ClearBridge
A Franklin Templeton Company

Developed Markets Income Strategy

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Key Takeaways

- Infrastructure rose strongly in July, outperforming global equities. Signs of a long-awaited market broadening began to appear, driven by the strong prospect of a U.S. interest rate cut in September, cuts in other economies underway, and positive corporate earnings.
- Our global listed infrastructure strategies outperformed infrastructure benchmarks and global equities for the month.
- We remain defensively positioned as impacts of tightened financial conditions are expected to impact the economy and ultimately corporate earnings.

Market Overview

Infrastructure rose strongly in July, outperforming global equities. Signs of a long-awaited market broadening began to appear, driven by the strong prospect of a U.S. interest rate cut in September, cuts in other economies underway, and positive corporate earnings. U.S. 10-year Treasury yields declined on economic reports and growing investor optimism for rate cuts during the month, ultimately ending at 4.04%, or 36 basis points lower.

Among listed infrastructure sectors, communications and renewables performed well on an easing monetary environment. Water utilities also outperformed; in the U.K., the regulator's draft determination base weighed average cost of capital was released and in-line with the consensus range, alleviating some uncertainty heading up to the determination. This will still involve some maneuvering however, before the determination is finalised in December. Oil prices declined to their lowest level in nearly two months, as faltering Chinese growth weighed on expectations for global demand. The price per barrel of WTI crude fell from $81.54 at the beginning of the month to $77.91 at the end. Energy infrastructure was among laggards in the infrastructure market. Meanwhile, rail performed well amid higher volumes. U.S. rails saw minimal damage from Hurricane Beryl and Houston flooding, with cleanup going better than expected and no material downside to operations.

Portfolio Highlights

Our global listed infrastructure strategies outperformed relevant infrastructure and global equities benchmarks for the month.

On a regional basis, the U.S. and Canada (+4.01%) was the top contributor for month, with U.S. communication companies American Tower (+0.61%) and Crown Castle (+0.58%) the lead performers. American Tower is a leading independent owner, operator and developer of wireless and broadcast communications infrastructure. The company has 41,000 sites in the U.S. and a further 139,000 sites across 19 countries, predominantly emerging markets (75,000 in India, 40,000 in Latin America and 18,000 in Africa).

Crown Castle is the leading independent owner and operator of wireless communications infrastructure in the U.S. with a portfolio of approximately 40,000 towers.

Shares of American Tower and Crown Castle outperformed as the market favoured more defensive sectors, while tower stocks, being notably sensitive to interest rates, experienced additional benefits due to the decline in bond yields.

U.S. electric utility Constellation Energy (-0.14%) and U.S. renewables utility NextEra Energy Partners (-0.21%) were the largest detractors.

Constellation Energy (**Constellation**) is primarily a nuclear generation company and is the largest producer of carbon-free electricity in the U.S., serving states including New York, Illinois, Maryland, Pennsylvania and New Jersey. The company's combined generation capacity is more than 32 GW and 90% of annual output is carbon free. Constellation shares fell amid concerns of potential challenges to behind-the-meter generation, to which we ultimately ascribe low probability of going through.

NextEra Energy Partners (**NEP**) is a growth-oriented contracted renewables company formed by its sponsor and general partner NextEra Energy to own, operate and acquire contracted renewable energy generation assets located in North America. NEP's share price fell due to disappointing commentary from management on their financial restructuring and capital allocation plan.

During the month, we exited our position in Japanese rail operator West Japan Railway.

All returns are in local currency.

Positioning and Outlook

We remain defensively positioned as impacts of tightened financial conditions are expected to impact the economy and ultimately corporate earnings. Inflation has been trending down thanks to the cooling off in areas such as wage inflation and rents, leading to increasing confidence by market participants that we are at the end of the rate hiking cycle and now looking toward the start of the rate-cutting cycle. We believe this could be the start of the turn for many of our long-duration assets that underperformed for most of 2023, such as towers and renewables. Utilities should continue to benefit from themes of electrification, renewables growth and more recently higher electricity demand from data centres, and we remain constructive on the sector, given reduced valuations.