Hamilton Lane

For Whom the Road Tolls: Part III

A Potential Solution: Biden's Ambitious & Encompassing Infrastructure Plan

August 11, 2021 | Brent Burnett, Co-Head of Real Assets

This month, a bipartisan group of Senators passed a bipartisan plan that jumpstarts federal involvement in U.S. infrastructure spending.

This plan contemplates $1 trillion of infrastructure investment, including $550 billion of new federal government spending across transportation, transit, ports, airports, water systems and broadband. Proponents of the plan believe that it will help to reposition the U.S. as a green energy leader, while keeping the country at the forefront of economic competitiveness. Opponents argue that it will simply crowd out other forms of infrastructure investment, including from state and local governments as well as private investors.

What do we think? Well, we think this is a promising development to provide much-needed infrastructure investment. What's more, there are some elements of the tentative plan as we understand it that may address some of the shortcomings of prior infrastructure spending bills:

- Relative to previous plans, it's the most broad and comprehensive, encompassing transportation, clean drinking water, the energy grid and digital infrastructure.
- It is focused more on the long term than other plans have been – this is key when thinking about long-term projects and assets.
- It seeks to more comprehensively address issues of resiliency and environmental sustainability, which in other plans have been modest.
- It's focused on areas in which the federal government can be most impactful, including around permitting, tax policy, leveraging federal highway rights-of-way and breaking federal agencies out of silos to address infrastructure needs.

But before anyone becomes too optimistic, let us point out that there is still a major question – perhaps the most important element to any infrastructure plan – that is currently unanswered: How will it facilitate or align the federal government with asset-level decisions made at the state and local levels? Recall during the aftermath of the GFC that nearly $800 billion of federal stimulus was intended to be invested in "shovel-ready" infrastructure projects. Yet, in the years following the GFC, we saw federal government spending on infrastructure fall.

Although there appears to be support from both political parties to get an infrastructure bill done, the impact on asset-level decisions and the resulting opportunities for private capital remain to be seen.

If the plan is taken as drafted today, what do we think it means for private infrastructure investment opportunities? We are infrastructure investors. We would love to say that a federal spending bill focused on infrastructure will create massive opportunities for private capital. The reality is, we believe the sector and asset-level impacts would be mixed. Below is a snapshot of the targeted spending in the bipartisan deal and our view of the resulting opportunities for private infrastructure investors across relevant sectors:

TRANSPORTATION		
Types of Infrastructure Assets	**Targeted Spending**	**Impact on Private Investment Opportunities**
Highways, Roads, Road Safety, Bridges, Rail, Airports, Port and Waterways	$269 billion	Neutral to negative

Commentary

- Largest component of this is focused on roads and highways, which have been a very small target for private infrastructure investors in the U.S. Deals that have been done have benefitted from fulfilling capital needs not funded by government sources. Likely effect on roads and bridges is to crowd out private investments.
- Rail spending targeted at Amtrak and public transport, which have not been targeted sectors in the U.S. given public ownership and operations.
- Amount allocated to airports and port facilities is negligible.

Likely Beneficiaries

- Services – heavy civil construction, design and engineering firms
- Equipment – Think CAT, Komatsu and John Deere
- Aggregates – concrete, asphalt, sand and gravel assets
- Trucking – road investment may improve efficiency, but labor elements of the plan may work against trucking cost

WATER		
Types of Infrastructure Assets	**Targeted Spending**	**Impact on Private Investment Opportunities**
Utilities, Treatment, Sanitation, Efficiency	$55 billion	Neutral to negative

Commentary

- Again, this has been a small sector target in the U.S. The few projects that have been done have benefitted from having a lack of public capital available to fund projects. Public capital likely to crowd out private capital for opportunities. · Unclear how much of this will be direct spending vs. subsidies or tax credits.
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Likely Beneficiaries

- Water utilities will be the largest beneficiaries, followed by service and pipe manufacturers

DATA / TELECOM		
Types of Infrastructure Assets	**Targeted Spending**	**Impact on Private Investment Opportunities**
Fiber, Towers, Data Centers, Spectrum	$65 billion	Neutral to positive

Commentary

- Data/telecom has been a large target for private infra investors. While this plan does not favor particular technologies, the minimum upload/download speed requirements would encourage additional fiber spending.
- The plan also supports rural broadband buildout and may prioritize networks that are not owned or managed by profit seeking enterprises.
- The plan subsidizes broadband for low-income households which could spur additional demand.

Likely Beneficiaries

- Rural broadband providers
- Fiber line manufacturers

RESILIENCY AND WATER STORAGE		
Types of Infrastructure Assets	**Targeted Spending**	**Impact on Private Investment Opportunities**
Cybersecurity, Waste management, Flood mitigation, Wildfire, drought and coastal resiliency, Ecosystem restoration and weatherization	$50 billion	Likely positive

Commentary	Likely Beneficiaries
• This is a broad category of investment to improve resiliency across a range of sub-sectors and industries. • Investment could benefit operating infrastructure businesses by investing in their physical plant and secure them from both environmental and cyber threats.	• Waste management businesses • Environmental services providers • Digital infrastructure and software providers • Ecosystem restoration specialists

MISCELLANEOUS		
Types of Infrastructure Assets	**Targeted Spending**	**Impact on Private Investment Opportunities**
Clean up of R&D abandoned wells, mines and Superfund sites, Semiconductors	$21 billion	Neutral

Commentary	Likely Beneficiaries
• Not a target for private infrastructure investment	• TBD

Our prediction is that the largest opportunities for private infrastructure investors could come from increased federal spending on broadband and energy transition.

- **Broadband**, globally, is now viewed as a critical service that serves to enhance the economic and productive capacities of the communities where it is available. This plan includes formula-based grants to states to enhance broadband rollout, including $2 billion directed to rural areas. The form of spending this takes will matter for private investors, but we believe the most likely scenario is that the federal government subsidizes the provision of rural broadband, which will allow existing asset owners to more effectively scale their networks. Rural broadband spending is politically very popular, with support from both parties.
- **Electrification** is another key theme for the Biden plan that could create additional opportunities for private investors in what is already a hotly-targeted sector for private capital. EV charging stations and fleet retrofitting could benefit from more permanent federal tax policies and streamlined regulation.

- **Transportation** is targeted for the largest amount of federal spending in the plan. This sector has, historically, been a small target for private infrastructure investors in the U.S., as most of the transportation infrastructure is already funded by state, local or federal governments. Without a willingness to privatize some transportation networks and provide for large-scale tolling arrangements, we think the opportunity for private investors here will be small. Given the intersection (pun intended) of state and federal governments on transportation-related assets, we think increased federal spending here has the highest likelihood of crowding out private investors.

So, how do we think the Federal government can have the most meaningful impact?

- Streamlining permitting and environmental review processes;
- Providing federal regulatory certainty as it relates to energy policy; and
- Making permanent certain tax credits and subsidies related to renewable energy or EV adoption (these tax credits and subsidies are currently intermittent and have to be renewed by acts of Congress every few years).

Without a strong federal government role, U.S. infrastructure assets are unlikely to receive the capital investment necessary to remain competitive on a global scale or keep pace with the expanding U.S. population. While public policy and public spending will continue to shape the infrastructure landscape in the U.S., there is a role for private capital to help shore up the funding gap if public and private incentives can be properly aligned.

Without a more coordinated approach between various funding sources, we believe the U.S. will continue to see a significant funding gap in infrastructure, resulting in a slow but deliberate decline. This is something that both parties understand. As more developed peers continue to invest in connecting people, goods and services, the U.S. may start to hear the funeral bell ringing on its long-term economic competitiveness. As Hemingway said, “never send to know for whom the bell tolls; it tolls for thee.”

As of August 11, 2021