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Infrastructure as Alternative Investment

Listed investments have been tracking oil prices lately, even businesses that have nothing to do with oil prices. Have a look at US alternative energy stocks, shares in companies that compete with coal and gas, not oil. That is because the listed markets often move together, whether that makes sense or not. Many investors look to alternative investments that are less correlated to balance their portfolios, and infrastructure, energy and non-energy alike, has gotten a lot of attention recently as a seemingly uncorrelated alternative.

There are many ways to invest in infrastructure. Infrastructure investment at its best can achieve inflation protection in substantially uncorrelated, long dated real assets. Infrastructure investment can also provide country and currency diversification when crossing borders, and there are even disruptive technology investment opportunities in the infrastructure delivery industry. Over the next few weeks, I will be writing about several ways to invest in infrastructure to meet these diverse investment objectives. First up today, investment to achieve exposure to what has become known as "infrastructure risk."

When I teach my class in infrastructure investment at Columbia University, I spend some time on the first day distinguishing between infrastructure assets and infrastructure risk. Infrastructure assets are generally the things that constitute basic services such as energy, water and transportation. There are many others but these are the big three. It's hard to have much of anything without those basics available. Investors like the essentiality of these assets.

Infrastructure risk, however, is defined by a different set of characteristics: long term, real asset based, steady uncorrelated revenue generation, high barriers to competition (often monopolistic or quasi monopolistic enterprises), and frequently government counterparties or government sponsored businesses. While infrastructure assets are good candidates for infrastructure risk, these are not at all the same thing.

Energy is an easy place to show the difference. Compare two identical power plants, both infrastructure assets. One is associated with a long term PPA—power purchase agreement—with a government sponsored power utility and the other is a "merchant" plant, meaning that it functions in the free market for electricity, selling for what it can, when it can. The first is most definitely a candidate for an infrastructure risk investment while the later is almost certainly not. You can play this game with any physical asset within the infrastructure class.

Not all infrastructure is alike and not all infrastructure provides a basis for an infrastructure risk investment. Some are downright venture-like investments, but with heavy up-front capital outlays, and some come close to direct government credit, just with a bit of complexity to understand how they work.

In the next post, I will examine the use of infrastructure investment in a portfolio to achieve global and currency diversification and then, finally, in the last of this series, a look at disruptive technology in infrastructure delivery.