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The potential return and yield opportunity of infrastructure

At Russell Investments, we have been laser-focused this year on helping advisors prepare clients for what we expect will be a lower return environment going forward. We believe this challenging market environment calls for investors to seek incremental returns where-ever they can, while at the same time ensuring they don't take on uncompensated risks and are still able to implement their portfolio efficiently.

In this vein of low yields and returns, we believe that infrastructure investing may offer an attractive source of incremental returns for investors with commensurate risk tolerance.

We've written before about the benefits of including infrastructure in a portfolio: diversification, defensiveness, and attractive yield and total return. In this blog post, I'd like to spend a little more time on the **attractive yield and total return** aspects of infrastructure.

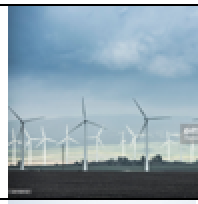
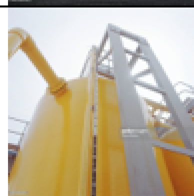
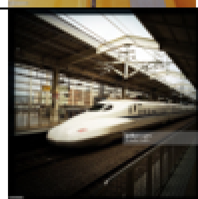
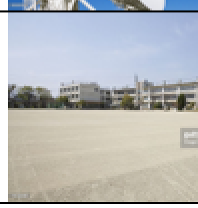
But first, a quick review of listed infrastructure investing—particularly the "pure play" infrastructure.

"Pure play" infrastructure

According to CBRE Clarion, the infrastructure investment universe is quite broad, encompassing approximately 500 stocks and $3.5 trillion in assets in sectors such as energy, water, transport, communication and social infrastructure as of June 2017. At Russell Investments, we prefer to focus on a subset of those stocks: "pure play" infrastructure companies.

These companies **own and operate infrastructure assets** that provide essential services, for example airports, toll-roads, sea-ports, electricity transmission & distribution assets and hospitals. In Russell Investments' estimation in June 2017, there were about 200 companies globally that fit this description, and they represented around $1 trillion in AUM.

Infrastructure assets in their purest form

ENERGY		Power generation, transmission, distribution, renewables
WATER		Water and wastewater networks, desalination plants
TRANSPORT		Ports, rail, airports, roads, bridges, parking
COMMUNICATION		Cable networks, telecom lines, towers, satellites
SOCIAL		Hospitals, prisons, schools, courts, public housing

What attracts us to this subset of opportunities from an investment standpoint? They typically:

- Operate in **monopoly-like** competitive positions—making them relatively immune from competitive market pressures and commodities price volatility;
- Enjoy **sustainable cash flows**—which help produce reliable income streams.

Those are precisely the characteristics that may make infrastructure investing attractive for many investors seeking yield and total return.

Seeking yield? Consider infrastructure investments

Many investors don't naturally think of infrastructure investments when they think about building an income stream. However, investments in infrastructure companies have historically provided a relatively:

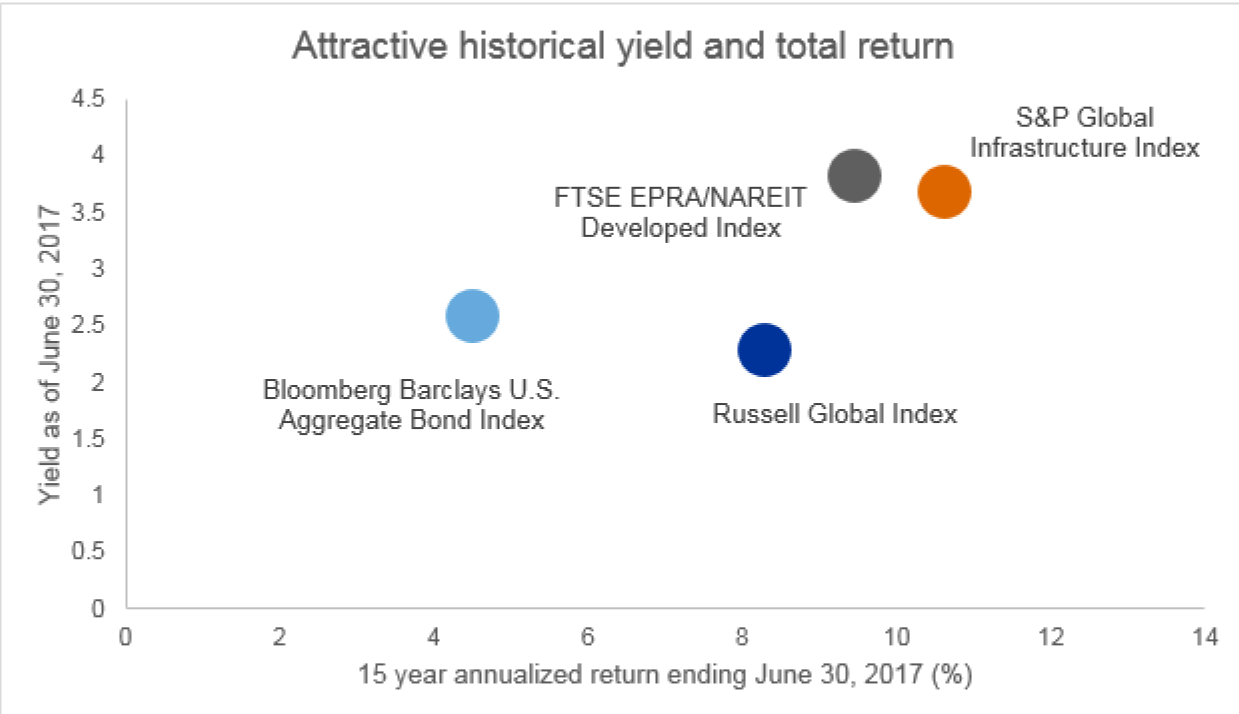
- **high dividend yield** (dividend yield of the S&P Global Infrastructure has ranged between 3.6% and 4.0% over the last two years ending 6/30/17)
- **predictable cashflow** because they're based on demand for essential services, which is relatively immune to the vagaries of the economic cycle, and infrastructure companies operate under long-term concessions they have negotiated with governments
- **potential buffer against inflation** because many infrastructure cashflows are fee- or toll-based, allowing companies to raise prices based on a price index.

Seeking total return? Considering infrastructure investments

Historically, infrastructure has also had attractive long-term returns. Remember, the services provided by infrastructure companies are essential for the functioning of a society. While governments may not allow companies to charge exorbitant prices for those services, they do need to allow companies to earn fair returns in order to incentivize them to keep their services (and physical structures) in good working order and invest for future growth and modernization.

A combination of attractive historical yield and total return

You can see in the chart below that global infrastructure has provided both an attractive yield and total return over the past 15 years ending June 30, 2017 relative to global equities, global real estate, and fixed income assets. With yields of other asset classes at low levels today, stable yields from infrastructure can be beneficial to a diversified portfolio seeking income, in additional to providing equity-like returns.



Data reflects the period from the inception of the S&P Global Infrastructure Index (12/31/2001) thru 6/30/2017. Indexes are unmanaged and cannot be invested in directly. Past performance is not indicative of future results.

Don't neglect the potential risks, though

Infrastructure investing is not without risks, however. The general risks surrounding investing globally and in emerging markets apply (e.g., currency fluctuations, foreign country economic and political risks), and diversification within infrastructure is important, as different economic and market cycles will impact various types of infrastructure differently.

Bottom line

In addition to providing diversification and defensiveness, including pure-play infrastructure assets in a portfolio may provide a more consistent level of income, as well as the potential for increased return.

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grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

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S&P Global Infrastructure Index: Provides liquid and tradable exposure to 75 companies from around the world that represent the listed infrastructure universe. To create diversified exposure across the global listed infrastructure market, the index has balanced weights across three distinct infrastructure clusters: Utilities, Transportation, and Energy.

Russell Global Index: measures the performance of the global equity market based on all investable equity securities. All securities in the Russell Global Index are classified according to size, region, country, and sector, as a result the Index can be segmented into thousands of distinct benchmarks.

Bloomberg Barclays U.S. Aggregate Bond Index: An index, with income reinvested, generally representative of intermediate-term government bonds, investment grade corporate debt securities, and mortgage-backed securities. (specifically: Barclays Government/Corporate Bond Index, the Asset-Backed Securities Index, and the Mortgage-Backed Securities Index).

FTSE EPRA/NAREIT Developed Index: A global market capitalization weighted index composed of listed real estate securities in the North American, European and Asian real estate markets.

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