



# PUBLIC POLICY, POPULIST POLITICS & COVID-19

Will infrastructure be the centrepiece by which governments stimulate their economies?



## Agenda

### **Shorter term, COVID-19 impact and response:**

- likely nature of government stimuli
- ESG and COVID-19, social licence to operate
- short and long of public sector response...

### **Longer term, populist politics and public policy direction:**

- substantial private market funded Infrastructure
- what to watch for investors

# Shorter Term, COVID-19 Impact & Response



# Will Infrastructure Be The Centrepiece Governments Stimulate Their Economies With?

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**Yes, but there are some subtleties...**

Near-term stimulus will be about getting people back to work

- ❖ hundreds of small projects dotted around the country
- ❖ focused on SMEs and local communities
- ❖ highly cyclical – contractors, engineering, aggregates, materials, local labour, etc.

Bigger opportunity is longer-term direction of public policy and populist politics

- ❖ climate change has been and will continue to drive infrastructure investment
- ❖ toward net zero by 2050 creates a significant target and accelerates investment
- ❖ variations on the Green New Deal thematic around the globe.

# Response to COVID-19 and ESG Implications for Corporates and Shareholders

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## ESG vs Sustainable Investing

'ESG' investing has **morphed into a broader 'Sustainable'** movement

- ❖ Heavy focus on the 'E'
- ❖ COVID-19 is bringing 'S' and 'G' considerations to the fore

**RARE's sustainable approach** has included ESG pricing since inception, but similarly has evolved

- ❖ Longer-term impacts on cash flows
- ❖ Adjustment to the cost of capital
- ❖ Deeper engagement with all stakeholders

## Stakeholders vs Shareholders

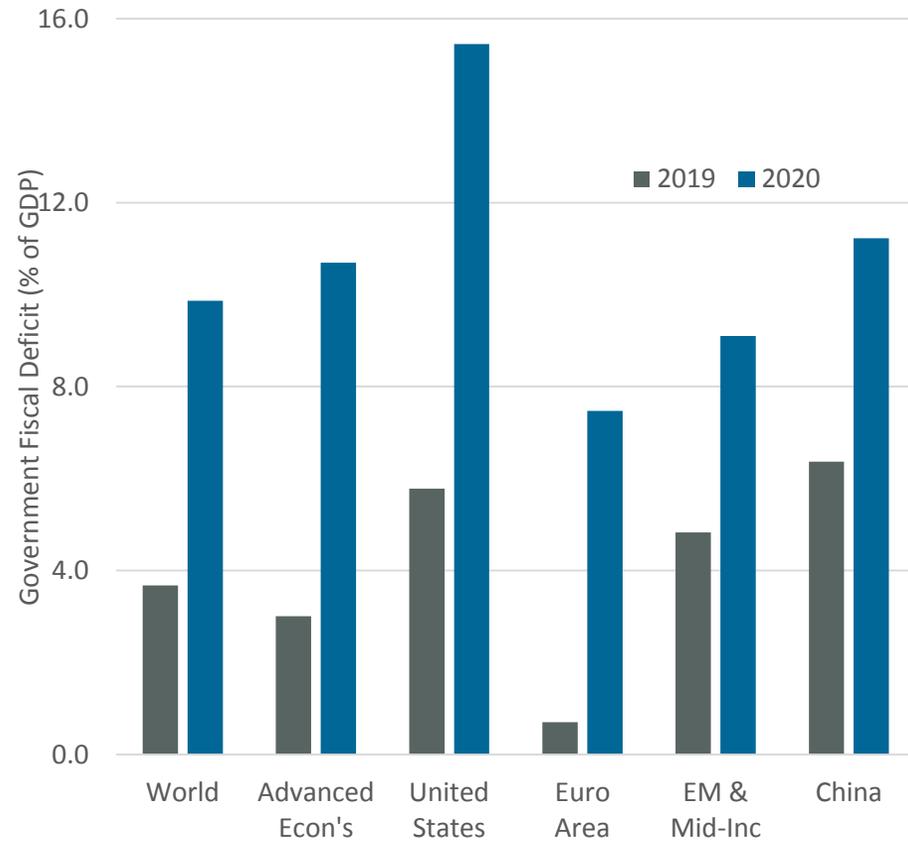
COVID-19 has accelerated the trend towards **Stakeholder Capitalism**

- ❖ Retooling to make PPE, providing goods/services to stakeholders free of charge, executive remuneration
- ❖ Government support will likely be exchanged for implicit or explicit erosion of shareholder rights

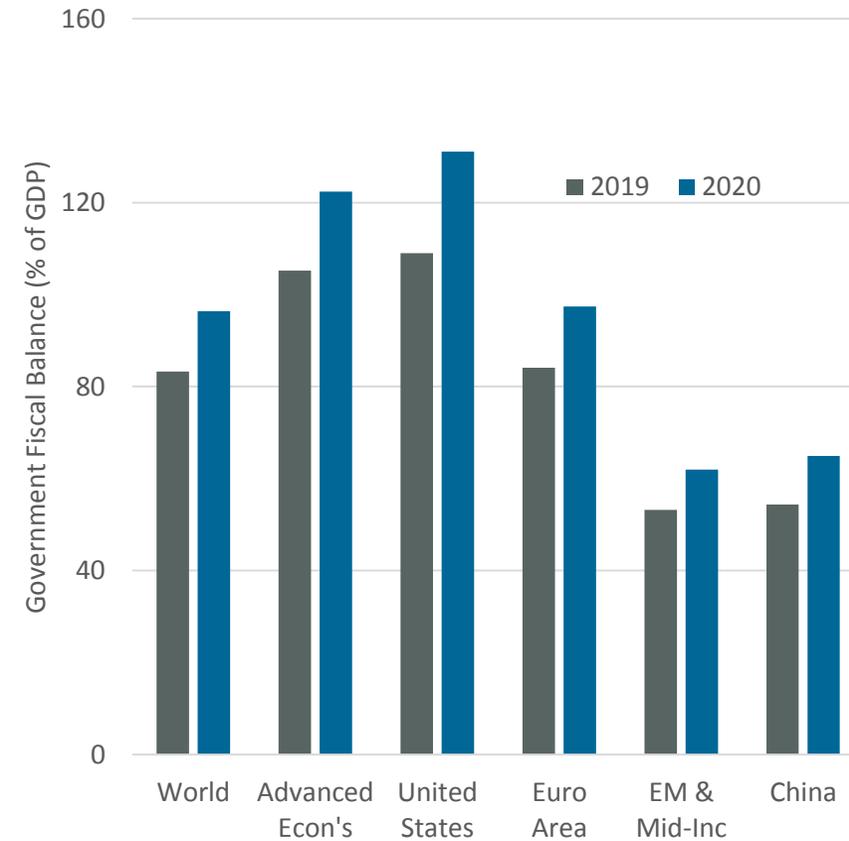
**Infrastructure is uniquely positioned to manage this transition** - has been doing so for years in balancing contracts with government (toll road companies) and regulatory stakeholders

# Short-Term Government Response to COVID-19 Crisis, More Debt...

## Government Fiscal Deficits (as %GDP)



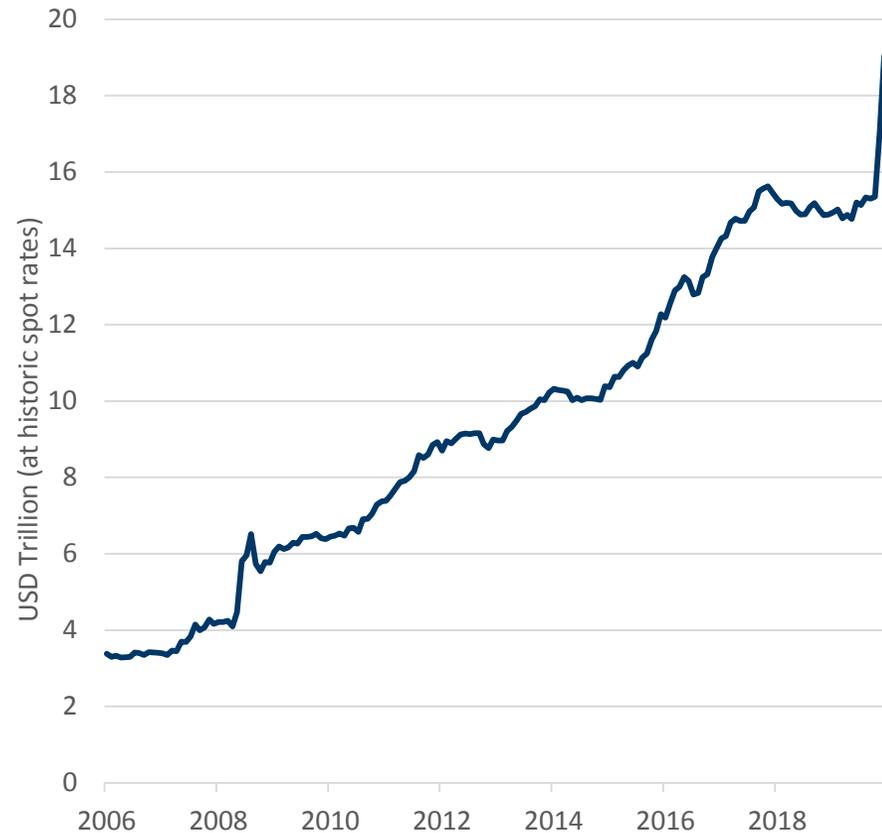
## Government Debt (Gross, as %GDP)



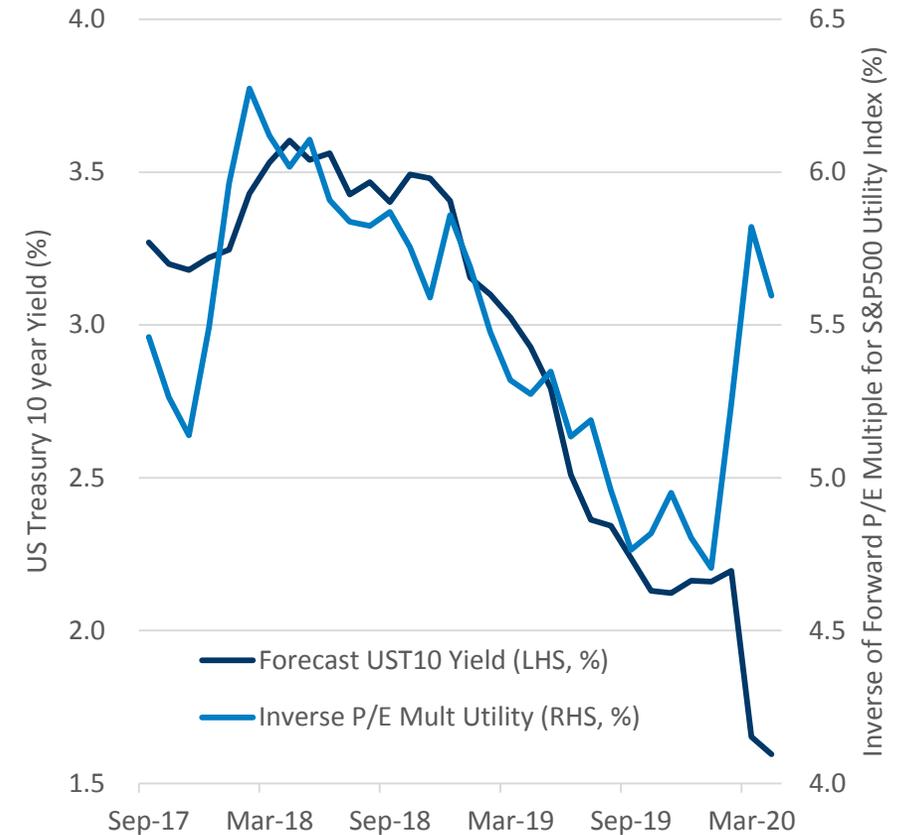
# Longer-Term Impact of More Debt at Governments and Larger Central Bank Balance Sheets

## Central Banks Balance Sheet Growth 2006-20

Fed, ECB, BOJ, PBoC and BOE (USD, trillion)



## Forecast UST10 Yield vs Inverse Utility P/E



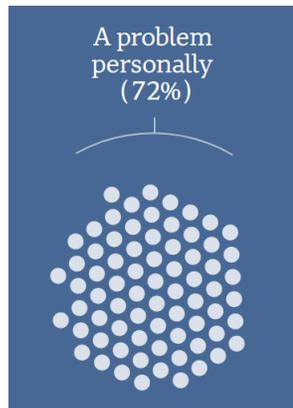
# Longer Term - Populist Politics & Public Policy



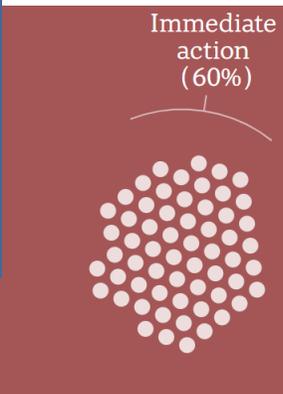
# The Push: Importance of Climate Change to the Population of Voters...and Customers

## Australian Voter Attitudes (ABC, Feb 2020)

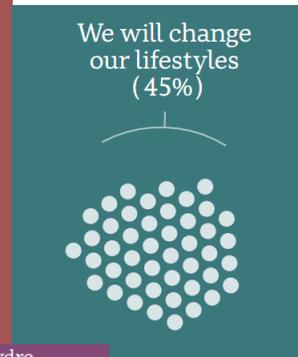
Out of 100 people in Australia, climate change is...



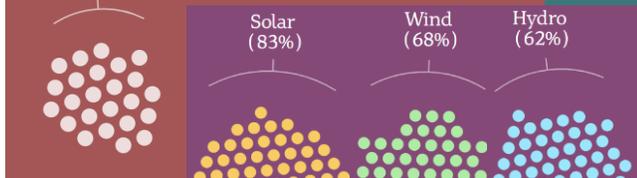
And 84% want immediate (or at least) some or action



To reduce energy consumption...



Some action (24%)

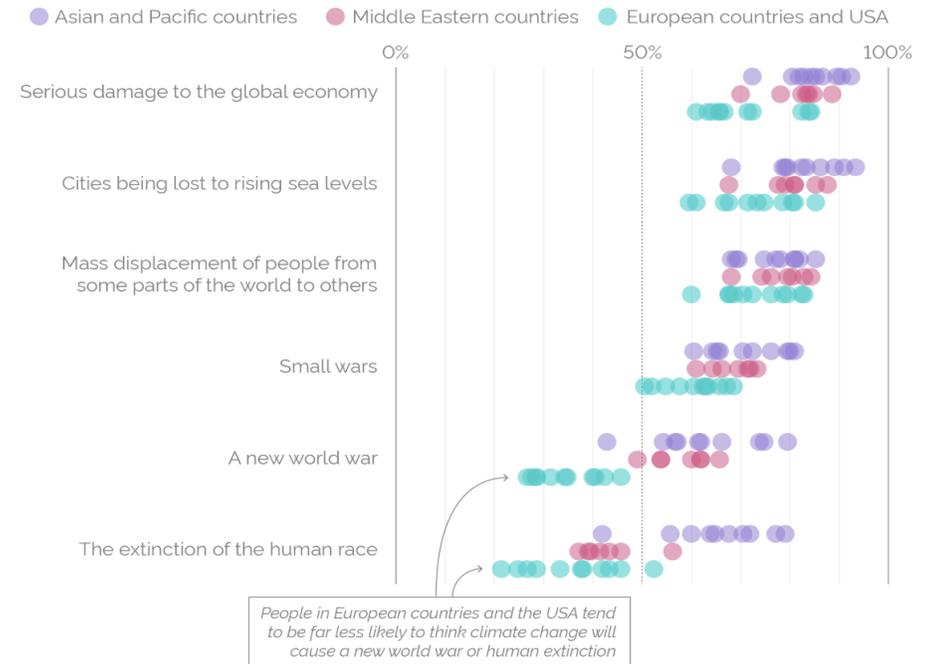


Additional types of energy we should rely on...

## Global Attitudes (YouGov, June-July 2019)

**A majority of people in 28 countries think climate change is likely to cause serious economic damage, destroy cities and start wars**

How likely do you think it is that climate change will cause each of the following? % in each country who said "very likely" or "quite likely"



YouGov

11 June - 22 July 2019

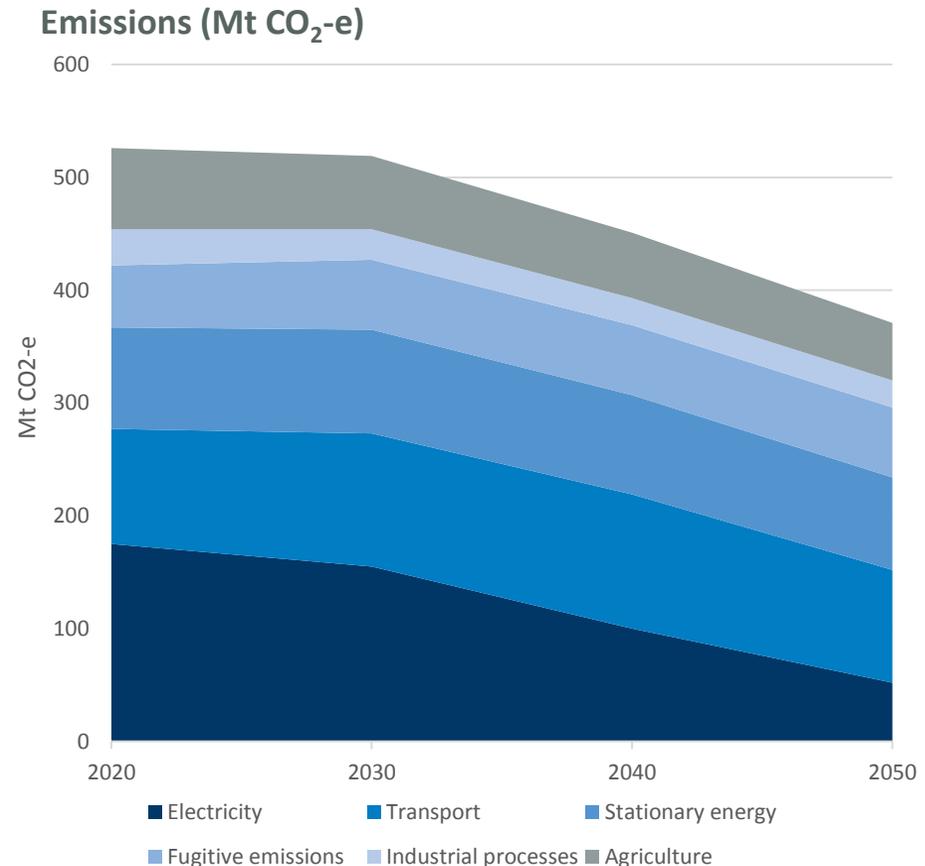
# Global Momentum Building for Climate Action...

## Toward Net Zero By 2050

### Act local, but think global...

- ❖ Expect a significant global push for commitment to zero emissions by 2050
- ❖ Multiple states and corporates have committed to 'net zero' targets (in many cases despite national opposition)
- ❖ We are beginning to see policies that will change the infrastructure investment landscape
- ❖ The challenge is significant. Infrastructure should be the easy part – the technology is largely there, its just a case of investment and build time!

### Australia's Emissions Forecast (BAU scenario)



# Green New Deals: Blueprint for Future Infrastructure Investment Programmes

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## Brief History

Phrase first used in 2007 by Thomas Friedman writing for NYT

Picked up by Green political parties around the world

- ❖ United Nations published Global Green New Deal in 2008
- ❖ Green New Deal resolution introduced to US Congress by Markey/AO-C in 2019 (see right)
- ❖ Major feature in UK Labour manifesto for 2019 election
- ❖ Resurrected by the Greens in Australia in 2020

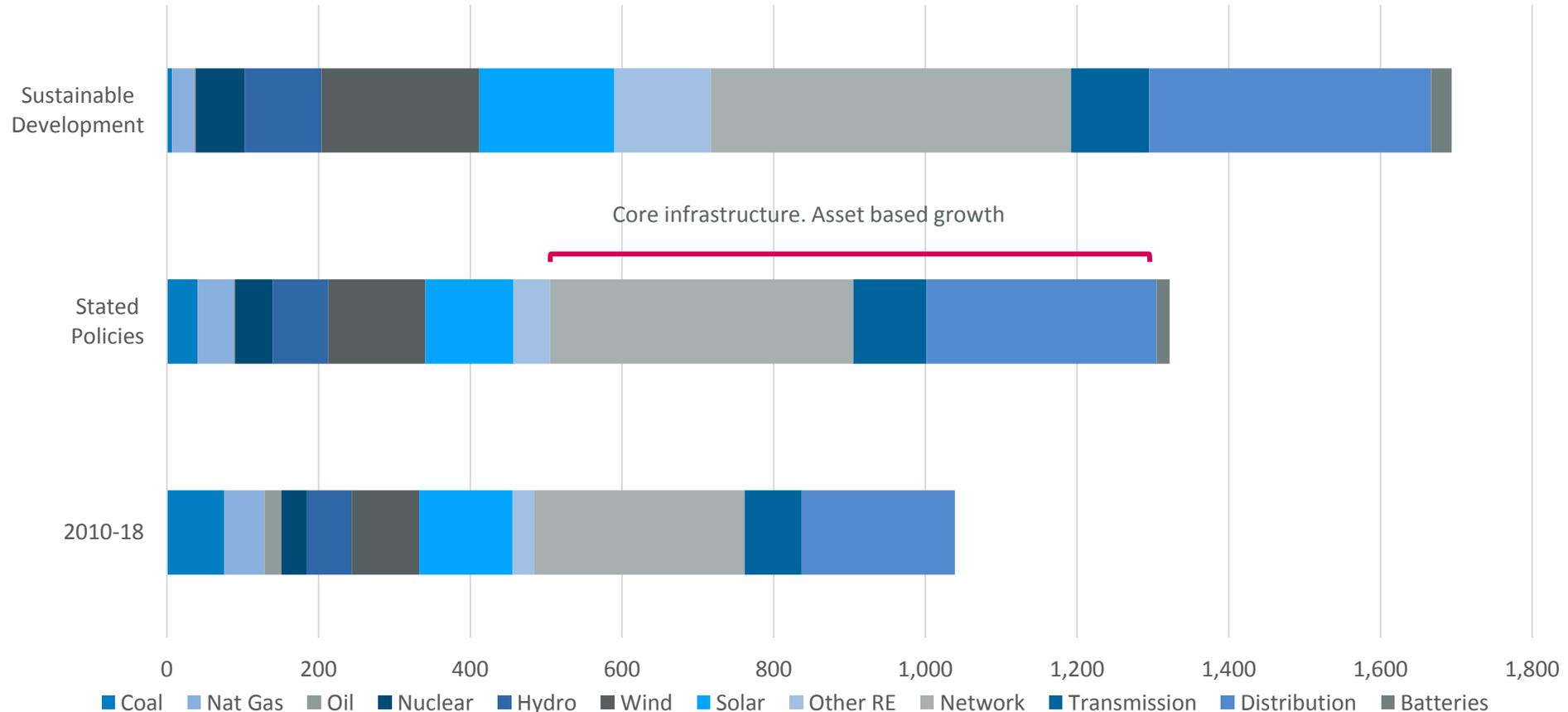
## Components of US Green New Deal (2019)

- ❖ Universal basic wage – guaranteed jobs
- ❖ Providing everyone with – health; housing; education, economic security; and clean water, nature, air and food
- ❖ Repair & upgrade infrastructure, including reducing pollution & GHG emissions, build affordable smart grids
- ❖ Upgrade all buildings to maximum efficiency
- ❖ Overall transport – zero emission vehicles, public transport, high speed rail
- ❖ Massive growth in clean manufacturing
- ❖ Eliminate pollution from agriculture

# How Big Could This Be?

## Trillions of Infrastructure Investment (Per Annum!)

Global Annual Average Power Sector Investment (USDb, constant 2018 dollars)



# Investor Alert - Generally Climate Change Beneficial for Infrastructure

## ...But Watch Asset Level Risks

### Stranded asset risk

- ❖ Generally climate change will change the way we use infrastructure, not the infrastructure itself...
  - ❖ AEVs have been forecast to result in an 8-fold increase in light-vehicle capacity on Toll Roads
  - ❖ However, generation and the pipeline sector may be challenged as energy sources and grids evolve

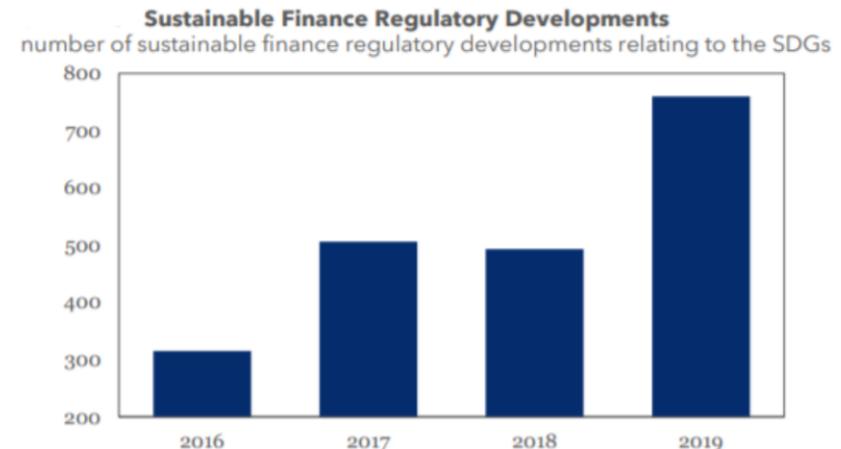
### Greenfield risk

- ❖ Building of infrastructure may carry significant risk. Investors should demand a higher cost of capital or return
- ❖ Riskiest time in greenfield infrastructure development is when the asset is first opened for use – the ramp up...
- ❖ Asset risk reduces as maturity is reached – lower operational and financing risk

### Climate change – capex, but also attitudes

- ❖ Asset based growth - adaptation of networks, mitigation of climate risk
- ❖ Evolving attitudes (and potentially regulation) for example **Flight shaming... Commuter rail... Reshoring supply chains**
- ❖ Lower carbon emissions given reduced transport distances, but may require a **re-alignment of infrastructure**

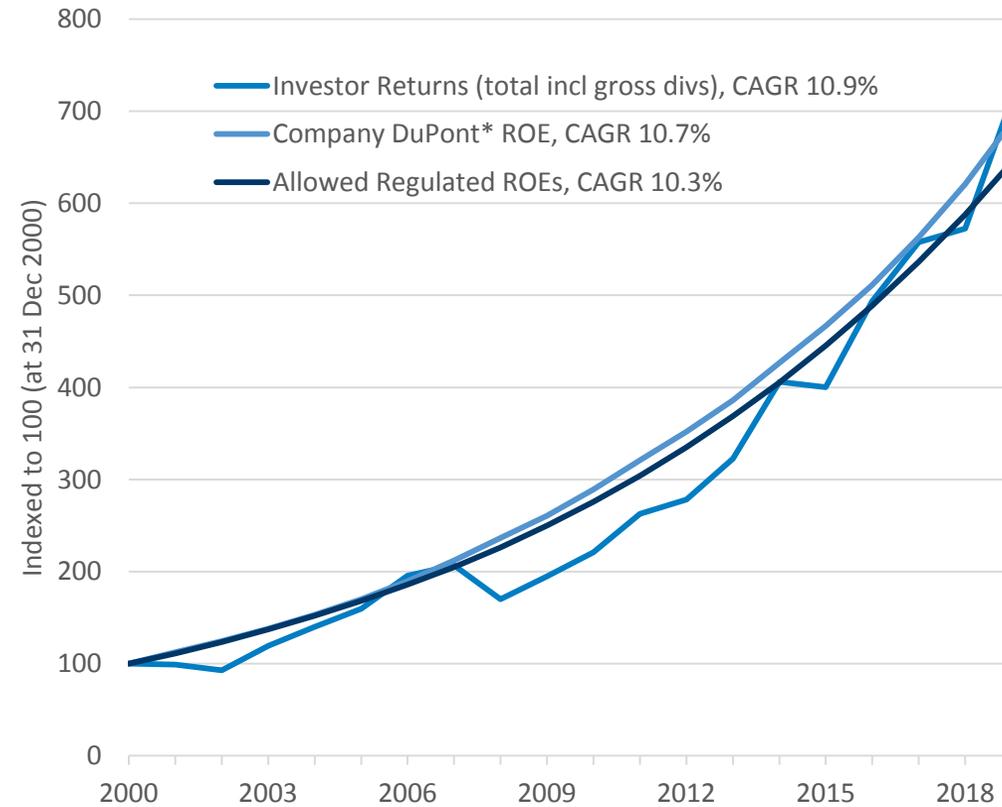
### Public policy risk



# Investor Alert: Psychology Leads Us to Underestimate Investment ...But Watch Returns Also

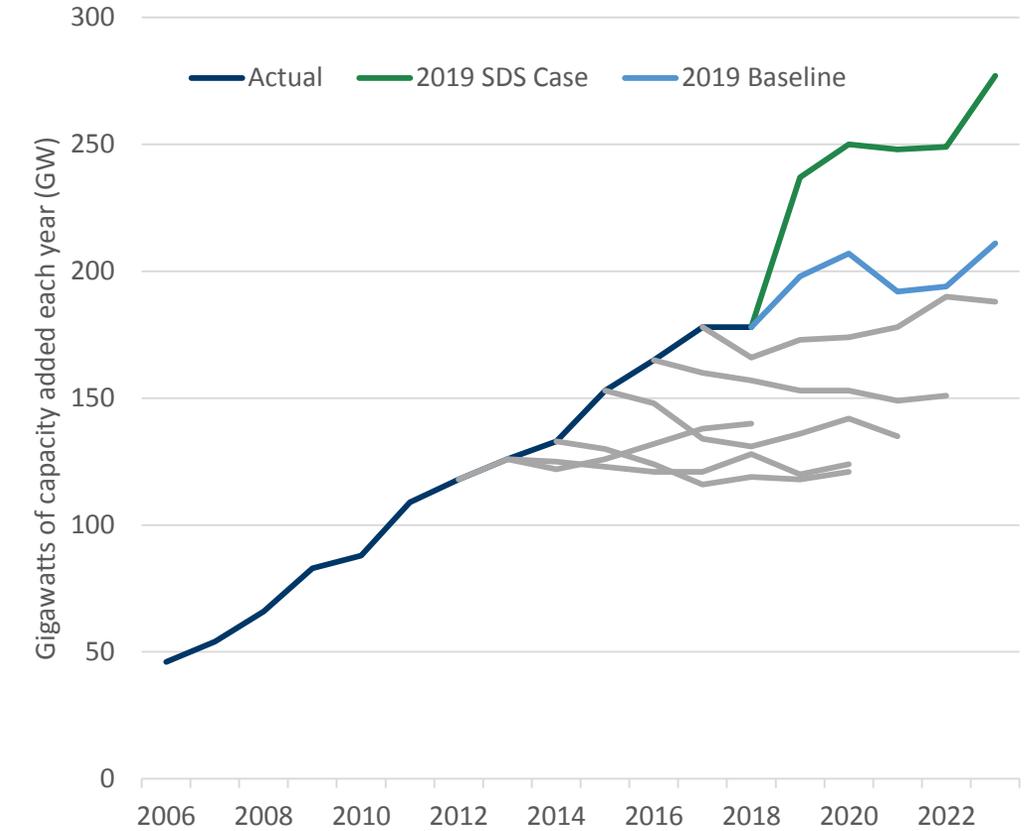
## North American Electric Utilities

Allowed ROEs vs Reported ROEs vs Investor Returns



## Renewable Capacity Actual Growth vs Forecast

2019 Forecasts vs Prior Years



# RARE's Integrated Approach to Sustainable Investing

## Three-Pillar Sustainability Framework

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### Valuation

- ⑩ Fundamental cash flow impacts are modelled – positive and negative
- ⑩ Comparison of global regulatory approaches
- ⑩ Industry wide themes are applied consistently across companies (overseen by sustainability committee)

### Risk Pricing

- ⑩ Sustainability issue exposures and management/mitigation actions are assessed
- ⑩ Scoring reflects actions over five year investment horizon
- ⑩ Relative scoring across sub-industries
- ⑩ A lower hurdle rate is applied to top sustainability performers and vice versa

### Engagement

- ⑩ Ongoing engagement with boards & management
- ⑩ Controversy monitoring
- ⑩ Voting at company meetings
- ⑩ Interaction with regulators, policy makers and other stakeholders
- ⑩ Engagement with third-party ESG experts

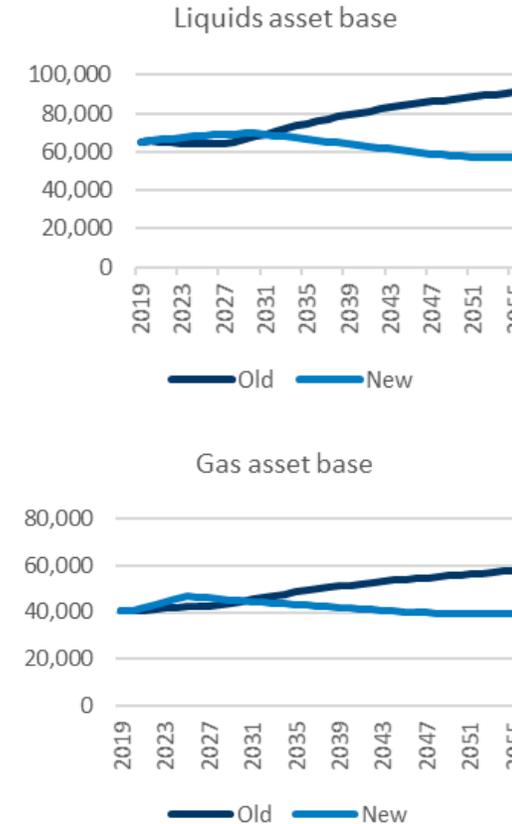
# RARE's Incorporation of Sustainability

## Example – North American Pipelines

### Key Research Findings / Changes

- ❖ Forecasts to 2040
  - ❖ Winners: Renewables, 7-9% p.a. CAGR
  - ❖ Neutral: Gas, 1-2% p.a. CAGR
  - ❖ Losers: Coal -5.0% p.a. CAGR
  - ❖ Losers: Oil -0.7% p.a. CAGR
- ❖ Assumptions adjusted –
  - ❖ Reduced our growth capex assumptions and longer-term returns lowered (*case by case basis*)
  - ❖ Terminal value approach – Gordon growth to 1.0x EV/Book for pipelines and infrastructure, ultimately results in declining asset base long term

### Enbridge Asset Base Growth (CADm)



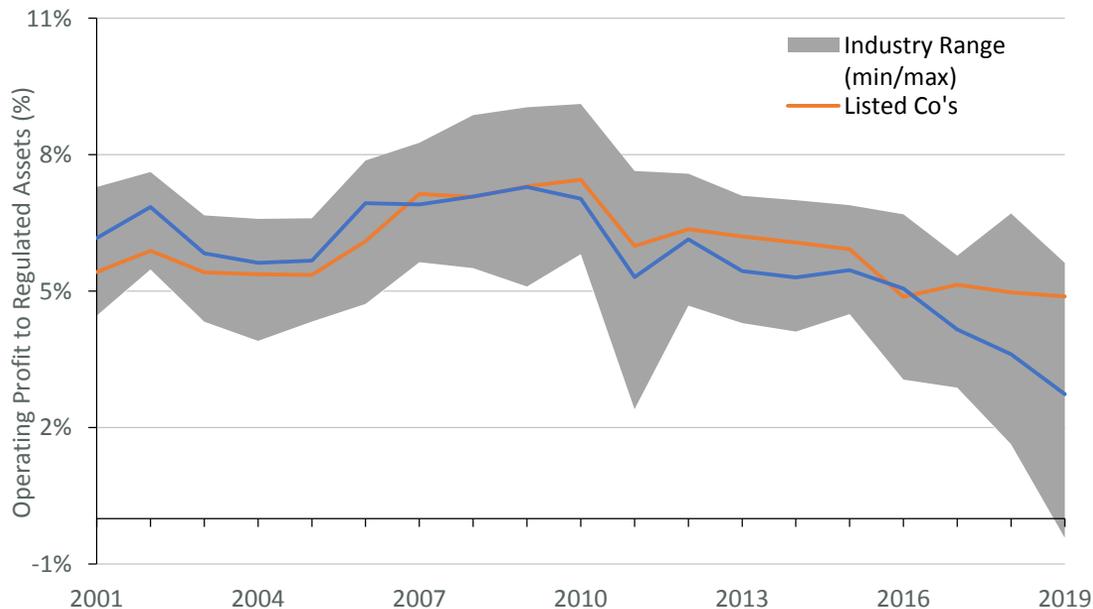
# RARE's Incorporation of Sustainability

## Example – UK Water

### Sustainability is driving the asset base and returns

**Increased cash flows** given sustainable asset base growth and operational incentives and...

**Lower discount rates** given better than average ESG ratings and quality of management teams.



### UK Water, customer experience ratings<sup>1</sup>

#### WATER

90%

Satisfied with what is provided by companies

#### SEWERAGE

85%

Satisfied with what is provided by companies

#### ENERGY

87%

Satisfied with what is provided by companies

72%

Satisfied it is value for money

75%

Satisfied it is value for money

71%

Satisfied it is value for money

*CCWater Water Matters Annual Tracking Survey (5,158 total customers surveyed)  
Source: CWater, England and Wales, Apr 2018 - Mar 2019*

Frontier Economics Nov 17 report to assess productivity changes in the sector:

“Customers are now 5X less likely to experience unplanned supply interruptions and companies have reduced leakage by 1/3...”

“The water companies are now 64% more productive than they were under nationalisation.”

# Where Does That Leave Us?



# Conclusions

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## Shorter Term

- ❖ COVID-19 response by corporates, governments and central banks is changing the game for investors
  - ❖ stakeholders over shareholders (therefore invest where stakeholder/shareholder balance been struck),
  - ❖ private sector investment will be front/centre,
  - ❖ as costs of capital (and therefore returns) decline further, invest in growth (increasing asset base...)

## Longer Term

- ❖ Climate change action – it's not just voters but also customers – will drive a target of net zero by 2050
  - ❖ Massive infrastructure investment required at a time that governments can ill-afford the spending – creates opportunities for the private sector, regulatory safe guards and investment models already tested
- ❖ Liquidity to be more valuable in managing risks for investors – stranded assets, policy risk – and enhancing returns from core infrastructure

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