Why Infrastructure and Why Now?

For a Limited Time Only: Secular Growth Is On Sale

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In this paper, we examine the future of Global Listed Infrastructure, as the combination of emerging secular growth and the current market reaction to COVID-19 has revealed a generational investment opportunity in the asset class.

A Perfect Storm for Opportunity

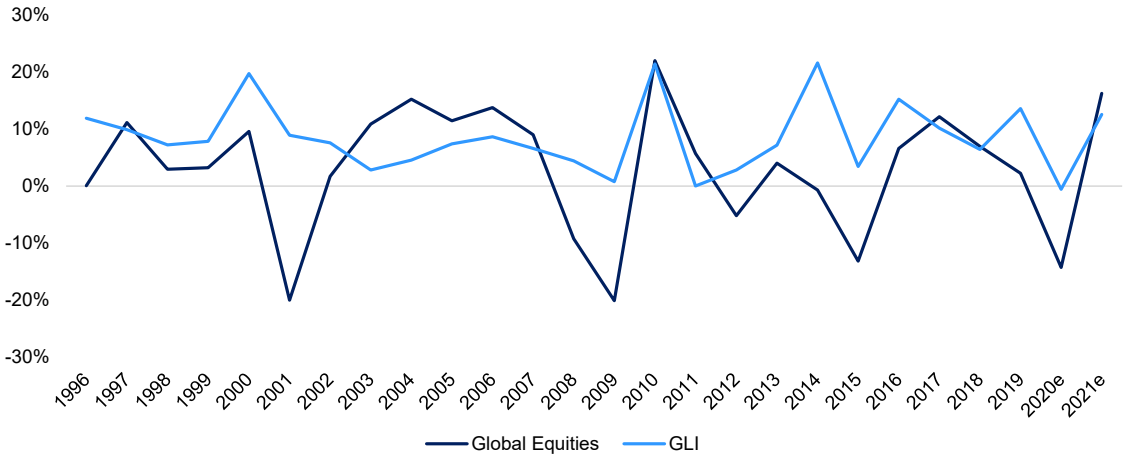
As global markets consolidate in the eventual aftermath of the COVID-19 pandemic, investors should focus their attention on what we regard as the highly advantaged cyclical and secular position in which the Global Listed Infrastructure ("GLI") universe finds itself. Over the next two decades, a reimagining of the global economy, spurred by a decarbonization effort that is already underway, will completely transform the nature of energy production and consumption, requiring massive investment in clean energy, power grids, transportation platforms, and data needs. GLI sits at the nexus of these changes, and we believe there is no group of companies and industries that is better poised to benefit from this shift. The forthcoming investment dynamics should drive above-market cash flow and earnings growth, leading to strong absolute and relative return opportunities for the asset class over the next decade and beyond.

From this vantage point, GLI looks particularly compelling. While GLI's cash flows have outperformed the broader market during this period of stress, the stocks are generally lagging those same broader markets. We see this underperformance as unsustainable, and indicative of an opportune time to allocate to the GLI asset class. From a macroeconomic perspective, we expect global central bank policies to be highly accommodative for some time, keeping interest rates low. The bounce in global markets should consolidate, if not subside, and secular growth should resume. In short: the cyclical and the secular dynamics are lining up to provide what we believe to be an attractive entry point to an asset class that might be the biggest winner in the budding stages of a global transformation story.

A History of Higher Quality and Durable Growth

Throughout economic cycles, GLI cash flows have traditionally grown and outperformed the cash flows of global equities. Using EBITDA as a proxy, Exhibit 1 shows cash flow growth through 2019 and includes forecasts based on both consensus and CenterSquare estimates for 2020 and 2021.

Exhibit 1: Y/Y EBITDA Growth - GLI vs Global Equities



Source: Bloomberg, CenterSquare estimates. Global equities represented by MSCI ACWI. GLI is represented by the FTSE Developed Core Infrastructure 50/50 Net Tax Index. Figures as of June 29, 2020. The above illustrations include forward looking information. Actual results may be materially different than these estimates. Please refer to definition of indices at the end of this document.

GLI's cash flow growth over time is unsurprising given its long-term assets—telecom, utilities, transports, and energy infrastructure — have produced stable, inflation-linked cash flows, providing essential services for which demand is largely inelastic. Historically, cash flows have grown at steady high single to low double digit rates, which when coupled with GLI's yield has provided a compelling total return.

Almost overnight, the landscape has shifted substantially. Today's economic crisis has been without precedent and has affected multiple asset classes in unforeseen ways. We have never seen national economies shut down, shelter-in-place mandates, and swaths of "non-essential" services shuttered on such a scale. In Exhibit 2, we examine GLI's cash flow performance by sector leading into this recession, and our expectations for its growth as we emerge.

Exhibit 2: GLI Earnings or Cash Flow Growth by Sector

Sector	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Transports	15.2%	4.8%	6.0%	11.5%	5.3%	5.8%	10.0%	9.6%	4.2%	-17.4%	20.4%	13.5%
Energy	18.7%	-0.8%	2.6%	11.9%	18.3%	12.0%	9.6%	12.2%	4.4%	-0.4%	3.1%	3.6%
Telecom	15.3%	22.4%	6.3%	19.8%	18.6%	23.3%	6.3%	11.9%	8.1%	5.0%	4.4%	7.2%
Utilities	5.6%	1.9%	1.7%	3.7%	2.2%	5.4%	3.9%	4.6%	3.3%	1.5%	7.1%	5.4%

Source: Bloomberg, CenterSquare estimates. The above illustrations include forward looking information. Actual results may be materially different than these estimates. Figures as of June 29, 2020.

The cash flows for GLI demonstrates the durability of the asset class, as it has strongly outperformed broader markets during the crisis thus far. Utilities, telecom, and energy are flat to growing. Transports have been the only notable weak patch, and perhaps rightly so. Prior to the COVID-19 pandemic, global airport traffic growth naturally showed cyclical sensitivities to recessions and major geopolitical crises, but it had never halted. Still, we do not believe the performance of transports in 2020 will impair GLI over the long term. Moving forward, even if one believes that air traffic will take years to recover, (a notion we subscribe to) or that toll road gains won't offset massive declines in air travel or mass transit, it is reasonable that transport growth of all stripes should rebound strongly irrespective of a vaccine in the near-term, and more durably once one is available, likely in 2021. Specifically, we see a 2021 transport recovery as providing a cyclical boost to GLI's existing and emerging secular growth.

Refer to important disclosures at the end of this document.

Utilities: A $35 Trillion Green Light to Keep Back the Night

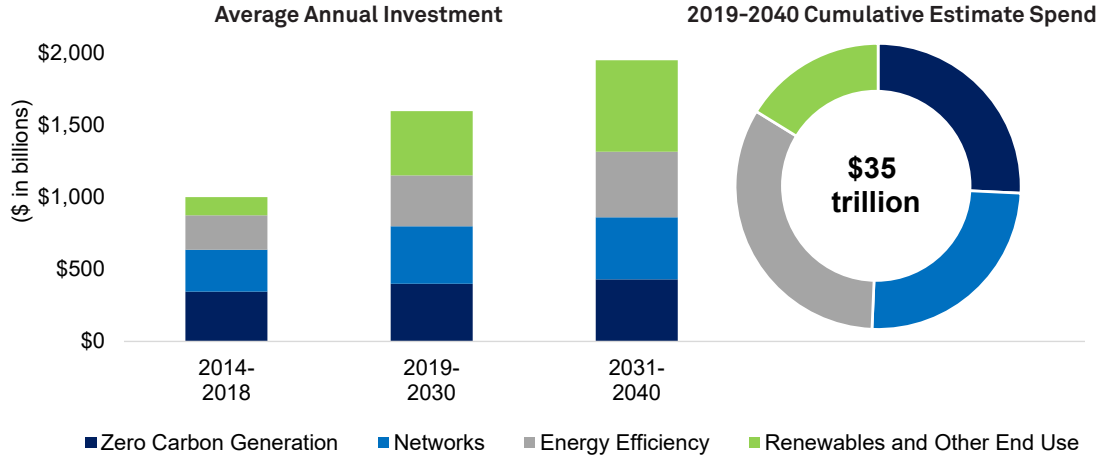
Utilities are the epitome of essential infrastructure, and in this crisis they have provided a light to the world, with governments guaranteeing grid access to all citizens and backstopping payments to energy distributors and utilities. As load growth cyclically recovers in mid-2020 onwards, we expect to see broader utility growth outshine many industries as the secular drivers of renewables deployment, decarbonization, and grid resiliency have only strengthened during this recession. We believe that the utilities sector offers one of the single best growth stories over the next decade, in a space with contracted and regulated returns.

As of May 2020, the European Union ("EU") has drafted a €1.9 trillion COVID-19 response plan, a €750 billion recovery plan and a €1.1 trillion budget. The Green Deal, an EU roadmap to zero net carbon emissions by 2050, is a pillar of this recovery package. The EU believes that meeting 2030 climate goals will help spur GDP and create over 1 million jobs. For a sense of scale, the recovery plan equates to industry analysts forecasting €2.6 trillion of total sector capex through 2050 as part of "must-have" spending. Major companies such as Enel Group, which spends about €9 billion annually, have commented that such proposals could theoretically lead to a doubling in growth opportunities. Even before the EU recovery plan, consensus saw the global renewables developers growing their earnings in the high single digits, investing in assets with a secure and guaranteed return. Recent developments in Europe should only drive this growth higher, with current sensitivities suggesting a potential double-digit growth in earnings.

Recovery packages and stimulus aren't limited to Europe alone. In Australia, the National COVID Coordination Commission is proposing new transcontinental energy pipelines. In Brazil, where COVID-19 cases are increasing, the government is passing legislation to keep utility cash collections intact. In the U.S., renewable tax credits have been extended and rules governing offshore-wind construction continue to lay the foundation for one of the highest infrastructure growth subsectors. Beyond government, the private sector is stepping up through the continued issuance of sustainable debt. These financings are either linked to specific renewable projects, or to a developer's balance sheet, with interest costs often driven by progress on carbon-reduction initiatives. Utility sustainable debt has seen a 70% CAGR[1] in issuance over the last four years, demonstrating robust demand for a combination of defensive and ESG-themed cash flows.

The global recovery packages are merely the tip of the iceberg in the effort to transform worldwide energy production and consumption over the course of the next three decades. Across Europe, the U.S., and other regions, we see the potential for over $1 trillion in utility capital annually, drawing from zero carbon generation, transmission grids, distribution grids, energy efficiency, and charging stations. These plans represent increases of 50-100% over current spending levels and will, at the very least, support current growth levels. Further, the spending will more likely lead to an upward migration in growth from amongst the safest of global sectors, all against the backdrop of massive political support backing up economics and earnings potential for investors. We see renewables and grid modernization as one of the greatest disruption stories for the investible future, representing a fundamental reorganization of global production and consumption of energy in the 21st century, with utility infrastructure companies well-positioned at the center of this wave of investment.

Exhibit 3: Global Green Policies Would Double the Current Rate of Utility Spend



Source: IEA World Energy Outlook 2019, Stated Policies Scenario. The above illustrations include forward looking information. Actual results may be materially different than these estimates.

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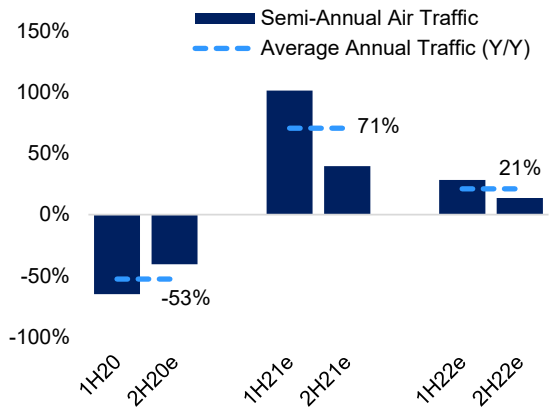
Transports: Venturing Highways

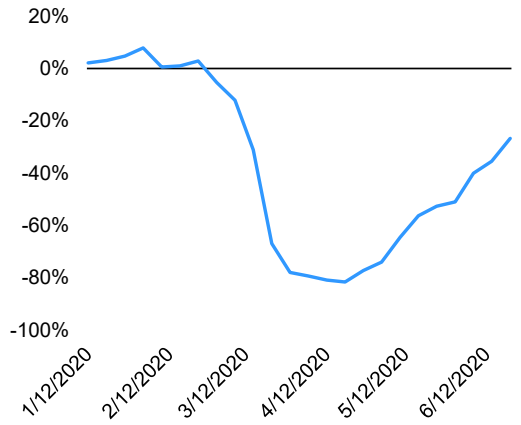
As noted above, transports have cyclically underperformed during COVID-19, but the secular attractiveness of the sector remains intact, with green shoots supporting a near-term recovery on top of sustainable growth longer-term. As counties, states, provinces, and nations ease lockdowns, we expect road traffic and air traffic to recover in any reasonable scenario, with the dependent variable in this equation being time. We view transports as a beneficiary of global privatization trends, the need for increased construction activity to promote GDP recovery and job growth, and the opportunity for modal shifts and cost rationalization to drive market share gains for road and rail.

Exhibit 4: European Airport Traffic - '20 Declines Suggests Strong Rebound Likely in 2021



Source: Company reports, CenterSquare estimates. The above illustrations include forward looking information. Actual results may be materially different than these estimates. Figures as of June 29, 2020.

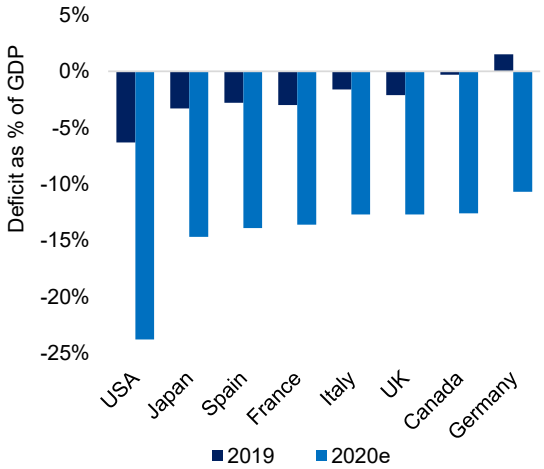
Exhibit 5: 2020 European Road Traffic Already Recovering Toward Growth



Source: Company reports, CenterSquare estimates. Figures as of June 29, 2020.

In the U.S., for instance, federal, state and local government budgets/balance sheets are stretched to their limits because of COVID-19 (Exhibit 6). This significantly increases the attractiveness of allowing private companies to finance new projects to stimulate economic recovery. For example, Maryland recently took a step forward on a $9 billion managed lane project by opening up the bidding process. We have seen this abroad as well, with the Italian government conducting meetings with construction and infrastructure companies to solicit ideas, and with the Canadian government providing a financial backstop to major crude pipelines in the energy sector. Broadly, more greenfield construction means more jobs. Today, governments are working hard to craft new deals for the next decade.

Exhibit 6: Government Budgets Stretched Due to COVID-19



Source: International Monetary Fund. The above illustrations include forward looking information. Figures as of June 29, 2020. Actual results may be materially different than these estimates.

Governments want more work completed on existing infrastructure as well, but the idea of raising tolls on consumers to fund these projects is unworkable. An elegant solution, possibly gaining more traction recently, is for governments to extend existing concessions to private operators in return for infrastructure upgrades. Concession extensions can be significantly accretive to a company's valuation, as the market often values them on a concession-by-concession discounted cash flow model.

Lastly, in terms of modal shifts, the crisis should support a newfound appreciation for roads over air and mass transit as a means of travel in the near-term. Globally, energy refiners have already commented

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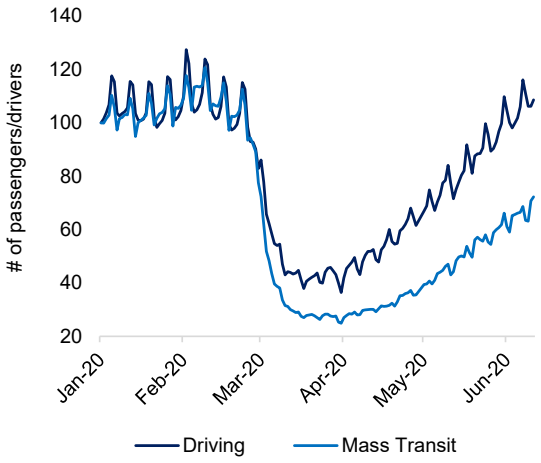
on this development, which is well supported by Apple's mobility data (Exhibit 7) where we see a clear recovery in driving over mass transit. This activity should benefit the publicly listed transport companies, where toll roads make up a greater percentage of their asset base. Modal shifts should continue across industrial freight transportation, as well. In major geographies, we continue to see freight rail gain share at the expense of long-haul trucking, as major businesses look to reduce costs across their logistical network.

Exhibit 7: Driving Continues to Gain Share Over Mass Transit (Indexed to 100)



Source: Apple Mobility. Figures as of June 29, 2020.

Telecom: Can You Hear Me Now?

As of July 2020, the majority of the global workforce is still working remotely, awaiting authorizations and increased comfort levels to reopen offices. We are constantly connected, some on a 5G connection, while in the next room, our children are streaming Netflix and attending virtual summer camps. In today's environment, telecom and data demand feels even more inelastic than electricity demand. We expect the feeling to continue. Even upon the global workforce's return to the office, we expect staggered scheduling, efforts to promote social distancing, and a newfound appreciation for the efficiency of remote workers to promote data usage, which has grown at a 79% CAGR[2] over the last 13 years in the U.S. alone. 5G implementation will be a necessity, and across the U.S., China, and Europe, we are still in the early stages of deployment.

Globally, appreciation for telecom assets is only intensifying, as deal-making has continued without pause through this recession. In prior commentary, we have noted billions in telecom deals in Europe. As recently as late May, we are seeing a pickup in Asia as well, with Google reportedly considering a 5% stake in a major Indian telecom operator, while local Indian telecoms report 20% YoY revenue growth. Google's interest follows KKR, Silver Lake, Vista, and Facebook in making investments in Indian carriers. This activity is validating the choices of publicly listed cell tower bellwethers such as American Tower Corporation.

The overarching point, as it concerns telecom investment and secular demand, is that between growth in data usage and 5G rollout, telecom will continue to be one of the global epicenters of technology investment over the next 20 years. Clearly, GLI stands ready to benefit from this evergreen growth story.

Energy: It's Been a Rough Few Years

Of all the sectors in infrastructure, energy alone tends to offer less of a secular growth story and more of a cyclical one. This year saw unparalleled demand destruction, and a consequential drop in benchmark prices to negative levels. The good news lies in the existence of a solid floor and, since late April 2020, both the commodities and the sector have had a hard bounce. As of July 2020, both have recovered to levels seen in early March. At that point, OPEC and Russia (OPEC+) had a falling out that was catastrophic, creating perhaps the worst-timed supply glut in the history of global crude. OPEC+ was eventually able to solve their differences shortly after COVID-19 took center stage, in a key development for cyclical recovery in the energy patch.

The reality that a major geopolitical alliance could collapse and re-form in a few weeks is one of the many reasons we believe midstream can outperform only cyclically, not secularly. Longer-term, the fragility of alliances, the evaporation of the shale growth story, and the growing global decarbonization trend make us question the durability of any rally.

Today, the North American midstream names offer some compelling and sustainable yields. While 40%[3] of midstream companies reduced dividends in Q1'20, the move left survivors on better footing. The C-Corps in our benchmark, the FTSE Developed Infrastructure Core 50/50 Net Tax, offers yields ranging from 5-8%, and those dividends are largely secure with only one potentially cutting, a risk mitigated by a recent equity offering. In the year ahead, North American midstream could still benefit from a cyclical recovery in cash flows against depressed valuations, but we view the sector warily and tactically.

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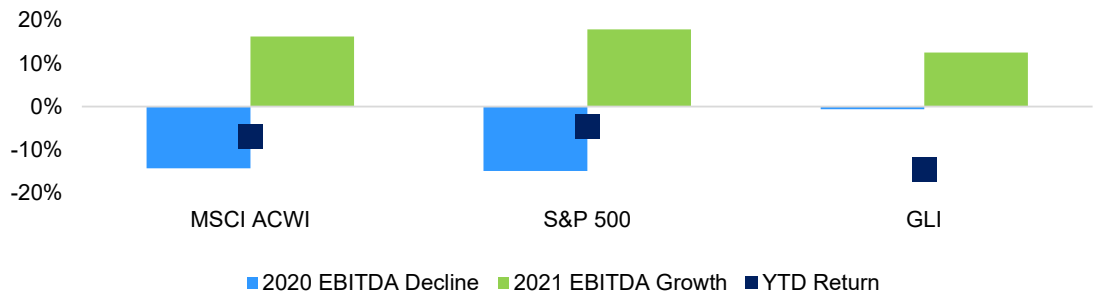
Valuation and Growth: GLI's Winning Combination

Relative to broader equities, GLI is exceedingly discounted for the growth it is positioned to deliver. We expect GLI cash flows to fall 1% this year and recover 13% in 2021 (Exhibit 8). This compares to a 14% decline in 2020 for the MSCI World, according to consensus. Yet, in the very recent cyclical rally, infrastructure has lagged, which is understandable. If the economy is emerging from recession, defensives should lag. However, what is noteworthy, both entering and emerging from this recession, is the speed at which equity prices have moved in both directions. In the space of three months, global markets have discounted both a generational bloodbath and a generational recovery—the latter of which has yet to fully bear out. We would assert that, in some cyclical sectors, the market is discounting perhaps too much of a recovery. As markets potentially consolidate after a strong run, we see this as an opportune time to add to infrastructure allocations.

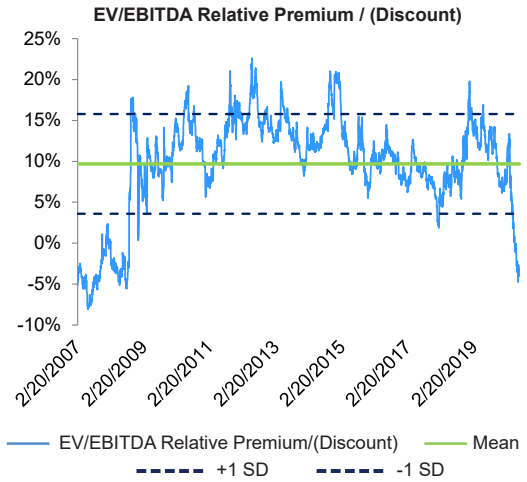
Exhibit 8: GLI Stocks Have Lagged Despite Superior Cash Flow Performance



Source: Bloomberg. As of June 29, 2020. The above illustrations include forward looking information. Actual results may be materially different than these estimates.

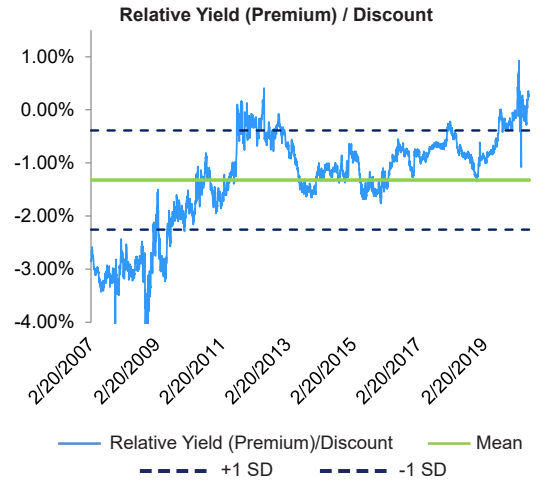
Indeed, taken as a whole, infrastructure is the cheapest it has been in a more than a decade relative to broader markets. Valuation metrics comparing infrastructure equities versus global equities, as well as dividend yields for the infrastructure space, are all exceedingly attractive. Relative, then, to other public market options, infrastructure looks compellingly placed and priced, especially as we see GLI's growth as meeting or leading broader markets on a more secular basis. This growth takes place in an asset class with a return structure far less susceptible to cyclical swings than broader equities, and at a discounted relative valuation due to the speed and magnitude of the recent market recovery.

Exhibit 9: EV/EBITDA - GLI vs MSCI World – Cheapest Since 2008



Note: Relative EV/EBITDA Premiums/Discounts are calculated using the MSCI World and the average of the FTSE Developed Core Infrastructure 50/50 Net Tax Index, S&P Global Infrastructure Index, Dow Jones Brookfield Global Infrastructure Total Return Index, FTSE Global Infrastructure Index (for years in which individual historical index data is available). Figures as of July 7, 2020. Please refer to definition of indices at the end of this document.

Exhibit 10: Dividend Yields - GLI vs Corporate Spreads Near Cycle Highs



Note: Relative Dividend Yield Premiums/Discounts are calculated using the Moody's Bond Indices Corporate BAA and the average of the FTSE Developed Core Infrastructure 50/50 Net Tax Index, S&P Global Infrastructure Index, Dow Jones Brookfield Global Infrastructure Total Return Index, FTSE Global Infrastructure Index (for years in which individual historical index data is available). Figures as of July 7, 2020. Please refer to definition of indices at the end of this document.

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Conclusion

There are two dimensions to GLI's attractiveness in today's market. First, the assets represent a strong, longer-term value proposition relative to broader alternatives in the equity and debt capital markets due to the unprecedented nature of this particular downturn and its causes. We see these causes and their effects as unique and transitory, with GLI assets benefitting swiftly from recovery. Second, we see infrastructure as perhaps singularly well-positioned to lead in the secular growth of the global economy as it transitions to a cleaner and greener future. Trillions of investment is expected to change the very nature of energy production and consumption, travel and freight transit realities, and the growing intensity of data usage. The positive growth that accompanies this investment, coupled with an intermediate global macro future replete with geopolitical risks, low interest rates, accommodative central bank policies, and lurching periods of economic instability, positions GLI not only as a friendly port in a storm, but a way to obtain maximum leverage to the greening of the 21st century economy -- all in an efficient, risk-adjusted manner.

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[1] Source: Bloomberg New Energy Finance as of June 29, 2020.
[2] Source: American Tower as of December 2019.
[3] Source: Alerian as of June 29, 2020.

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GLI: FTSE Developed Core Infrastructure 50/50 Net Tax Index
Global Equities: MSCI ACWI
Global Infrastructure: For periods after 12/31/2005, FTSE Developed Core Infrastructure 50/50 Net Tax Index. For periods prior to 12/31/2005, Dow Jones Brookfield Global Infrastructure Index.

FTSE Developed Core Infrastructure 50/50 Net Tax Index
The FTSE Global Core Infrastructure 50/50 Index and FTSE Developed Core Infrastructure 50/50 Net Tax Index give participants an industry-defined interpretation of infrastructure and adjust the exposure to certain infrastructure sub-sectors. The constituent weights for these indices are adjusted as part of the semi-annual review according to three broad industry sectors – 50% Utilities, 30% Transportation including capping of 7.5% for railroads/railways and a 20% mix of other sectors including pipelines, satellites and telecommunication towers.

MSCI ACWI
The MSCI ACWI, which is part of The Modern Index Strategy, is a broad global equity index that represents large and mid-cap equity performance across 23 developed markets countries. It covers approximately 85% of the free float-adjusted market capitalization in each country and MSCI ACWI does not offer exposure to emerging markets.

S&P 500
The S&P 500 is an index that is considered to be a gauge of the U.S. equities market. The index includes 500 leading companies spread across the major sectors of the U.S. economy. The index focuses on the larger cap segment of the U.S. market and represents approximately 75% of the market capitalization of U.S. securities. The index is the most notable of the many indices owned and maintained by Standard & Poor's, a division of McGraw-Hill Companies.

S&P Global Infrastructure Index
The S&P Global Infrastructure Index is designed to track 75 companies from around the world chosen to represent the listed infrastructure industry while maintaining liquidity and tradability. To create diversified exposure, the index includes three distinct infrastructure clusters: energy, transportation, and utilities.

Moody's Bond Indices Corporate BAA
The Moody's Seasoned Baa Corporate Bond Yield measures the yield on corporate bonds that are rated Baa. Corporate bonds are rated based on their default probability, health of the corporation's debt structure, as well as the overall health of the economy. The Baa rating is relatively low risk, and is considered investment grade, however it is only one grade above a junk bond rating. An important way to analyze bond yields is spreads between different kinds of bonds. During the financial crisis in 2008-2009, the spread between Aaa and Baa bonds widened because of the unpredictability of bonds and increased default rates.

Dow Jones Brookfield Global Infrastructure Total Return Index
The Dow Jones Brookfield Global Infrastructure Total Return Index measures the stock performance of companies that exhibit strong infrastructure characteristics. The index intends to measure all sectors of the infrastructure market and is weighted by float-adjusted market capitalization. The Dow Jones Brookfield Global Infrastructure Index was first calculated on July 14, 2008.

FTSE Global Infrastructure Index
The FTSE Infrastructure Index Series is a comprehensive set of indexes designed to reflect the performance of listed infrastructure and infrastructure-related listed securities worldwide.

These benchmarks are broad-based indices which are used for illustrative purposes only and have been selected as they are well known and are easily recognizable by investors. However, the investment activities and performance of an actual portfolio may be considerably more volatile than these indices and may have material differences from the performance of any of the referenced indices. Unlike these benchmarks, actual portfolios are actively managed. Furthermore, actual portfolios may invest in substantially fewer securities than the number of securities comprising each of these benchmarks. There is no guarantee that any of the securities invested in by actual portfolios comprise these benchmarks. Also, performance results for benchmarks may not reflect payment of investment management/incentive fees and other expenses. Because of these differences, benchmarks should not be relied upon as an accurate measure of comparison.

A direct investment in an index is not possible.

About CenterSquare

Founded in 1987, CenterSquare Investment Management is an independent, management-owned real asset manager focused on listed real estate, private equity real estate, private real estate debt and listed infrastructure investments. As an investor and manager, our success is firmly rooted in aligning our firm's interests with those of our clients, partners and employees, as well as our commitment to alpha-generating research.

CenterSquare Investment Management is headquartered in suburban Philadelphia, with offices in New York, Los Angeles, London and Singapore. CenterSquare is proud to manage investments on behalf of some of the world's most well-known institutional and private investors.

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