29 March 2023, 1:38PM UTC
Chief Investment Office GWM
Investment Research

The case for private infrastructure exposure

UBS House View - Daily Europe

Mark Haefele, Global Wealth Management Chief Investment Officer, UBS AG
Jon Gordon, Strategist, UBS AG Hong Kong Branch
Karim Cherif, Head Alternative Investments, UBS Switzerland AG
Vincent Heaney, Strategist, UBS AG London Branch

Video – Should I consider private infrastructure? (6:54)
Hear the arguments for infrastructure investing from CIO's Karim Cherif.

Thought of the day

In many economies, government-led infrastructure investing is at the forefront of the strategic agenda. While not as familiar to some investors, the types of projects involved are not particularly mysterious: transportation and regulated utilities (like power lines and airports), energy and communication assets (power plants and data centers), and social infrastructure (schools and hospitals).

CIO estimates USD 70–100 trillion of aggregate spending will be required to support global infrastructure through 2040.

But governments alone cannot bear this cost—which, in our view, offers opportunities for private capital:

Private infrastructure is key to several critical secular trends. Digitalization requires more high-speed mobile networks and data centers. A reversal of globalization will require modernized ports and other logistics systems. The energy transition needs more renewable power generation and battery storage. A significant part of the funding for these projects must come from private investors. Take the global net-zero emissions target of 2050, which a 2023 McKinsey Transition Finance Model suggests is predicated on at least USD 1.5 trillion in private investor funding.

For investors, it can also offer portfolio benefits. Many private infrastructure assets exhibit common characteristics, such as high barriers to entry, low price elasticity of demand, and stable and often inflation-linked cash flows. In an uncertain economic environment with elevated inflation, the prospect of more stable income generation may help smooth out the performance of a multi-asset portfolio.

There are infrastructure strategies targeting different levels of return and risk. Core and core plus strategies require limited capital expenditure, rely on low operational complexity, and offer modest GDP sensitivity, leading to more predictable, inflation-linked potential returns. Value-add strategies require a measure of capital expenditure, offering less predictable income but

Market update

Hang Seng +2%, after a 0.2% gain on Monday.
EURUSD flat, above 1.08 in Asia trade.
Brent crude oil +0.25%, to USD 78.85 a barrel.

What to watch: 29 March 2023

- France March consumer confidence
- ECB's Kazimir speaks

higher targeted returns and some capital appreciation. Finally, opportunistic strategies tend to build new facilities, posing development and cycle risks but offering capital appreciation and yield returns closer to private equity.

So, we think investors should consider infrastructure alongside other income-generating strategies such as direct lending and real estate within a portfolio context.

Investors can gain infrastructure exposure directly or indirectly. For individual investors, direct exposure to the cash flows from utility, communication, or transportation assets can be attained via private market vehicles. We recommend investors focus on maintaining a consistent deployment plan that is in line with long-term investment objectives and diversified across vintages, managers, and regions. More broadly, putting fresh capital to work in private markets in the years following declines in public markets has historically proven to be a rewarding strategy over the long term.

Indirect exposure can be attained via bond or equity markets. For example, in the US REIT sector, we like exposure to communication towers and data centers. Greentech companies are exposed to infrastructure spending on the energy transition, decarbonization, and energy efficiency. We also have a preference for the global utilities and industrials sectors—both are indirect ways of investing in infrastructure and benefiting from increased infrastructure investment.

Finally, while much of this piece has focused on the investment outlook, investors must also consider the risks. These vary depending on the asset and strategy selected, from leverage risks to concentration issues or deal timing. Changes in general business conditions may impact end-user demand, and investors can also face unexpected changes to political or regulatory policies. While these risks cannot be fully eliminated, they can be reduced through strong due diligence, monitoring, and manager selectivity.

Caught our attention

Alibaba reorganization a positive signal for China tech. The Hang Seng Tech index rallied 2.8% Tuesday, led by a 13.5% surge in Alibaba shares after the tech giant announced plans to reorganize its businesses into separate units with their own CEOS and fundraising plans. Alibaba Group will now act as a holding company for the six groups: split across China ecommerce, global ecommerce, cloud computing, logistics, local consumer services, and digital media. The changes come amid signs of easing tech regulatory scrutiny in China, and as a new government in Beijing softens its tone on private sector oversight.

Our view: Without taking any single-stock views, we see several positive potential implications for investors. First, we see tacit regulatory consent for capital market activity and splitting up conglomerates, which could help unlock shareholder value across different units of large-cap tech in China. Second, broadly speaking, spinning off units may help conglomerates lower potential regulatory risk, unlock trapped values at the conglomerate level, and reduce the regulatory risk discount conglomerates have faced. With both MSCI China and China's tech sector trading at historically undemanding valuations, this action could encourage international investors to revisit fundamental valuations. We remain most preferred on China equities in our Asia strategy, and on emerging market equities in our global strategy.

The energy transition. Canada's newly-announced federal budget features some USD 83bn in green investment tax credits, including support for equipment used to produce and transmit clean energy, to manufacture EVs, or to extract key transition minerals. Alongside speeding the transition to zero-emissions, the subsidies appear aimed at closing the gap with generous US subsidies under the Inflation Reduction Act. Elsewhere, Australian lithium miner Pilbara Minerals announced plans to spend USD 375mn on a new processing plant, with plans to nearly double its lithium output by 2025. Earlier in the week, rival lithium producer Liontown rejected a takeover bid from US producer Albermarle.

Our view: State-level policies on critical minerals and EV production have taken on a new urgency amid concerns over national security, market dominance, and supply chain resilience. We expect global EV sales to reach at least 50% auto market share in 2030, and that continued demand for transition metals will help underpin the structural bull case for commodities. With strong capital commitments from governments and businesses alike, we continue to believe that sustainability should be a key long-term driver of investment returns. We see strong tailwinds for associated longer-term investment themes, from smart mobility and greentech to clean air, as well as carbon reduction and energy efficiency.

Non-Traditional Assets

Non-traditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments). Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

Interests in alternative investment funds are not deposits or obligations of, or guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board, or any other governmental agency. Prospective investors should understand these risks and have the financial ability and willingness to accept them for an extended period of time before making an investment in an alternative investment fund and should consider an alternative investment fund as a supplement to an overall investment program.

In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- Hedge Fund Risk: There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, "junk bonds," derivatives, distressed securities, non-U.S. securities and illiquid investments.
- Managed Futures: There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
- Real Estate: There are risks specifically associated with investing in real estate products and real estate investment trusts. They involve risks associated with debt, adverse changes in general economic or local market conditions, changes in governmental, tax, real estate and zoning laws or regulations, risks associated with capital calls and, for some real estate products, the risks associated with the ability to qualify for favorable treatment under the federal tax laws.
- Private Equity: There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
- Foreign Exchange/Currency Risk: Investors in securities of issuers located outside of the United States should be aware that even for securities denominated in U.S. dollars, changes in the exchange rate between the U.S. dollar and the issuer's "home" currency can have unexpected effects on the market value and liquidity of those securities. Those securities may also be affected by other risks (such as political, economic or regulatory changes) that may not be readily known to a U.S. investor.

Appendix

UBS Chief Investment Office's ("CIO") investment views are prepared and published by the Global Wealth Management business of UBS Switzerland AG (regulated by FINMA in Switzerland) or its affiliates ("UBS").
The investment views have been prepared in accordance with legal requirements designed to promote the **independence of investment research.**
Generic investment research – Risk information:
This publication is **for your information only** and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product. The analysis contained herein does not constitute a personal recommendation or take into account the particular investment objectives, investment strategies, financial situation and needs of any specific recipient. It is based on numerous assumptions. Different assumptions could result in materially different results. Certain services and products are subject to legal restrictions and cannot be offered worldwide on an unrestricted basis and/or may not be eligible for sale to all investors. All information and opinions expressed in this document were obtained from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to its accuracy or completeness (other than disclosures relating to UBS). All information and opinions as well as any forecasts, estimates and market prices indicated are current as of the date of this report, and are subject to change without notice. Opinions expressed herein may differ or be contrary to those expressed by other business areas or divisions of UBS as a result of using different assumptions and/or criteria.
In no circumstances may this document or any of the information (including any forecast, value, index or other calculated amount ("Values")) be used for any of the following purposes (i) valuation or accounting purposes; (ii) to determine the amounts due or payable, the price or the value of any financial instrument or financial contract; or (iii) to measure the performance of any financial instrument including, without limitation, for the purpose of tracking the return or performance of any Value or of defining the asset allocation of portfolio or of computing performance fees. By receiving this document and the information you will be deemed to represent and warrant to UBS that you will not use this document or otherwise rely on any of the information for any of the above purposes. UBS and any of its directors or employees may be entitled at any time to hold long or short positions in investment instruments referred to herein, carry out transactions involving relevant investment instruments in the capacity of principal or agent, or provide any other services or have officers, who serve as directors, either to/for the issuer, the investment instrument itself or to/for any company commercially or financially affiliated to such issuers. At any time, investment decisions (including whether to buy, sell or hold securities) made by UBS and its employees may differ from or be contrary to the opinions expressed in UBS research publications. Some investments may not be readily realizable since the market in the securities is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. UBS relies on information barriers to control the flow of information contained in one or more areas within UBS, into other areas, units, divisions or affiliates of UBS. Futures and options trading is not suitable for every investor as there is a substantial risk of loss, and losses in excess of an initial investment may occur. Past performance of an investment is no guarantee for its future performance. Additional information will be made available upon request. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in foreign exchange rates may have an adverse effect on the price, value or income of an investment. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information.
Tax treatment depends on the individual circumstances and may be subject to change in the future. UBS does not provide legal or tax advice and makes no representations as to the tax treatment of assets or the investment returns thereon both in general or with reference to specific client's circumstances and needs. We are of necessity unable to take into account the particular investment objectives, financial situation and needs of our individual clients and we would recommend that you take financial and/or tax advice as to the implications (including tax) of investing in any of the products mentioned herein.
This material may not be reproduced or copies circulated without prior authority of UBS. Unless otherwise agreed in writing UBS expressly prohibits the distribution and transfer of this material to third parties for any reason. UBS accepts no liability whatsoever for any claims or lawsuits from any third parties arising from the use or distribution of this material. This report is for distribution only under such circumstances as may be permitted by applicable law. For information on the ways in which CIO manages conflicts and maintains independence of its investment views and publication offering, and research and rating methodologies, please visit www.ubs.com/research-methodology. Additional information on the relevant authors of this publication and other CIO publication(s) referenced in this report; and copies of any past reports on this topic; are available upon request from your client advisor.
Options and futures are not suitable for all investors, and trading in these instruments is considered risky and may be appropriate only for sophisticated investors. Prior to buying or selling an option, and for the complete risks relating to options, you must receive a copy of "Characteristics and Risks of Standardized Options". You may read the document at https://www.theocc.com/about/publications/character-risks.jsp or ask your financial advisor for a copy.
Investing in structured investments involves significant risks. For a detailed discussion of the risks involved in investing in any particular structured investment, you must read the relevant offering materials for that investment. Structured investments are unsecured obligations of a particular issuer with returns linked to the performance of an underlying asset. Depending on the terms of the investment, investors could lose all or a substantial portion of their investment based on the performance of the underlying asset. Investors could also lose their entire investment if the issuer becomes insolvent. UBS does not guarantee in any way the obligations or the financial condition of any issuer or the accuracy of any financial information provided by any issuer. Structured investments are not traditional investments and investing in a structured investment is not equivalent to investing directly in the underlying asset. Structured investments may have limited or no liquidity, and investors should be prepared to hold their investment to maturity. The return of structured investments may be limited by a maximum gain, participation rate or other feature. Structured investments may include call features and, if a structured investment is called early, investors would not earn any further return and may not be able to reinvest in similar investments with similar terms. Structured investments include costs and fees which are generally embedded in the price of the investment. The tax treatment of a structured investment may be complex and may differ from a direct investment in the underlying asset. UBS and its employees do not provide tax advice. Investors should consult their own tax advisor about their own tax situation before investing in any securities.

Important Information About Sustainable Investing Strategies: Sustainable investing strategies aim to consider and incorporate environmental, social and governance (ESG) factors into investment process and portfolio construction. Strategies across geographies and styles approach ESG analysis and incorporate the findings in a variety of ways. Incorporating ESG factors or Sustainable Investing considerations may inhibit the portfolio manager's ability to participate in certain investment opportunities that otherwise would be consistent with its investment objective and other principal investment strategies. The returns on a portfolio consisting primarily of sustainable investments may be lower or higher than portfolios where ESG factors, exclusions, or other sustainability issues are not considered by the portfolio manager, and the investment opportunities available to such portfolios may differ. Companies may not necessarily meet high performance standards on all aspects of ESG or sustainable investing issues; there is also no guarantee that any company will meet expectations in connection with corporate responsibility, sustainability, and/or impact performance.

External Asset Managers / External Financial Consultants: In case this research or publication is provided to an External Asset Manager or an External Financial Consultant, UBS expressly prohibits that it is redistributed by the External Asset Manager or the External Financial Consultant and is made available to their clients and/or third parties.

USA: This document is not intended for distribution into the US and / or to US persons.

For country information, please visit ubs.com/cio-country-disclaimer-gr or ask your client advisor for the full disclaimer.

Version A/2023. CIO82652744