Macquarie Global Listed Infrastructure[1]

Energy infrastructure – Back to the future

Central to our investment philosophy is that Global Listed Infrastructure should be an access point for pure, essential service infrastructure.

With such an approach, investors can access the contractual cashflows that are key to the efficient functioning of many of the world's economies.

What is energy infrastructure?

Energy infrastructure assets include oil and gas transmission pipelines, storage terminals and liquified natural gas (LNG) export facilities that are essential for the delivery of energy to the world

At its heart is energy infrastructure. A robust and reliable energy infrastructure network is fundamental to modern society, it underpins economic stability and ultimately quality of life.

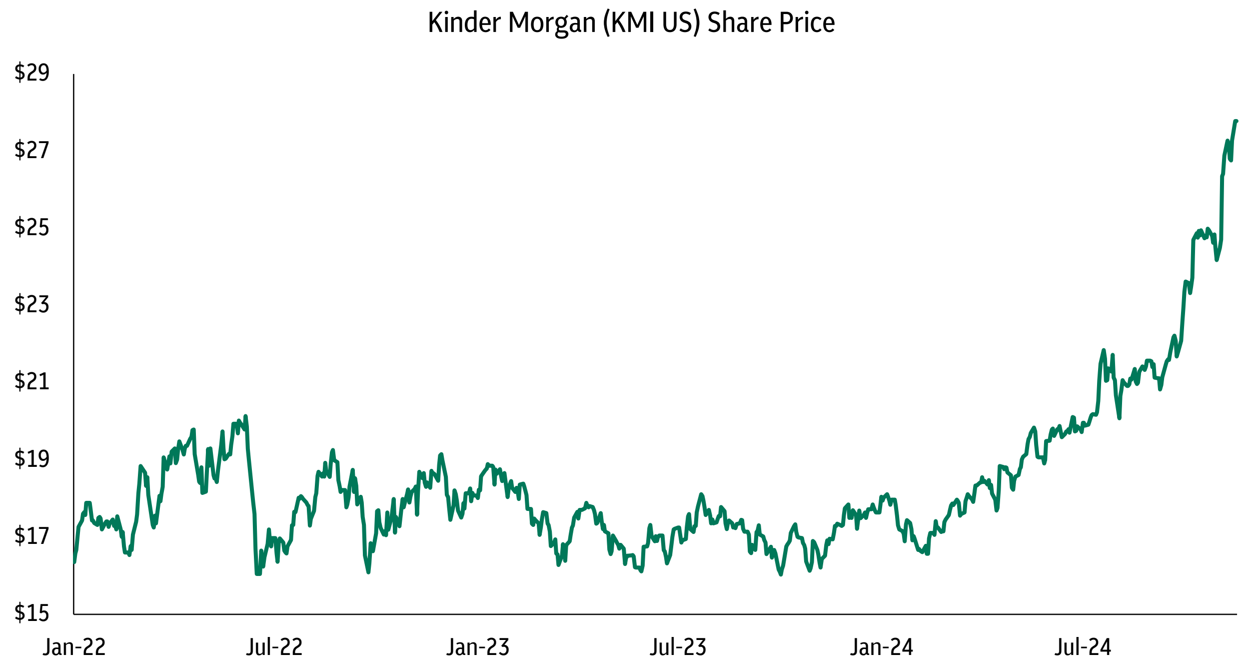
Prior to 2024, the listed energy infrastructure sector had been out of favour with some investors. The build-out of renewable energy, investment in energy transition and the electrification of transport increased concerns about the long-term demand outlook for oil and gas. The rise of sustainable investing resulted in an increasing number of investors avoiding the sector.

Importantly, despite being out of favour, the sector continued to deliver strong and contractual cashflows throughout.

Back to the future

In 2024, investors perspectives have, in our view, changed. There has been a resurgence in market interest in the energy infrastructure sector and pipeline stocks once shunned are now market darlings. One example is Kinder Morgan, one of the largest energy infrastructure[2] companies in the US, as shown in the graph below.

[1] Macquarie Global Listed Infrastructure is an equity team within Macquarie Asset Management's (MAM) Equity & Multi-Asset business. [2] Kinder Morgan.



Source: Macquarie, Kinder Morgan

Why?

There are, in our view, three key factors behind the market's new-found excitement for a sector that our team has always viewed as providing an essential service and should continue to do so for many years.

1. Data centres and Artificial Intelligence (AI)

One key driver of the recent positive market sentiment towards energy infrastructure relates to the hottest topic in markets this year, data centres and AI.

While the market initially focused on stocks such as Nvidia, it did not take long for many to join the dots and see that energy infrastructure is also exposed to the thematic given the expected surge in electricity demand from AI. To give you some sense of the scale of the potential demand, Chart 1 below shows that, on average, a ChatGPT query needs nearly 10 times more electricity to process compared with a Google search. In addition, the uptake by households of generative AI, such as Chat GPT, has been almost twice as that of the internet as shown in chart 2 below!

Chart 1: Electricity consumption per request (Wh)

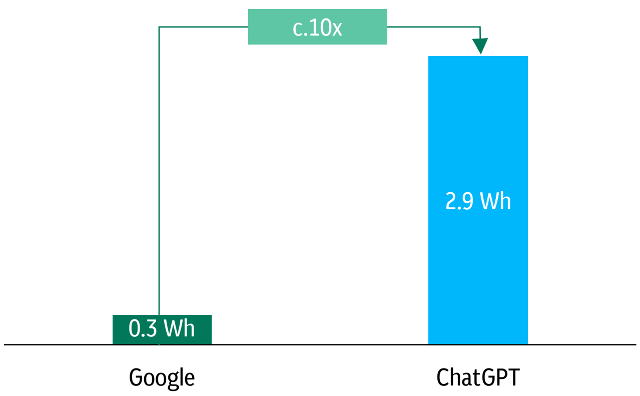
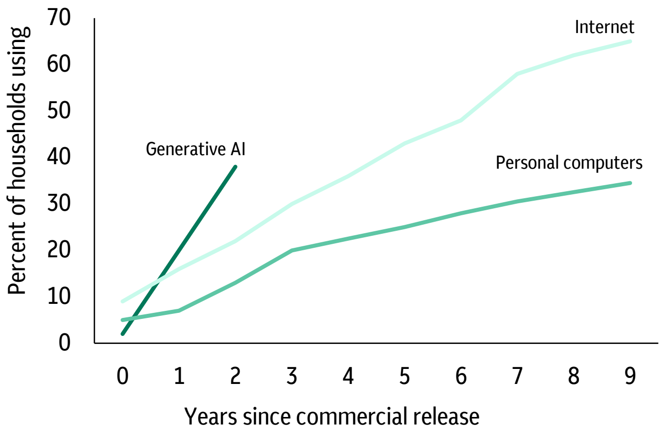


Chart 2: Household adoption rates of digital technologies



Source: Chart 1 IEA (April 2024), Chart 2 USA, IEA (2024)

With the growing realisation that renewables alone will not be enough, and that natural gas will be critical to meet surging baseload capacity demand, energy infrastructure stocks exposed to this thematic performed strongly.

Kinder Morgan is one example. It owns the largest natural gas network in the US, with ~67,000 miles of natural gas pipelines that move ~40% of the natural gas consumed in the US (source: Kinder Morgan). In addition to the tailwinds from LNG exports, electrification and coal-to-gas conversions, midstream companies such as Kinder Morgan are expected to benefit from power hungry data centres driving strong growth in the demand for natural gas.

2. President-elect Trump

The recent US election has further boosted market sentiment towards the energy infrastructure sector in that market. Expectations that President-elect Donald Trump will reduce regulatory requirements on domestic oil and gas production, as well as roll back various climate-related rules has lifted market expectations for domestic oil and gas investment and production levels.

A key challenge to building new energy infrastructure has been permitting and legal challenges to new projects on environmental grounds. There is increasing expectation that the new administration will introduce measures aimed at making this process easier.

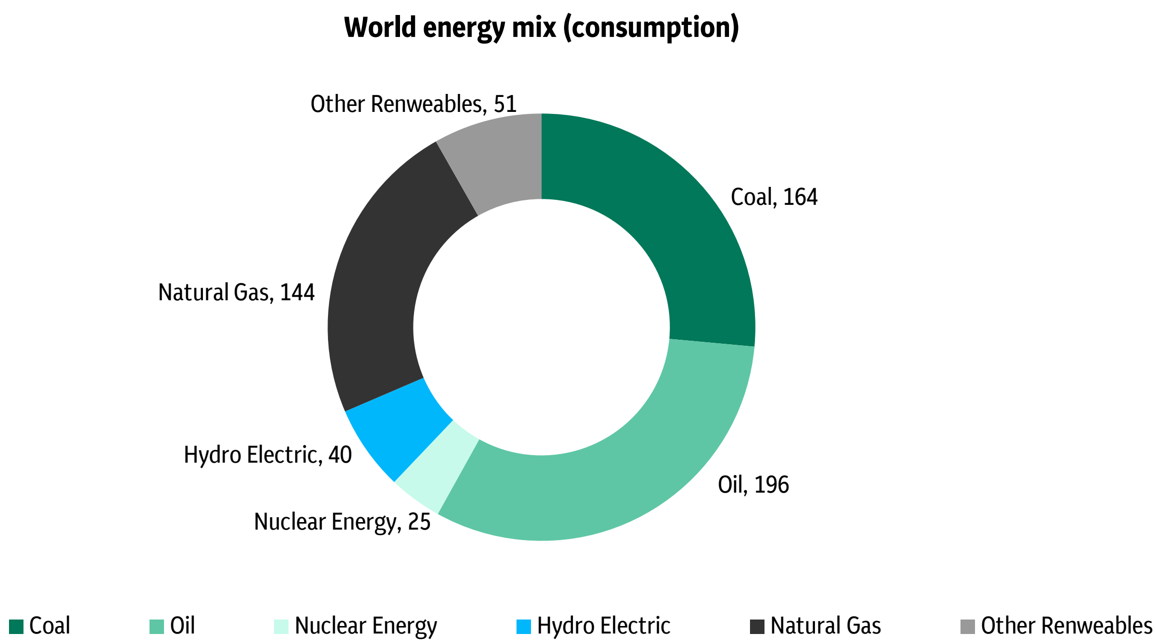
One example of a company expected to benefit from this is Cheniere Energy. Cheniere is the largest producer of liquified natural gas (LNG) in the US and the second largest LNG operator in the world. Cheniere operates two LNG facilities on the US Gulf Coast that process natural gas into LNG which is then loaded onto ships and delivered to countries globally. Cheniere has plans for capacity expansion at its facilities as it expects the global demand for its LNG to continue to grow as countries around the world seek cleaner ways to power their economies. In early 2024 the U.S. Department of Energy announced a pause on pending approvals for new LNG export projects. However, it is expected that President-elect Trump will remove this pause, allowing future LNG export projects to go ahead.

Sabine Pass LNG Terminal (Image: Cheniere Energy)

3. Gas and oil for longer

Another factor behind the rally in energy infrastructure stocks is the emergence of the “gas and oil for longer” thematic. With rising global energy demand forecasts and increasing challenges facing global energy transition, markets expectations around the decline in demand for fossil fuels are being adjusted. This has forced the market to reassess its view on the stranded asset risk of many energy infrastructure assets, as well as the terminal values ascribed to these businesses.

Despite the enormous global investment in renewables and energy transition to date, the world continues to rely heavily on fossil fuels. According to the Energy Institute, global primary energy consumption grew by 2% in 2023. A new record in the consumption of fossil fuels (in absolute terms) was recorded, with fossil fuels still accounting for over 81% of the global energy mix in 2023.



Source: Energy Institute, 2023 https://www.energyinst.org/statistical-review

Conclusion

Given the strong performance of listed energy infrastructure it has become more challenging to find value in the sector, but opportunities remain. We remain laser-focussed on strong infrastructure attributes, cashflow generation and minimal commodity price exposure in our Global Listed Infrastructure portfolio.

Contact us

Visit Macquarie Asset Management to find out more about our range of investments and how our solutions can help you to meet your goals.

Have a question? Please contact us and we will respond as soon as possible.

Key risks

The potential for adverse events in the global infrastructure sector to impact the performance of the investments of the Strategy. Investments in securities issued by companies which are principally engaged in the infrastructure business will subject the Strategy to risks associated with direct investment in infrastructure assets. Factors such as the availability of finance, the cost of such finance in general as well as in comparison to prior periods, the level of supply of suitable infrastructure projects and government regulations relating to infrastructure may influence the value of these investments and hence the Strategy.

The risks of investing in the infrastructure sector include those listed here.

New project risk: Where an infrastructure issuer invests in new infrastructure projects, it is likely to retain some residual risk that the project will not be completed within budget, within the agreed time frame and to the agreed specification.

Strategic asset risk: Infrastructure assets may include strategic assets, that is, assets that have a national or regional profile, and may have monopolistic characteristics. The nature of these assets may generate additional risk given the national/regional profile and/or their irreplaceable nature and may constitute a higher risk target for terrorist acts or political actions.

Documentation risk: Infrastructure assets are often governed by a complex series of legal documents and contracts. As a result, the risk of a dispute over interpretation or enforceability of the documentation may be higher than for other issuers.

Operation risk: Should an infrastructure issuer fail to maintain and operate the assets efficiently, the ability to maintain payments of dividends or interest to shareholders may be impaired. Failure by the infrastructure issuer to carry adequate insurance or to operate the asset appropriately could lead to significant losses and damages.

International investments entail risks including fluctuation in currency values, differences in accounting principles, or economic or political instability. Investing in emerging markets can be riskier than investing in established foreign markets due to increased volatility, lower trading volume, and higher risk of market closures. In many emerging markets, there is substantially less publicly available information, and the available information may be incomplete or misleading. Legal claims are generally more difficult to pursue. The Strategy may invest in preferred stock and hybrid securities, which may have special risks. Preferred and hybrid securities may include provisions that permit the issuer, at its discretion, to defer distributions for a stated period without any adverse consequences to the issuer. Some preferred and hybrid securities are non-cumulative, meaning that the dividends do not accumulate and need not ever be paid. A portion of the Strategy's assets may include investments in non-cumulative preferred or hybrid securities, under which the issuer does not have an obligation to make up any arrears to its investors. Preferred and hybrid securities may be substantially less liquid than many other securities, such as common stocks or US government securities. Generally, preferred and hybrid security holders (such as the Strategy) have no voting rights with respect to the issuing company unless preferred dividends have been in arrears for a specified number of periods, at which time the security holders generally may select a number of directors to the issuer's board. Generally, once all the arrears have been paid, the security holders no longer have voting rights. In certain varying circumstances, an issuer of preferred or hybrid securities may redeem the securities prior to a specified date. For instance, for certain types of preferred or hybrid securities, a redemption may be triggered by a change in federal income tax or securities laws. A redemption by the issuer may negatively impact the return of the security held by the Strategy.

Important information

Source for all performance data unless noted: Macquarie.

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