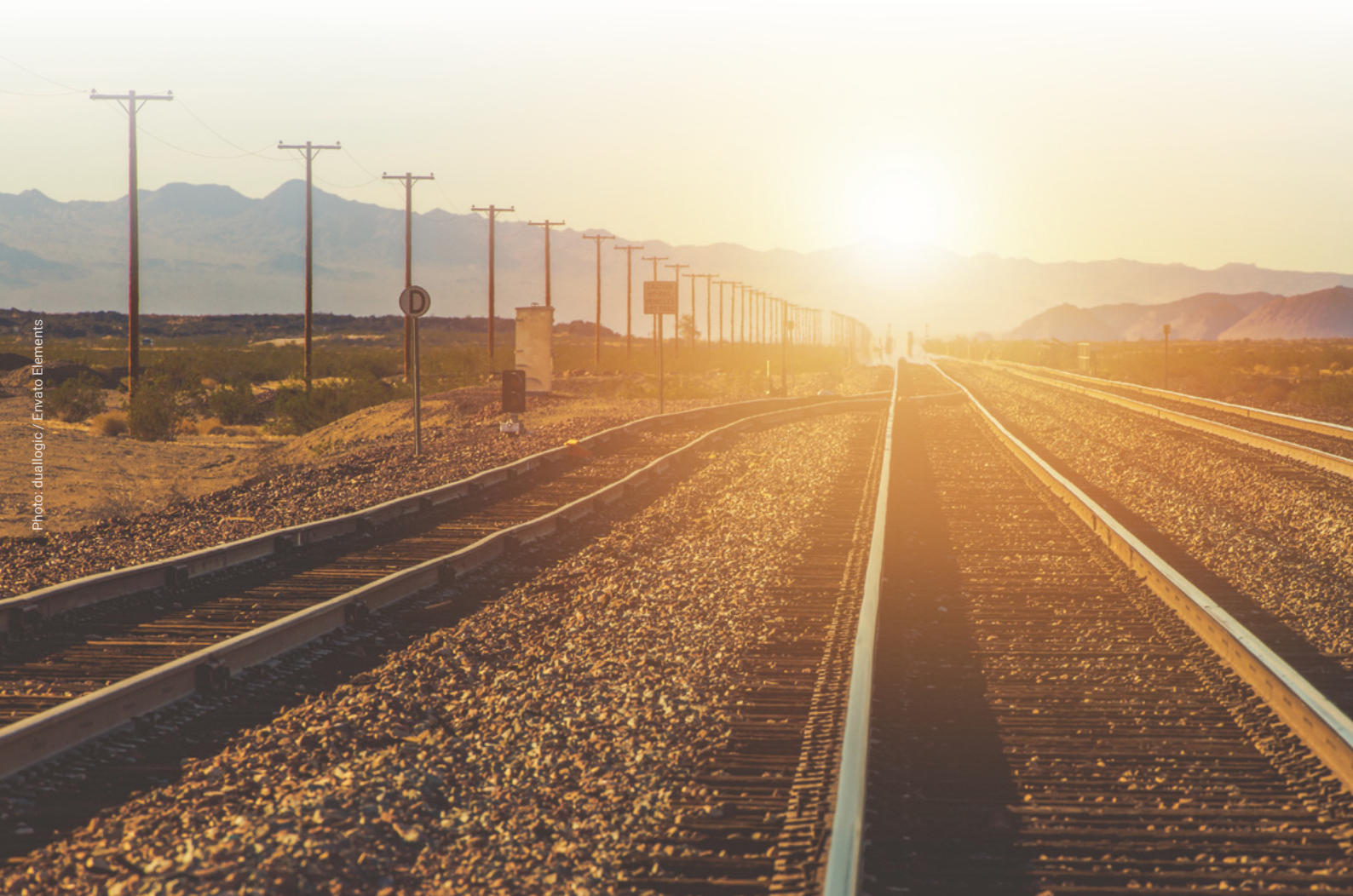
5. Investment opportunities in the transportation sector

• Rail

Biden has pledged a "second great railroad revolution" to make the US rail system the cleanest, safest, and fastest rail system in the world, for both passengers and freight.

A panelist stated that US politicians have often talked a lot about increased governmental investment in rail, only for such investment to not actually materialize.

Environmental, social and corporate governance (**ESG**) concerns are a key piece of the puzzle from the freight perspective. From the commuter rail perspective, the Biden policy will focus on improving air quality and reducing congestion through increased use of light rail. The transportation sector may also see use of public-private partnerships (**P3**) for passenger transportation, and may also see private opportunities, the divestment of transportation assets by major industrial companies and governmental funding in situations where the private sector does not get involved.



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• Aviation

The impact of the Covid-19 pandemic on aviation has been quite severe. A panelist noted that most economic forecasts point to full recovery in the sector not occurring until 2025 or afterwards. Governmental stimulus in this area is very important.

Covid revealed that airports were more economically fragile than was previously thought. Airports are now thinking about how to make their assets more resilient and are examining which of their assets are noncore and could be divested or managed by private enterprise.

Airports are seeing rapid changes in technology, with the aim to create seamless and contactless journeys. Airports are looking at ways to make existing assets smarter and digitized, including the use of biometrics, investments in modernized HVAC, as well as smarter buildings and infrastructure. There is a huge potential role to play for the private sector and for P3s.

In the US, airports are managed at local level. Some cities are exploring airport privatization. Airports are considering ways in which private sector efficiency can be introduced to manage airport assets without effecting a change of ownership of such assets to the private sector. Airports are looking at ways to develop and operate their existing assets with the private sector.


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• Lending

The panel considered the role of lenders in restructuring the debt of infrastructure assets. A panelist divided transportation assets into two principal classes for lenders for this purpose: (i) toll roads (which saw a temporary drop in revenues during the pandemic, but have now recovered) and (ii) airports. Airports are suffering at the moment due to liquidity issues. However, long term investors are taking a long term view: these assets are necessary and will remain so. There is a great opportunity for the Biden administration to provide stimulus for these assets.

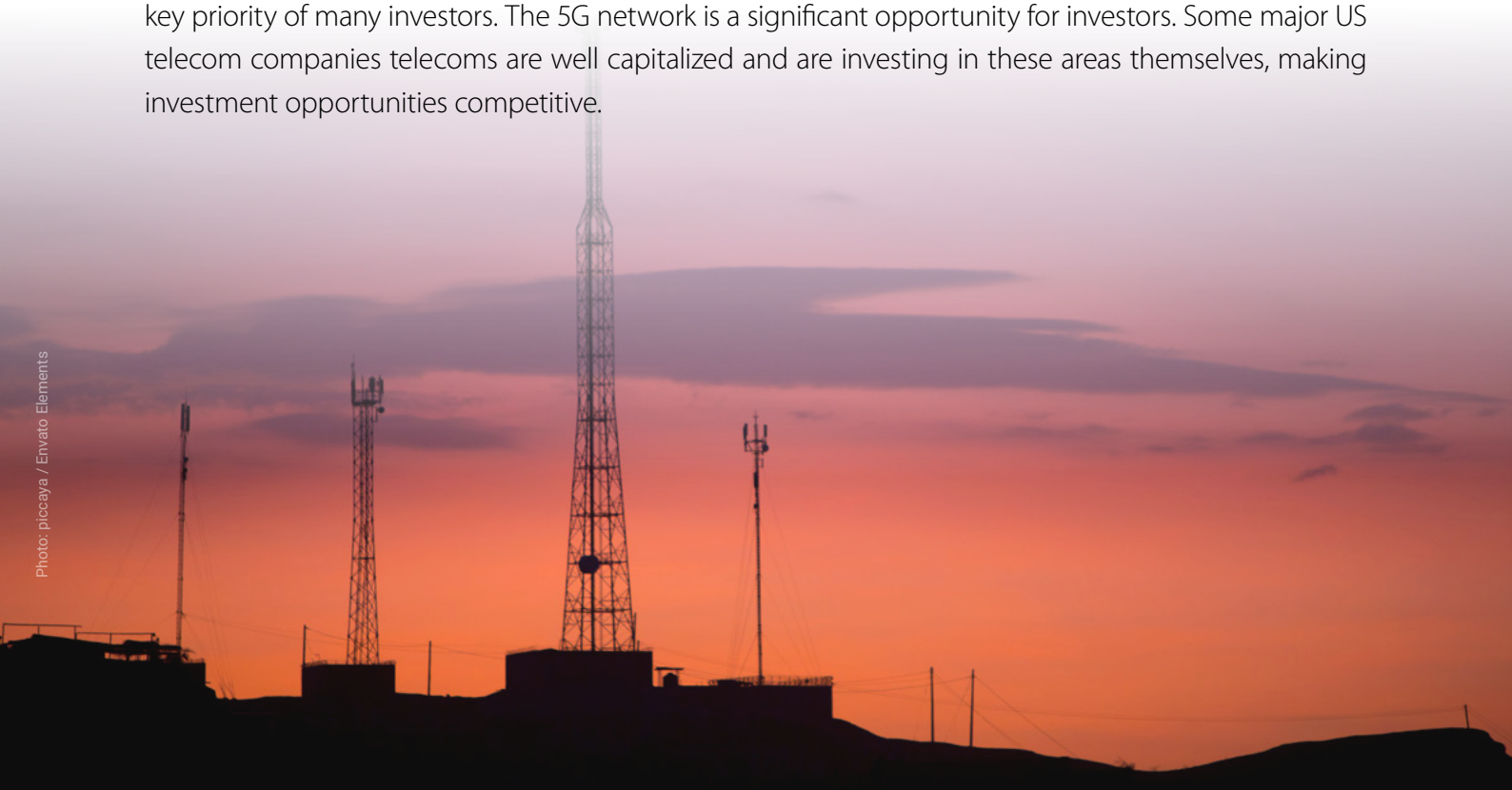
A panelist noted that the US reliance on tax-exempt debt to finance infrastructure assets may be an inefficient means to finance these assets, in that the capacity of state and local governments to issue this debt may be limited. The panelist noted that some airports were looking outside the tax-exempt market for debt investors, and that some investors may be willing to invest in non-tax-exempt debt.

• Carbon capture

A panelist expressed the view that carbon capture was not currently investable at scale, and is currently seen as very expensive and uneconomical. May see investments in carbon capture in Europe before this type of investment is seen in the US.

• Digital infrastructure

Digital infrastructure (including data centers, satellites, wireless towers (multiple transponders), smaller scale digital transmission (transponders on existing buildings), cyber networks and fiber to home) are a key priority of many investors. The 5G network is a significant opportunity for investors. Some major US telecom companies telecoms are well capitalized and are investing in these areas themselves, making investment opportunities competitive.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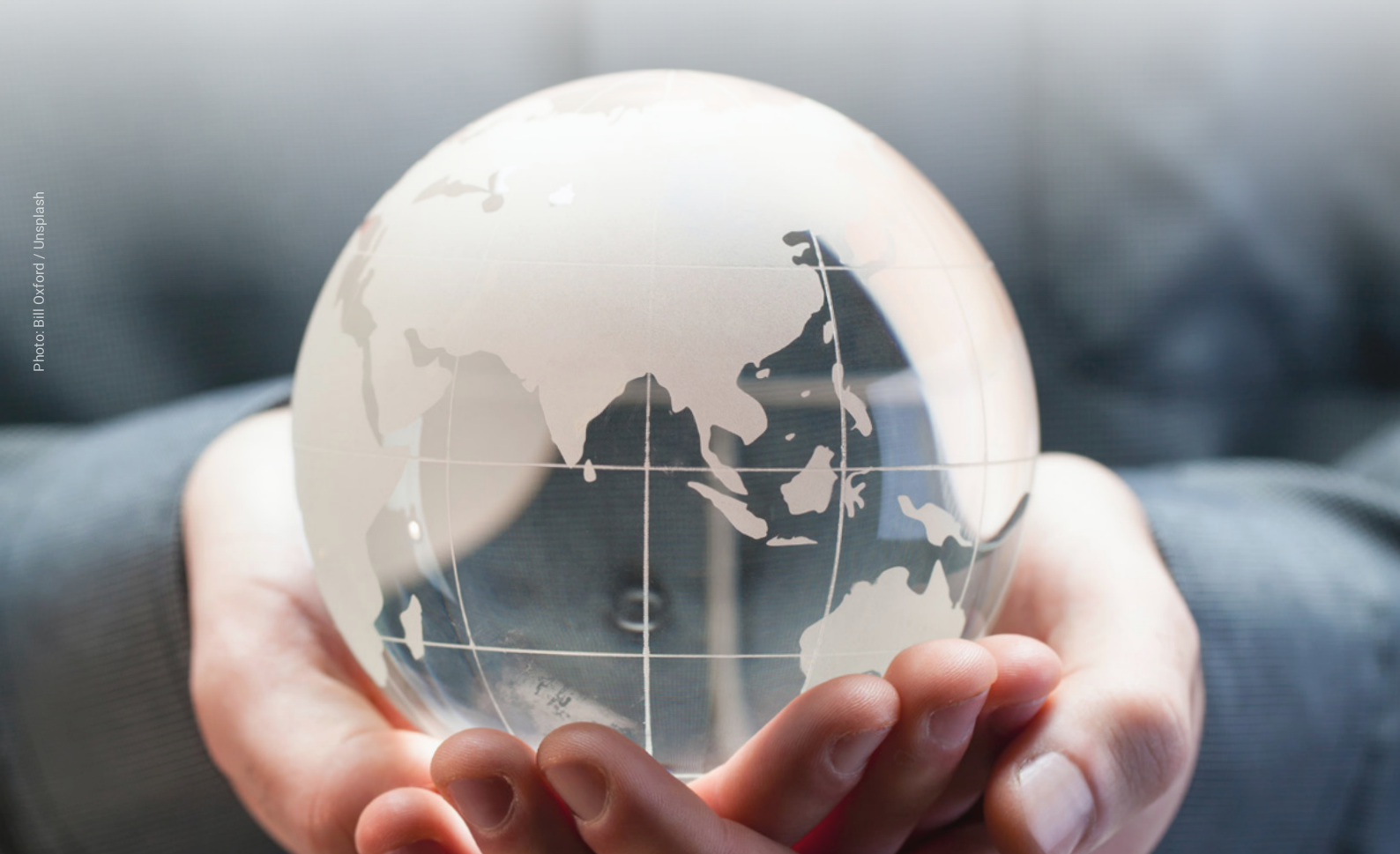
6. Climate change

There is an enormous appetite for sustainable infrastructure. ESG, including climate change, is important to many companies and investors. In this regard, North America is catching up to Europe, where these concerns have been viewed as important for a longer period.

Investors are getting smarter at evaluating climate risks. ESG is now part of the discussion at investment committees, which now recognize that ESG concerns affect the economics of investment. ESG concerns can impact the longevity of a particular company, in terms of retaining customers and employees and overall viability. Investment committees look at whether an investment will be disrupted by ESG concerns.

Investors are looking for returns and opportunities. Investors wish to make money and do the right thing. Finding the right balance between these two goals is important. A panelist stated that there will be more sustainable investment on the planet. We are past the tipping point. Investors are taking ESG concerns seriously.

With respect to lending, green bonds and impact were seen as important, but as of now only providing limited impact. The world (and the US) may follow the lead of Europe on ESG, in particular from the EU taxonomy for sustainable activities. This taxonomy sets the direction of travel by providing a common template to evaluate the effects of sustainability within investment portfolios.



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The mission of GRI is to connect leaders from these markets and contribute to the building of privileged relationships and real business opportunities. In this context, more than 6 thousand businessmen, senior executives and investors participate annually in the club's programming in the world.

GRI is a global club bringing together key players in the real estate and infrastructure sectors. Founded in 1998 in London, it is present in 25 strategic countries. In Brazil, it has been active since 2010.

GRI Club Infra, in particular, has made itself the great meeting point for infrastructure and energy abroad. Its exclusive platform provides meetings focused on exchanging experiences, thematic discussions between members and government authorities, and propositional dialogues with the authorities, as well as holding large events open to other members of the market.

The GRI Club Infra portfolio also includes a series of practical suggestions for enhancing industry competitiveness, the GRI Hub, an online news platform, and the GRI Thermometer, a six-month gauge of market mood.

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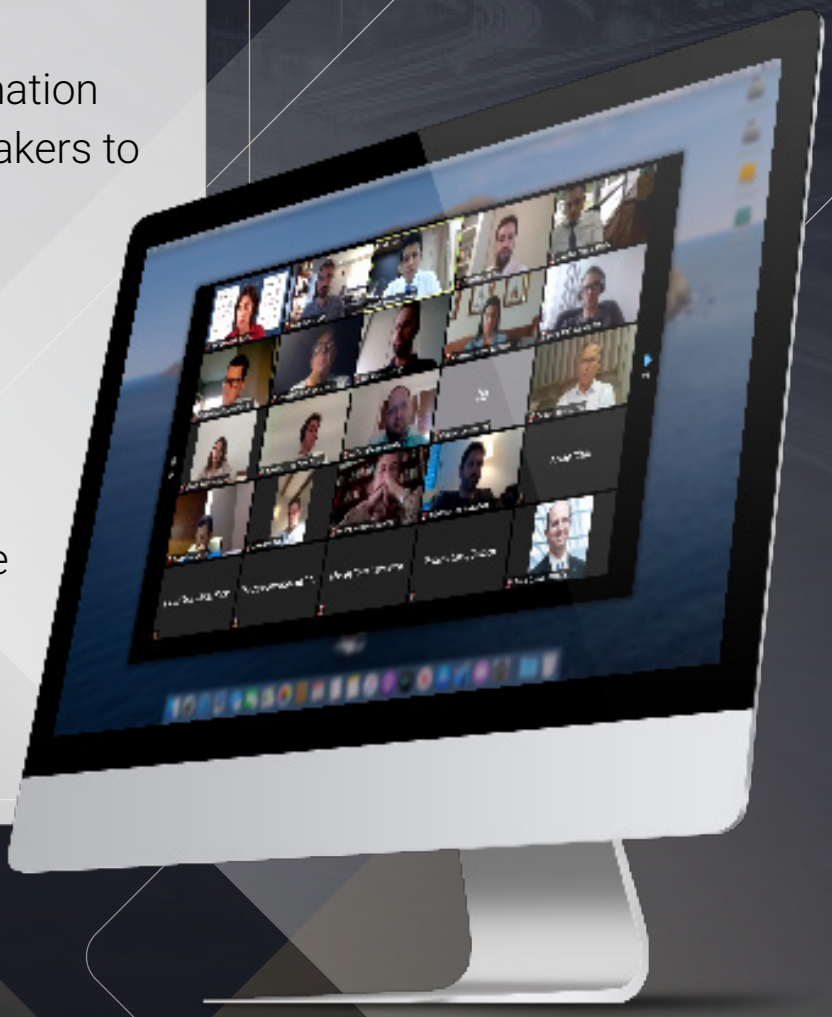

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