THE ALTERNATIVE
INVESTMENTS PLATFORM

An Overview of Private Infrastructure

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An Obsiido Whitepaper

Part 1. Why Private Infrastructure?

While infrastructure has assumed a steadily increasing weight in many institutional investment portfolios in recent years, it has yet to become a staple within the portfolios of individual investors.

Infrastructure falls within the real assets complex, a collection of asset classes that includes real estate and natural resources. Real assets are characterized by their direct connection to an underlying physical or tangible asset and are appealing to investors as they can provide diversification benefits not always available in other asset classes.

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Part 2. What is Private Infrastructure?

Infrastructure assets are irreplaceable networks and systems with stable demand that provide essential services that facilitate economic activity. Typically, they have secure, monopolistic positions with very high barriers to entry and a limited availability of substitutes. A key defining trait of core infrastructure businesses is their long-term, predictable cash flows, which may also benefit from economic growth.

Revenue streams for infrastructure assets tend to sit in one of four categories – contracted, regulated, volume-linked and market-based revenues.

- Contracted and regulated revenues exhibit the lowest level of downside risk, and often include protections against inflation through CPI-linked escalators.
- Volume-linked and market revenues, on the other hand, show a higher level of correlation to economic activity and, as such, present a relatively higher risk profile.

Ultimately, a diversified balance across these different revenue types is key to building a resilient infrastructure portfolio while providing the potential for upside return.

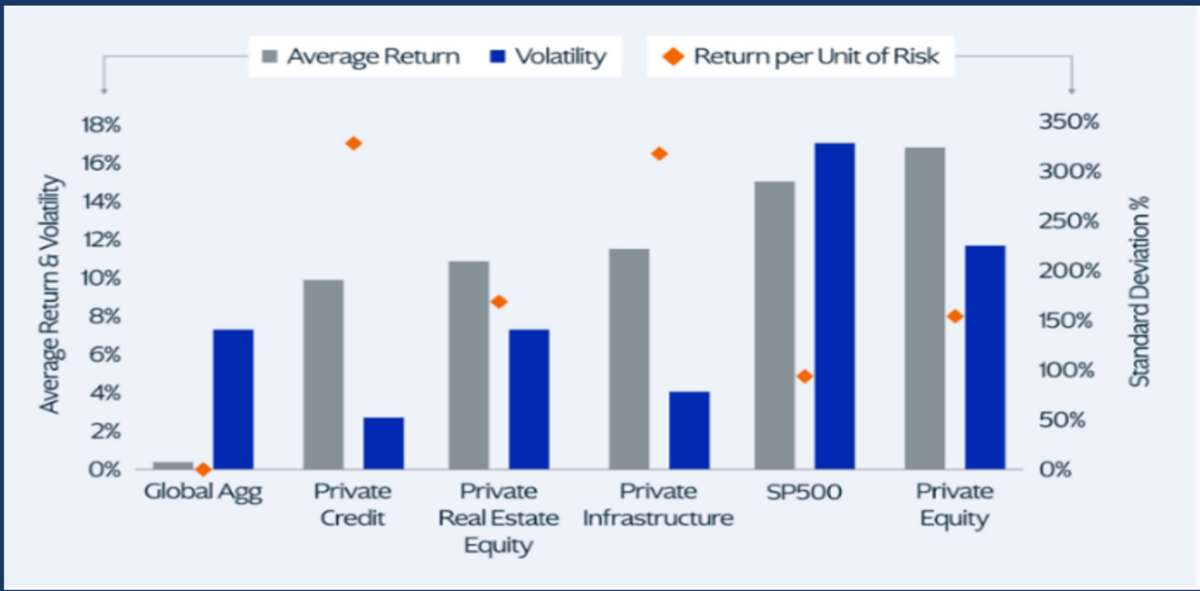
As the infrastructure asset class has matured and evolved, it has expanded in scope in terms of the qualifying asset type. Infrastructure spans a variety of sub-sectors, including the following:

- **Transportation** - airports, toll roads, ports, rail, aviation, shipping
- **Telecommunications** - data centers, wireless network infrastructure, and fiber optic networks
- **Energy & Energy Transition** - renewables, midstream infrastructure, energy storage
- **Utilities** - electricity and gas transition and distribution, district heating, water, and wastewater
- **Industrial & Social Infrastructure** - hospitals, schools, and transport

Part 3. The Investment Case for Private Infrastructure

Relative to other asset classes, private infrastructure has displayed a low level of volatility while also producing attractive returns. As cited in KKR's research paper "Infrastructure: A Potential Shock Absorber", the combination of these two factors resulted in attractive risk-adjusted returns for infrastructure for the period 2012 to 2022.

Asset Class Annual Return and Standard Deviation: 2012-2022
Exhibit 1



Source: KKR Global Macro, Balance Sheet and Risk team. Return Per Unit of Risk is calculated by taking the total return divide by the standard deviation of that return. Data as of December 30, 2022.

Additionally, private infrastructure has exhibited a low level of correlation to other major asset classes, including public equity markets, underscoring its portfolio diversification benefits. According to KKR, based on 20 years of historical quarterly return data, private infrastructure had a return correlation to global public equities of less than fifty percent.

Given the essential nature of infrastructure assets and the durability of their underlying cash flows, the asset class has proven to be resilient in times of economic stress. For example, in 2022 when bond and equity markets sold off aggressively as interest rates rose, private infrastructure was one of the few asset classes to increase in value in that year.[1]

[1]Preqin Global Report on Infrastructure 2024

Part 4. Risk & Return Opportunities

The design of an infrastructure portfolio ultimately must balance the trade-off between income yield and capital gains. Typically, lower-risk assets will generate predictable ongoing cash flow where most of the return is expected to come from yield. Higher risk/return investing will typically generate a greater share of its return from capital gains.

In thinking about infrastructure investments, the market typically categorizes them into three primary buckets: Core, Core Plus and Value-Add.

These can be understood as follows:

Core - Low-risk 'bond-like' defensive assets that generate attractive yields from inflation-linked contracts with high-quality counterparties or regulated assets.

- Essential services with inelastic demand
- Brownfield assets that are operating and generating cash
- Strong barriers to entry due to regulatory and/or contractual frameworks
- Sustainable, long-term cash flows with high operating margins
- Deals utilize low levels of leverage
- Investments focused in developed OECD countries

Core Plus / Value Add - Similarities to core infrastructure but generally include a development or GDP-linkage component.

- Typically, transactions with a greater level of operational complexity
- Value enhancement through an operations-oriented approach
- Return profile with a higher capital gain component
- May include a greenfield (development) component
- Deals may involve higher levels of leverage
- Might include transactions in developing economies

Part 5. General Risks, Infrastructure Investing

Infrastructure is a management intensive asset class where the burdens and responsibilities of ownership are real. Many of the risks associated with infrastructure investing can, of course, be potentially managed by a skilful and experienced infrastructure manager who has extensive operating experience and who can underwrite the risks they identify in a specific asset before they invest. The biggest risk associated with any such investment is the predictability of the underlying cash flows. There are many things that can directly or indirectly affect that, including the following:

- Change in energy prices - a particular infrastructure asset might be highly exposed to commodity price risk.
- Infrastructure investments are subject to different statutory and regulatory regimes which can change unexpectedly.
- Environmental claims arising in respect of infrastructure acquired with undisclosed or unknown environmental problems.
- Investments in infrastructure projects often require development, during which time the asset will generally not be able to generate income.
- The revenue generated by an infrastructure asset may be impacted by the demand for the products or services e.g., traffic volume on a toll road.

In addition to the risks highlighted above, liquidity risk is particularly relevant when it comes to infrastructure investing. Infrastructure assets typically have very long lives and are one of the less liquid alternative asset classes. Typically, institutional investors have invested in infrastructure through closed-end fund structures with up to 12-year terms that offer no interim liquidity. Today, however, individual investors can access investment vehicles investing in infrastructure that are structured as open-end evergreen vehicles that offer greater liquidity options.

Part 6. Summary

Against an uncertain economic backdrop where inflation may well settle in at more elevated levels, the appeal of real assets as a component of a well-diversified investment strategy has only increased. Real assets, such as infrastructure, provide collateral-based cash flows that often have a strong inflation linkage. Moreover, infrastructure today, offers investors exciting investment opportunities in the areas of digitalization, decarbonization and deconsolidation, compelling investment themes that are likely to remain in place for decades to come.

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Obsiido is a technology enabled investment management firm that specializes in researching, structuring, and enabling investments in core alternative investment opportunities within private markets and hedge funds. Obsiido is registered as an investment fund manager in Ontario and as a portfolio manager and exempt market dealer in Ontario, British Columbia and Alberta.

Obsiido is a wholly-owned subsidiary of Obsiido Capital Management Ltd.

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