

# THE EUROPEAN SUSTAINABLE INFRASTRUCTURE STRATEGY

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## An introduction

- An exciting time to invest in European infrastructure, with significant growth potential in a continent with a shortfall of infrastructure capital.
- Focus on a portfolio of high-quality, sustainable infrastructure assets to generate stable inflation-linked cashflows across economic cycles.
- Proposed vehicle unique open-ended structure allows assets to be held over the long-term, matching their duration.
- Clear alignment with investors through structure and level of fees.

Europe's economies face a sizeable shortage of infrastructure finance. This presents an attractive opportunity for investors to generate stable, inflation-protected yields over the long term from a portfolio of high-quality 'best-of-class' infrastructure assets.

Columbia Threadneedle Investments is developing an innovative approach to exploit this opportunity. To reflect the multi-decade nature of infrastructure assets, we are proposing the first European infrastructure strategy with an open-ended structure. Additionally, this structure enables active portfolio management, which means the strategy can target low volatility and steady returns more effectively.

The European Sustainable Infrastructure Strategy is a new approach, designed to suit the asset class. The euro-denominated strategy, focused on core assets<sup>1</sup>, will aim to produce a target annual IRR of 8-10% per annum, with a target annual net yield of 5-6% per annum, while protecting capital.

## Why invest in European infrastructure?

Investment in European infrastructure is currently falling far short of what is needed. Public expenditure across Europe stands at 1.25% of GDP, according to the European Investment Bank.<sup>2</sup> Yet, European infrastructure requires an investment of 3.6% of

GDP to keep economies growing. The European Commission estimates that Europe needs €2 trillion of investment in infrastructure by 2020 and that €600 billion needs to be spent annually to keep Europe competitive.

European governments have relatively limited resources, given their restricted ability to raise debts or taxes, creating an attractive opening for institutional investors to provide infrastructure capital.

Europe is also home to some of the highest-quality infrastructure assets globally, ahead of the game in terms of technological innovation and operating in some of the most stable and attractive investment markets in the world.

## What the strategy offers:

### **Attractive target returns**

The European Sustainable Infrastructure Strategy aims to produce attractive risk-adjusted returns and an inflation-linked yield across economic cycles. Columbia Threadneedle intends to achieve this by constructing a diversified portfolio of high-quality infrastructure assets with monopolistic attributes and a focus on sustainability. The strategy will target a net IRR of 8-10% p.a. and a net yield of 5-6% p.a.

### **Active portfolio management**

Contrary to consensus opinion, infrastructure assets do not necessarily insulate investors from economic cycle volatility. Infrastructure is a diverse asset class and different investments, even within a single asset type (transportation, utilities, social infrastructure, renewable energy, telecommunications) are impacted differently by macro influences.

By using dynamic portfolio construction techniques, we aim to deliver robust diversification that will withstand varying macroeconomic conditions. The strategy will combine a bottom-up analysis of yield and return prospects with an in-depth evaluation of cashflow correlations to key macroeconomic movements (GDP growth, interest rate developments and inflation). Portfolio weightings for each investment type will be determined to achieve optimal target returns and yields at reduced volatility across economic cycles.

### **Focus on sustainability**

In infrastructure, sustainability and attractive long-term returns often go hand in hand. Incorporating Environmental, Social and Governance (ESG) criteria into investment analysis and decision making can also mitigate regulatory and political risk. If a project/asset is ecologically and/or socially sustainable there is lesser risk of intervention by politicians or regulatory bodies in the long term.

Columbia Threadneedle aims to optimise sustainability outcomes by seeking exposure to areas which focus on a range of social or sustainability themes. ESG criteria is embedded in the investment decision-making process. Upon acquisition, we will monitor and engage with infrastructure assets to protect their value and promote good governance, employing our extensive industry experience to work with management and incentivise them appropriately.

## **Optimal structure**

The proposed strategy will have an open-ended structure as it is best suited to the nature of the asset and the objectives of institutional investors. By nature, most infrastructure assets are long-term. They have neither a natural end-point nor a transformation point, which at some point in the future would require an exit. Likewise, most investors are interested in infrastructure as longer-term investments.

An open-ended structure matches the long duration of infrastructure assets with investment horizons.

Further, it provides scope to adjust the portfolio. This will be critical to minimise volatility across economic cycles.

## **Clear alignment**

A management fee of 1%, on invested capital only, incentivises long-term investment. There will be no commitment fees and the management fee will not increase with NAV, rewarding early investors by minimising the 'J-curve' or fee drag on investment returns.

Columbia Threadneedle's profit share of 15% is conditional upon achieving an excess cash yield above inflation<sup>3</sup> plus 2% per annum. This aligns the manager's incentives with the strategy's yield focus. Given the strategy also has a growth objective, profit share will also be conditional on achieving a net IRR of 8% per annum.

## **Experienced infrastructure team**

Heiko Schupp, Global Head of Infrastructure Investments, has more than 23 years' experience of investing in infrastructure, including senior roles at market-leading practices. He will be able to leverage the wider resources of the Columbia Threadneedle Investments group, drawing on a range of expert perspectives. This includes the ESG team led by Iain Richards and macro research capability led by Adrian Hilton.

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