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The Beauty of "Boring:" Why Private Infrastructure Shines in Unpredictable Markets

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In an investment landscape marked by volatility, uncertainty, and a constant demand for returns, "boring" can often be a virtue. Private infrastructure, with its potential for steady returns and relatively low volatility, may offer a measure of consistency for investors seeking stability. As global markets continue to grapple with geopolitical tensions, inflationary pressures, and shifting monetary policies, private infrastructure offers the potential for more resiliency as an asset class, blending consistency with diversification.

The Core Appeal of Private Infrastructure

At its heart, private infrastructure is grounded in essential services. From highways and airports to renewable energy grids and water systems, these investments are tied to the fundamental needs of society. This may translate into more predictable cash flows, often underpinned by long-term contracts or regulatory frameworks.

For instance, toll roads generate revenue based on usage, while energy projects like wind farms benefit from power purchase agreements (PPAs) that lock in prices for extended periods. These historically predictable revenue streams may potentially make private infrastructure an attractive option during times of economic stress when other asset classes may face wild swings in valuation.

The Potential Steady Returns Advantage

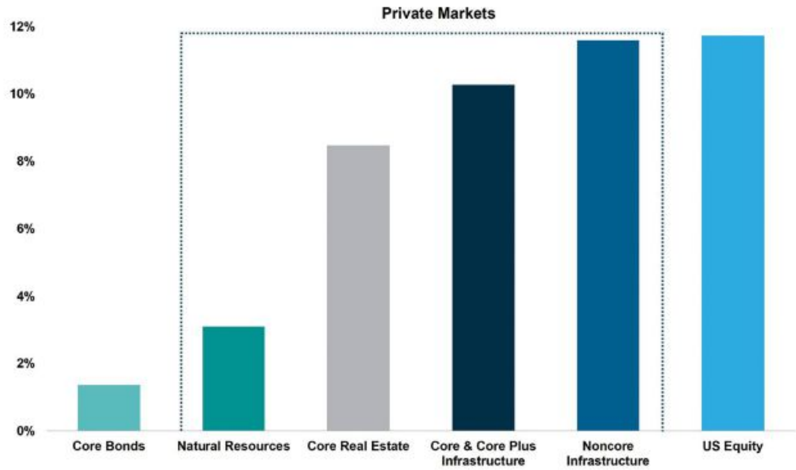
One of the most compelling attributes of private infrastructure is its historical track record of delivering steady returns. Unlike equities, which can be highly sensitive to market sentiment, infrastructure assets may be less prone to sharp fluctuations. This resilience stems from their intrinsic link to economic fundamentals (See Figure 1 to the immediate right).

Even in a downturn, people need electricity, water, and transportation. As a result, the demand for many infrastructure services is inelastic, insulating assets from broader market shocks. For investors seeking to preserve wealth while generating income, this combination of stability and yield may be a winning formula. It's no wonder that institutional investors, such as pension funds and insurance companies, have long favored infrastructure as a core allocation in portfolios.

Diversification Within Infrastructure

While the word "infrastructure" may conjure images of concrete and steel, the asset class is far from monolithic. Investors can tap into a diverse range of opportunities spanning multiple sectors and geographies. Here are some of the key categories (See Figure 2 on the next page).

Looking at History | Trailing 10 Year Annualized Returns (Figure 1)



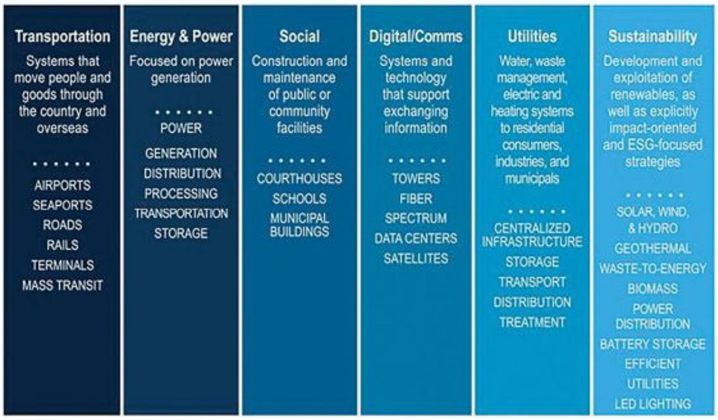
Past Performance is not Indicative of Future Performance. May Lose Value.

Source: Quarterly returns sourced from NCREIF, Bloomberg, and Cambridge Associates via HIS Markit for the period 4/1/2013 to 3/31/2023 (pulled in November 2023 and January 2024). Indices: Cambridge Core & Core Plus Infrastructure Composite, Cambridge Value Add Infrastructure Composite, Cambridge Opportunistic Infrastructure Composite, Cambridge Natural Resources Composite, Russell 3000, Bloomberg US Aggregate Bond Index, NFI-ODCE Value Weighted Net Total Return.

Note: For purposes of return comparison, we linked quarterly IRRs of Natural Resources and Infrastructure as reported by Cambridge Associates. This is because timeweighted returns for these series were not available and the quarterly IRRs used should not differ materially from time-weighted quarterly returns. Note that the trailing returns we present by linking the quarterly IRRs are different from the trailing IRRs as the trailing IRRs are running the calculation over a longer period in which the weighting of cash flows has a more substantial impact.

Note: There is no complete and reliable data set for private investments. The information is extremely limited, and most data is compiled from funds that elect to self-report and tend to be biased toward higher performing funds. Losses are underreported. Funds included in these measures lack commonality and transparency. Over time, components of the data may change. Funds may begin or cease to be represented based on these factors, thereby creating a "survivorship bias" that may additionally impact the data reported.

Breakdown of Infrastructure Sectors and Subsectors (Figure 2)



Source: Meketa Investment Group

This variety allows investors to diversify not only across sectors but also across risk profiles. For example, core infrastructure assets such as utilities may offer lower risk and lower returns, while value-add projects, such as the redevelopment of an aging airport, may carry higher potential returns but also greater complexity.

Inflation Buffer in a Changing Economic Environment

With inflation persisting as a key concern for investors, private infrastructure offers a natural hedge. Many infrastructure assets have revenues directly tied to inflation. For example, toll roads and regulated utilities often include contractual provisions that allow for periodic price adjustments based on inflation indices.

Additionally, infrastructure assets typically have long useful lives and are backed by physical assets, potentially providing inherent value protection. This characteristic is particularly appealing in an environment where inflation erodes the purchasing power of cash and fixed-income investments.

Challenges and Considerations

While private infrastructure may boast many advantages, it is not without potential challenges. These investments are typically illiquid, requiring investors to commit capital for long periods. This characteristic may not suit all investors, particularly those with shorter investment horizons or liquidity needs.

Additionally, the success of infrastructure projects often depends on strong governance and operational expertise. Investors must carefully evaluate the quality of the underlying assets, the experience of the management team, and the regulatory environment in which the assets operate.

Another consideration is the growing focus on sustainability. While renewable energy projects align well with environmental goals, some traditional infrastructure investments, such as fossil fuel pipelines, may face increased scrutiny from regulators and investors alike. Incorporating environmental, social, and governance (ESG) criteria into the investment process is becoming an essential part of managing risk in this space.

Why "Boring" is a Good Thing

In a world where headlines are dominated by market turbulence and uncertainty, the potential reliability of private infrastructure is a refreshing counterpoint. The asset class potentially may offer a blend of stability, income, and diversification that can anchor portfolios in unpredictable times.

For investors seeking to navigate today's complex market dynamics, private infrastructure may represent an opportunity to embrace the "boring" and benefit from its enduring appeal. Whether through transportation networks, renewable energy projects, or digital infrastructure, the historically steady drumbeat of infrastructure returns may provide peace of mind—and long-term financial growth—in an era defined by change.

By leaning into the predictable nature of private infrastructure, investors can unlock its potential to deliver both resilience and value, proving that sometimes, boring truly is beautiful. ■

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