BARRON'S
THE DOW JONES BUSINESS AND FINANCIAL WEEKLY www.barrons.com FEBRUARY 14, 2017

Q&A

5 Infrastructure Plays for the Trump Era

Morgan Stanley Global Infrastructure favors renewable power, toll roads, pipelines, and cellphone towers.

By TERESA RIVAS

Infrastructure has become a fashionable topic in recent months, thanks to the election. Matt King thinks there are plenty of reasons besides a new president to be excited about it.

King, the co-manager of the Morgan Stanley Global Infrastructure fund (ticker: MTIPX) with Ted Bigman, began investing in infrastructure long before it was trendy. The pair thinks that while proposals from Washington could have a positive effect on some sectors, they're more interested in infrastructure's long-term appeal.

Infrastructure stocks tend to have higher annualized returns with lower volatility than global equity markets, they generally sport higher dividends than their peers, and they offer growth—and, in many cases, inflation protection—despite their defensive nature.

The duo's approach has certainly paid off. The fund, which gets a four-star rating from Morningstar and charges annual fees of 1.12%, has beaten both Morningstar's benchmark MSCI ACWI index and the fund's infrastructure peers over the past one, three, and five years, returning about 9% annualized over the five-year period, in which it's ranked ninth in its category.

The managers are optimistic that the infrastructure space—mainly utilities, transportation, energy, and communications stocks—is on the same path that real estate was in the last decade, when it became accepted and increasingly popular among institutional and individual investors.

Manager's Bio

Name: Matt King
Age: 41
Title: Managing Director, Portfolio Manager for Global Listed Infrastructure
Education: B.A., Occidental College; M.B.A., Columbia Business School

Manager's Bio

Name: Ted Bigman
Age: 54
Title: Managing Director and Head of Global Listed Real Assets Investing
Education: B.A., Brandeis University; M.B.A., Harvard University

Read excerpts from the Barrons.com interview with King below.

***Barrons.com:* How do you see the outlook for infrastructure in the U.S. under President Donald Trump?**

Matt King: The $1 trillion proposal by the Trump administration currently lacks detail. We're still waiting to see how that $1 trillion filters down to the various parties and constituents and furthers development of infrastructure in the U.S. If you look at transportation infrastructure, roughly three-quarters of that is actually undertaken at the local municipality and state level, not the federal level. So for many projects, we need to see a mechanism by which the benefits designed at the federal level move down to the local municipal level and ultimately get funded.

Directionally, the rhetoric seems quite positive. Outside the direct spending, we think a lot of companies in our investible universe will likely benefit from more-favorable tax policy and/or tax subsidies. The most apparent area is energy infrastruc-

(over please)

Fund Facts
(as of Jan. 26, 2017)

Morgan Stanley Global Infrastructure (MTIPX)
Assets: $357.1 million
Expense Ratio: 1.12%
Front Load: None
Annual Portfolio Turnover: 48%

Source: Morningstar

ture. Under a Trump administration, a number of projects potentially could be approved more quickly going forward, which would be positive for the overall sector.

Are there any sectors that may see less benefit?

Immediately after the election, utilities in general suffered, in particular the renewable-power companies. As a value investor, that's an area of interest to us, given that we think those stocks have been misunderstood and have suffered from the initial reaction to a Trump victory.

We value all companies on an ex-growth [assuming the business is holding steady or falling] basis, and then we take into account the value of any potential growth. We think we can own a number of these companies in the renewable space on an ex-growth basis. They are attractively valued, even if tax incentives for the development of renewable power are rolled back from current levels. Furthermore, renewable-power mandates are done at the state level, not at the federal level, and many states have continued or accelerated their RPS mandates [government targets to meet a certain percentage of their overall power mix by renewable power sources by a particular date].

How do you see the outlook for infrastructure outside the U.S.?

Both for the U.S. and outside the U.S., fundamentals within the infrastructure universe, generally speaking, are stable to improving, despite the very uncertain macro environment. What's less certain is how the market reacts to certain political and macro events in the various regions.

Europe is a good example: If you look at toll-road or airport-transportation assets, fundamentals are growing, traffic is growing low- to mid-single digits—which we think is quite healthy for that particular region. Yet the share prices have not performed as well relative to some other markets due to the concerns over potential political developments in that region and what that may mean for the broader euro zone. But these assets and the companies we invest in are regulated or controlled through contracts. Even if the macro deteriorates, usually there are mechanisms by which cash flows remain quite stable. So we're looking at Europe quite closely, given the number of political elections and political events, not only Brexit, but also the number of elections in Continental Europe in 2017.

Let's talk about some of your holdings from each of your infrastructure categories.

In utilities, two of the renewable-power companies that we like are Saeta Yield (SAY.Spain) and Atlantica Yield (ABY). Both are owners and operators of developed or currently operating renewable-power assets, both wind and solar, in various regions. Saeta is more of a pure-play Spanish operator; Atlantica is a more-diversified operator across regions.

We like these particular companies because we can actually acquire them at a discount to what the private market is paying for these assets. Both, in our view, are trading at a good discount to intrinsic value, even though we're assuming no growth. We think this is the infancy of a larger industry that will end up growing. The prospects are good, but the market hasn't done a lot of work. We think generally these assets are somewhat difficult to value, and it is an area that offers us a quite attractive prospective return consistent with what infrastructure assets should achieve without growth.

In energy, the obvious example is the Canadian pipeline operator Enbridge (ENB.Canada), the primary transporter of crude oil from Canada to the U.S. We like to find attractive investments where we think our thesis will play out, but we don't have to make a specific bet on the commodity price itself. And given the unique dynamics of Canadian crude oil and the lack of available outlets for transporting it in a pipeline to the U.S., the volumes on the Enbridge system have been very stable despite the significant variability in the crude oil price over the last year and a half. So it's not making a bet on the commodity price but a bet on volume, and in this instance it's quite healthy. It also has a significant barrier to entry as there are not many pipelines that cross the Canadian border to the U.S.

With transportation, clearly traffic on a toll road or containers moving through a port are a function of economic growth. What we like to do is find stories where effectively the transportation network is congested and companies create value by expanding that network. Hopewell Highway Infrastructure (0737.HongKong) owns stakes in two assets. They're the primary trunk roads in Guangdong Province moving on both sides of the Pearl River Delta, so between Guangzhou and Shenzhen and on the western side as well. Its primary asset, the Guangzhou-Shenzhen Superhighway, is a highly congested road. So we're not making a macro bet on Chinese growth accelerating, we're investing in some assets that are in a more-affluent area of China, have good, steady, stable traffic growth, and are attractively valued.

In communications, we own American Tower (AMT), a real estate investment trust. The wireless-tower business is a play on the proliferation of data-driven devices and their usage. You can triangulate to a level of organic growth without having to say, well, the economy is running at 1% or 3%. It doesn't really matter when you are looking at the organic growth prospects for a company like American Tower. The wireless-tower business has very stable cash flows. Effectively the wireless carriers pay the tower companies rent, which escalates every year, and they're under contract. It's an inflation-protected asset where cash flows grow at a minimum by inflation every year, and you get operating leverage as you add tenants or additional wireless carriers on the tower. And once you build the tower, your cash flow grows with very little capital expenditure. American Tower is one of the big three U.S. operators and the one that we like the most.

Thanks.

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The holdings discussed are not all of the Portfolio's holdings and not all holdings performed in a similar manner as the holdings discussed.

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Past performance is not indicative of future results.

MSIF Global Infrastructure Portfolio Top Ten Holdings

SECURITY NAME	% OF PORTFOLIO
ENBRIDGE ENERGY MANAGEMENT LLC:USD COM	7.55
JOHN LAING GROUP PLC	4.42
KINDER MORGAN INC	4.35
ATLANTICA YIELD PLC	4.24
PATTERN ENERGY GROUP INC	4.07
SAETA YIELD SA	4.01
PG & E CORP USD COM	3.89
TRANSCANADA CORP CAD COM	3.79
ENBRIDGE INC	3.51
HOPEWELL HIGHWAY INFRASTRUCTURE	3.49

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1714937 3/7/2018