2023 OUTLOOK

GLOBAL LISTED INFRASTRUCTURE

December 2022

DUFF & PHELPS
INVESTMENT MANAGEMENT CO.

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2022 Reflections

Investors will not be anxious to repeat the experience of 2022. Global equity and fixed income markets struggled, weighed down by high inflation, rising interest rates, a war in Ukraine, a developing energy crisis, and the overhang of China's zero-Covid policy. Despite this laundry list of challenges, global listed infrastructure provided some relief as it outperformed the broader global equity and fixed income markets. Outperformance was driven by attractive relative valuations for infrastructure assets as well as durable business models designed to withstand challenging economic conditions.

The energy infrastructure sector led performance with improving company fundamentals supported by solid commodity prices and robust volume growth. The sector experienced substantial increases in cash flow while management teams maintained capital discipline, which led to stronger balance sheets and a return of cash to shareholders. Utilities and transportation stocks performed in line with the infrastructure benchmark and substantially better than the broader market. Utilities provided another year of steady growth as they continued to benefit from strong capital programs and efficient operating-expense management. Transportation stocks were bolstered by encouraging volume growth across the sector. The communications sector was the worst performer, as higher interest rates took a toll on the tower stocks.

Looking Forward

The year ahead will present challenges as industries adjust to higher interest rates and commodity prices as well as continued political uncertainties. We are optimistic that listed infrastructure companies will display the resiliency of their business models as they weather these headwinds. We believe that secular trends support continued progress within each sector. Asset renewal, energy security, decarbonization, and data growth are driving durable, long-term investment cycles that will continue for years to come despite negative short-term economic developments.

As we look forward to 2023, we see the following trends in each of the infrastructure sectors:

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COMMUNICATIONS

Wireless tower activity in the U.S. remained robust in 2022 as the big three carriers built out their networks and deployed new spectrum to accommodate the increased demand for data and video. We expect this to continue in 2023 and beyond as carriers shift from the initial stages of 5G buildout and blanket coverage to focus on more targeted network densification.

In Europe, M&A was robust in 2022 with private-equity firms dominating the deal activity due to their willingness to pay higher multiples than the public companies. A solid level of organic growth underpins these transactions as wireless data demand continues to be robust. We expect healthy organic activity to continue into 2023 as the tower companies benefit from 5G expansion as well as inflation-linked escalators embedded in their contracts.

We believe the 5G buildout and predictable cash flows provided by long-term contracts will make the tower companies more resilient to the macro-economic challenges that may be ahead in 2023.

UTILITIES

Utilities benefit from long-term capital plans that increase their regulated assets while also improving reliability and safety. In addition, decarbonization of the economy creates a win-win for utilities as they improve their environmental profile while also increasing earnings. The transition to renewable energy and renewal of assets provide positive tailwinds that should last for more than a decade. Higher interest rates and commodity prices provide near-term challenges that must be overcome, but we believe these obstacles are a speed bump rather than a dead end. In fact, the Inflation Reduction Act of 2022 provides strong financial support for the energy transition in the United States and should help offset short-term headwinds.

For European utilities, the war in Ukraine and the loss of Russian natural gas remain the greatest hurdles. Higher natural gas prices have led to consumer affordability issues and potential political intervention. To date, European governments have managed affordability with power price “caps” and windfall taxes on energy companies. While we find valuations of European utilities attractive, our enthusiasm is tempered by potential fallout from even higher energy prices if weather conditions are extreme over the coming months. Ultimately, we believe that Europe will secure adequate energy resources for 2023 and an acceleration of renewable energy deployment will be part of the solution.

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TRANSPORTATION

Toll road volumes have shown resiliency with many roads already exceeding pre-pandemic traffic levels. Investor concerns over Covid-19 variants have significantly waned in the countries where we invest. Toll roads are stable businesses with inflation-linked tolling regimes and efficient cost structures. Therefore, we foresee another steady year of operations ahead.

North American railroads are beginning to emerge from the service issues induced by the global supply chain disruption. Railroads provide critical, reliable transportation for manufacturers, retailers, and other rail customers. The essential nature of rail service translates into strong pricing power. In 2023, we expect strong pricing gains, which can act as a powerful hedge to inflation headwinds.

Furthermore, rising global political tensions have disrupted the supply of essential commodities. We see railroads' best-in-class network as part of the solution, shipping commodities to meet elevated demand.

Airport traffic saw a sharp recovery in 2022. Pent-up demand for leisure travel has fueled "revenge travel" and businesses are eager to reconnect with customers in person, but we see signs of a potential slowdown in 2023. Higher prices for jet fuel and airline tickets may weigh on leisure travel, while business travel is likely to face continued competition from video conferencing and corporate ESG objectives. Airport stocks are likely to remain volatile until there is more certainty around travel trends.

MIDSTREAM ENERGY

Midstream energy was the best-performing infrastructure sector in 2022 and we remain constructive on the outlook for 2023. Although crude oil, natural gas, and NGL prices are off their peaks set earlier this year, commodity prices remain at levels that encourage producers to increase volumes. The disruption of Russian oil and gas supplies due to the war and resulting embargoes provides support for U.S. supply growth.

A loosening of China's zero-Covid policy and a replenishment of the U.S. Strategic Petroleum Reserve present demand-side variables that are likely to keep the market tight in 2023. Supply-side constraints should continue to drive the fundamental story, and while we may see some modest pullback on energy demand, we do not see this as an impediment to the strong financial setup for midstream.

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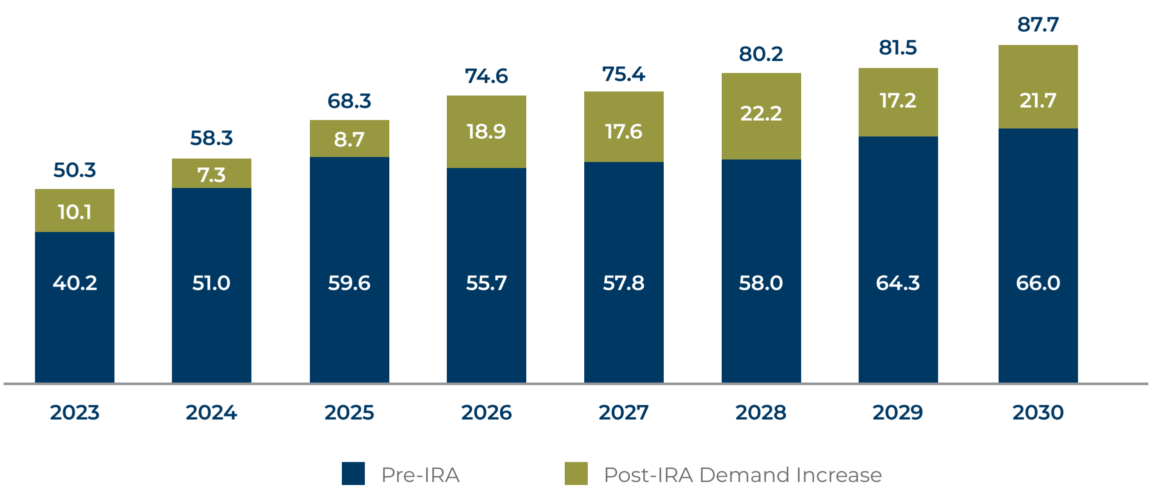
The midstream sector continues to be well-positioned to weather high inflation and commodity price volatility. Midstream balance sheets are significantly stronger and dividend payouts are at sustainable levels. Most companies are at or near targeted leverage metrics and have pivoted to shareholder-friendly capital allocation policies. The sector is more insulated than it has been in prior downturns, which gives us a higher degree of comfort amid an uncertain macro backdrop.

Inflation Reduction Act (IRA) is a Significant Accelerant to Growth of US Renewables Market

Projected Capacity Additions in GW



IRA Demand Outlook

	2023	2024	2025	2026	2027	2028	2029	2030	Total
Pre-IRA Demand (GW)	40.2	51.0	59.6	55.7	57.8	58.0	64.3	66.0	452.6
Post-IRA Demand (GW)	50.3	58.3	68.3	74.6	75.4	80.2	81.5	87.7	576.3
% Increase	25%	14%	15%	34%	30%	38%	27%	33%	27%

Source: Bloomberg NEF.

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