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"COP26 was an extraordinary opportunity – at a pivotal moment in the climate change crisis – for government and business to work together to solve our greatest climate challenges, while also strengthening economies and communities."
Ralph Izzo, CEO at PSEG
What changed for infrastructure at COP26
Expanding the listed universe
Listed infrastructure in sustainable investing
Not all net zero targets are created equal
GLIO/GRESB ESG 2021 results

Measuring up: the gap between listed and unlisted infrastructure

By *Robert* **CRIMES**

A spate of infrastructure transactions has taken place at premiums to current market prices of listed infrastructure, highlighting a sense that listed infrastructure is deeply undervalued. But what is the best way to measure this valuation gap?

Infrastructure assets are still recovering from COVID-19, but transaction volumes[1] have risen more than threefold since 2019, with acquirers increasingly preying on listed assets such as Autostrade per l'Italia, Sydney Airport, OMA (Mexico) and Ideal Road Builders (India).

Against this backdrop, investors have been looking to define a framework to assess valuation arbitrage between unlisted and listed infrastructure, determine the main drivers and identify undervalued listed companies to seize the opportunities.

Our valuation framework

We have reviewed the 109 largest transactions in 2015-21 across the main sub-sectors within our global infrastructure universe; 25 companies in Toll Roads, Airports and Towers across Europe, South America and Asia Pacific. In Toll Roads and Airports, we have focused on DCF valuations for larger transactions to reflect differences in specific assets, such as concession durations, traffic forecasts, pricing formulae, capex levels and cost of capital but used EV/EBITDA multiples for smaller transactions.

In Towers, EV/EBITDaL multiples (post-cash lease payments, not included under IFRS 16) are more appropriate, given similar characteristics of assets including perpetual durations, similar contracts with telecom operators, inflation-linked pricing, capex levels and cost of capital.

1 As tracked by Insight IR, i.e. our covered companies and other large infrastructure corporates.

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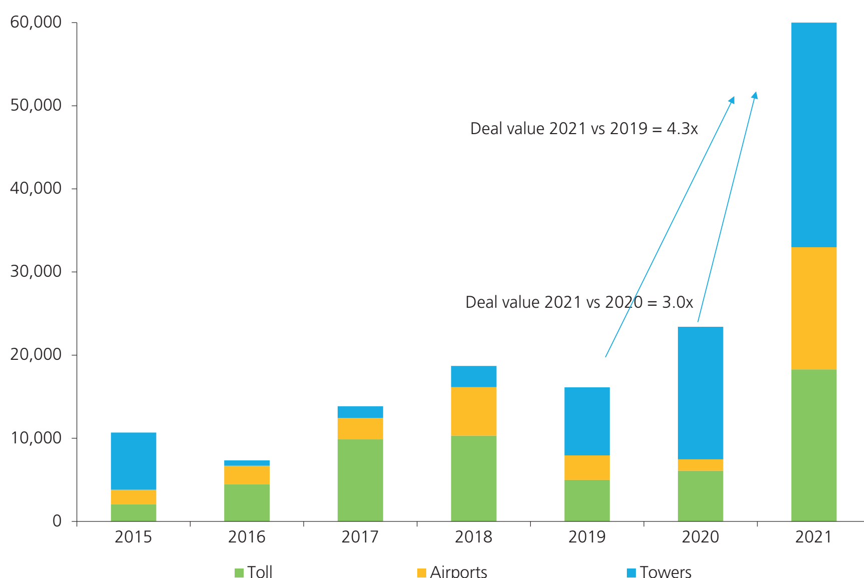
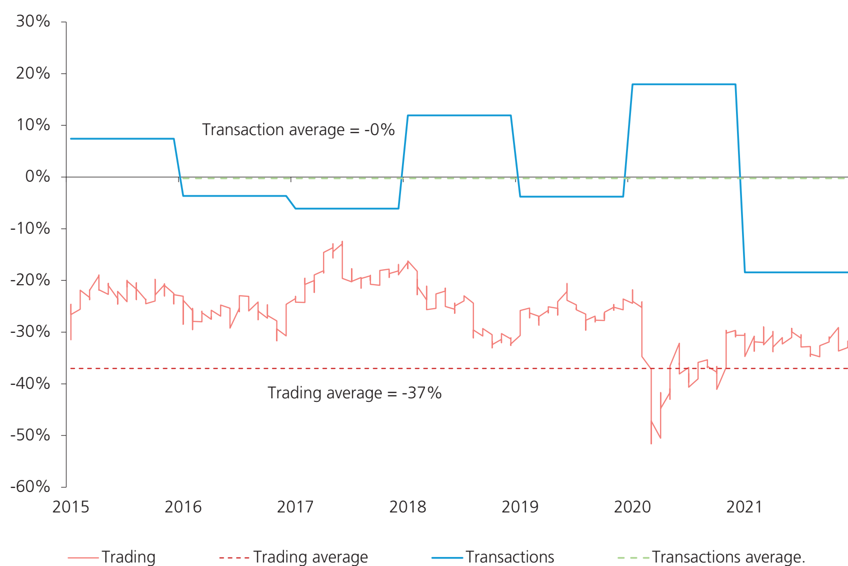
Figure 1: Transaction volumes in overall infrastructure sector (€m)



Source: Insight Investment Research LLP, company data

Figure 2: Listed and transactions' premium/discount to NAV



Source: Insight Investment Research LLP, company data. Rolling six-month average of transactions relative to Insight NAV.

1. More transaction volumes at large premiums to listed infrastructure

Global infrastructure transactions we track reached €58bn in 2021E, a threefold increase on the average annual level in 2019-20 (Figure 1), with a recent trend of listed companies being taken private, such as Autostrade per l'Italia and Sydney Airport.

Our estimates indicate overall listed infrastructure valuations are on average at approx. -30% discounts to transactions valuations, a little below their six-year average of -37% in 2015-21.

We assess valuation for Toll Roads and Airports relative to our NAVs, set by DCF valuations for individual assets or SOTP-based valuations for multi-asset companies, and for Towers based on EV/EBITDaL multiples. We estimate that for listed valuations to close the gap with transaction valuations, listed infrastructure share prices would need to rise approx. 40% in transportation infrastructure. Transactions have been on average at our NAVs, but listed valuations significantly below that level.

We have assessed valuation separately by sub-sector. Regarding Toll Roads, for the larger 19 transactions in 2015-21 – from Australian fund IFM acquiring 25% of Conmex in 2015 to Ferrovial acquiring 25% of Ideal Road Builders in 2021 – our DCF valuations indicated transaction prices were on average only -12% below our Insight NAVs.

However, our listed Toll Road universe currently trades at an average discount to Insight NAV of -40%, with listed share prices needing to rise on average 42% to close the gap versus transactions.

In Airports, for the larger 11 transactions in 2015-21 – from GAP >

acquiring Montego Bay in 2015 to an IFM-led consortium agreeing to acquire Sydney Airport in 2021 – our DCF valuations indicated transaction prices were on average at a 23% premium to Insight NAV.[2]

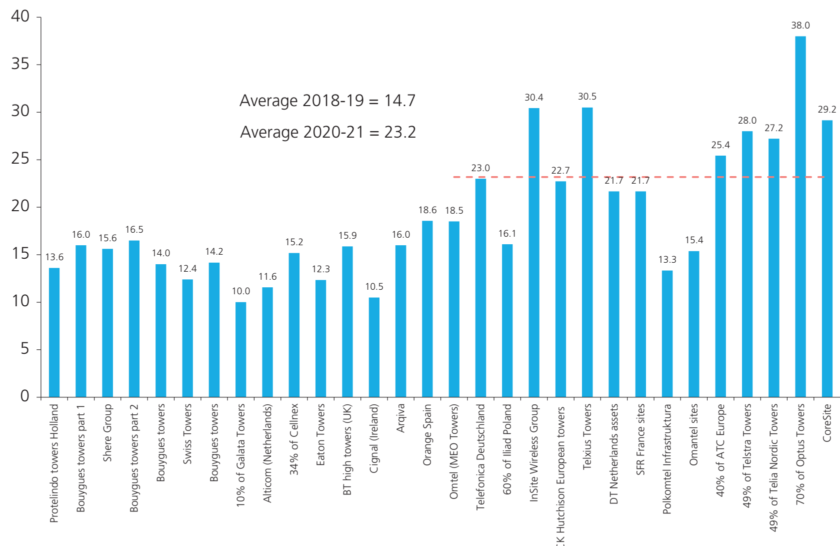
Most notably three deals were at sizeable premiums to our NAVs, namely Vinci's acquisition of 50% of Gatwick, Eiffage's acquisition of 49.99% of Toulouse Airport, and ADP's acquisition of 49% of GMR Airports in India.

However, our listed Airport universe trades at an average discount to Insight NAV of -27%, with listed share prices needing to rise on average 40% to close the gap to our NAVs, or even more to close the gap to transactions.

In Towers, for the larger 30 transactions in 2016-21 – from Cellnex acquiring Protelindo towers in Holland in 2016 to American Tower acquiring CoreSite in 2021 – FY0-FY1 EV/EBITDaL multiples paid averaged 18.8x. However, multiples have risen from an average 14.7x in 2018-19 to 28.0x in 2021.

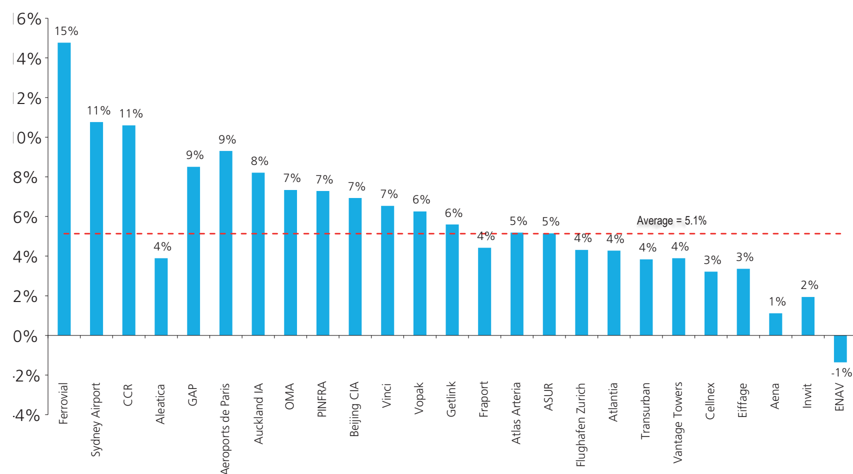
Listed Towers currently trade at an average EV/EBITDaL of 21.6x in 2023E. Share prices need to rise an average 40% to close the EV/EBITDaL gap to transactions in 2021 (based on equity to EV of 75%), but significantly more to close the gap to the average EV/EBITDaL implied by our NAVs for Inwit, Cellnex and Vantage Towers of 38x (Figure 3).

Figure 3: Towers transaction FY0-FY1 EV/EBITDaL multiples



Source: Insight Investment Research LLP, Company data.

Figure 4: Recurring FCF CAGR in 2023-31E by company



Source: Insight Investment Research LLP. Recurring FCF Op FCF minus post interest, tax and maintenance capex.

2. Drivers: low cash-on-cash and strong, reliable free cash flow (FCF) growth

In addition to attractive valuations for listed infrastructure, the recent boom in transactions has two main drivers:

a. Reliable dividend streams: We estimate for our infrastructure universe an average IRR of 8.6%, 310bps above an average cost of equity of 5.4%, indicating high and undervalued lifetime FCF with recurring FCF growth of 5.5% CAGR in 2023-31, and a recurring FCF yield of 7.5% in 2022E, driven by a solid 5.1% CAGR in organic EBITDA in 2024-35E (Figure 4). French toll road APRR provides a good example, having grown traffic consistently at 2.3% CAGR (average GDP multiplier 1.0x) and EBITDA at 2.8% CAGR (traffic, margin enhancement and CPI linkage) in 2002-19. We estimate continued growth in traffic at +1.2% CAGR and EBITDA +2.4% (CPI 1.5% pa) in 2024-34E (Fig-

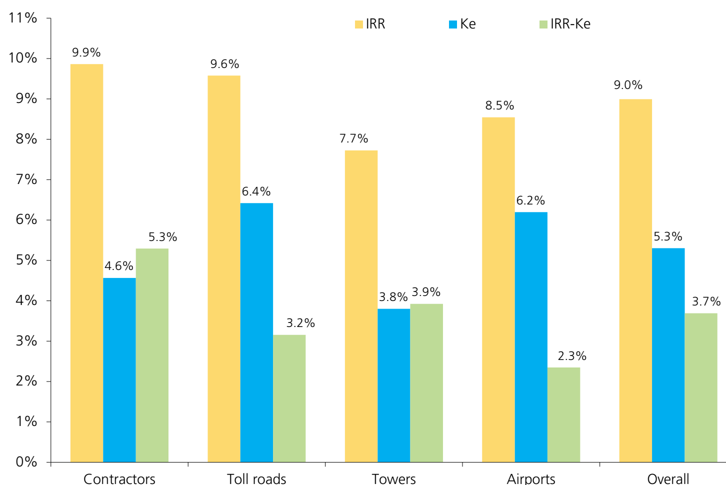
2 Excluding ASPI sale agreed in June 2021 at a price -32% below our NAV due to government pressure.

ure 5). In 1971-2019, surprisingly APRR traffic fell only twice in 50 years (-1.2% in 2008, -1.7% in 2012).

b. Historically low real bond yields contributing to low cost of capital: Real bond yields are key for valuations as we use current nominal bond yields as the risk-free rate of return in our WACCs and revenues mostly linked to inflation, both often with similar sensitivities.

   In developed markets, current nominal ten-year sovereign bond yields of -0.2% to 2.5%, which we mark to market, lead to our low WACCs of 3.0-5.4% and cost of equities of 3.7-6.3%. Indeed, such attractiveness led to the GLIO Infrastructure index providing average annualized returns of 10.6% above the MSCI World Index at 7.1% in 2005-21.

Figure 5: IRRs and cost of equity by sub-sector



Source: Insight Investment Research LLP

3. Inwit, Getlink, Aleatica and Ferrovial: undervalued, arbitrage plays

The growth in infrastructure transaction volumes, mostly at valuations above those of listed counterparts, highlights the depth of the undervaluation of the listed sector. This tallies with our "Overweight" sector rating and our estimated weighted average valuation upside for our global infrastructure universe to reach our NAVs of 65%, with potential for further corporate activity.

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Getlink, Aleatica, Ferrovial and Inwit look attractive in our view, particularly to arbitrage between listed and unlisted valuations.

Getlink NAV €28, +115%) in our view has two core shareholders potentially looking to redeploy excess capital – Atlantia, with a 15.5% holding, and Eiffage with 5%. Atlantia has raised approx. €8bn from selling ASPI, and we estimate Eiffage will receive €2.8bn in 2021-25E from APRR distributions. An acquisition of Getlink would increase their average concession durations as its key Eurotunnel concession does not expire until 2098.

In Mexico, unlisted fund IFM may acquire its non-owned 14% of Aleatica (NAV M$50, +170%) to delist it. We consider Ferrovial (NAV €63, +145%) attractive given its unique position in North American toll roads with congestion pricing and high valuation upside, although it has a large market cap of €19bn.

We expect continued high transaction volumes in Towers, given efficiency benefits from combining networks and raising tenancy ratios, with Cellnex likely to continue to benefit most as an acquirer. Inwit (NAV €20.9, +100%) may be a potential target for Vantage Towers (33.2% holder) to diversify outside its key dominant market in Germany. We see less scope for transactions in European Airports due to a large degree of state ownership. We do not expect state sales of Zurich Airport and Fraport, but of ADP and Aena potentially in the long term, subject to future government strategy.

Robert Crimes

Robert Crimes founded Insight Investment Research LLP, an independent advisory boutique for listed and unlisted infrastructure investors, in 2013. His aim was to provide an alternative focus on lifetime free cashflows, in contrast to investment banks. He has 23 years infrastructure-related investment experience and holds a BSc in Management Science from Warwick Business School.