Emerging Markets Strategy

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Our global listed infrastructure strategy outperformed global equities for the quarter.

The outlook for interest rates and inflation continues to cause volatility in markets following the outbreak of the conflict between Ukraine and Russia. We expect this volatility to continue as the market digests the impact on inflation and global growth.

Geopolitical risks, ongoing COVID-19 disruption, supply chain issues and high inflation continue to reduce expectations for economic growth, although a recession is still not considered the base case.

In emerging markets, the Chinese equity market, in particular, experienced weakness due to COVID outbreaks and lockdowns, coupled with internet sector concerns from a regulatory crackdown and ADR de-listing threats.

Portfolio Performance

On a regional basis, Latin America was the top contributor to quarterly performance (+4.30%), of which Mexican airport operator Grupo Aeroportuario del Pacífico (+0.62%) and Brazilian toll road operator CCR (+0.62%) were the lead performers.

Grupo Aeroportuario del Pacífico SAB de CV (GAP) is Mexico’s largest airport operator with a portfolio of 13 airports focused in Mexico’s Pacific region with an additional airport in Jamaica. GAP continued to perform well during the first quarter as passenger traffic continued its strong pace of recovery. Additionally, the company hosted an investor day and outlined bullish expectations for future volumes.

CCR is Brazil’s largest public infrastructure concession holder, operating concessions across motorways, urban mobility (sea ferries, subways, light rail) and airports. CCR was up in the first quarter following a favourable conclusion on their final contract rebalances and news that Andrade Gutierrez were in advanced talks in selling their stake in the company, which should help its corporate governance.

Turning to Asia Pacific, Philippines-based port operator International Container Terminal Services (+0.65%) and Malaysian airport operator Malaysia Airports (+0.62%) also performed well during the quarter.

International Container Terminal Services operates terminals through long-term concession agreements with local port authorities and governments. The company’s FY21 results beat market expectations and it is achieving healthy operational trends year to date.

Malaysia Airports is one of the world’s largest airport operators by passenger numbers. Based in Kuala Lumpur, it operates all but one airport in Malaysia and also has a 100% stake in Istanbul’s Sabiha Gokcen Airport. The share price of Malaysia Airports benefited from the positive outlook for the reopening of international borders.

Chinese electric utility China Resources Power (-1.64%) was the largest detractor from quarterly performance.

China Resources Power (CRP) is an independent power producer (IPP), operating 33GW of thermal power units and 17GW of wind and solar power units in China. Its holding company is China Resources Group, a major state-owned conglomerate. Shares were down mainly due to market concerns over its planned renewables spin-off potentially not maximising value for shareholders. Losses in the second half of 2021 across coal-fired plants in China, due to rising coal prices putting pressure on 2021 earnings also triggered some profit-taking in the IPP sector after a strong rally in December.

All returns are in local currency.

Positioning and Outlook

This strategy is invested in high-quality companies benefiting from structural drivers, with strong cash flow and dividend yields. We have strong conviction in the long-term opportunities within emerging markets listed infrastructure. At the regional level, the majority of the strategy is split between Asia Pacific EM (57%) and Latin America (40%). At the sector level, the strategy is split between economically sensitive user-pays infrastructure (58%) and regulated and contracted utilities (40%).

For the **Global Infrastructure Emerging Markets Strategy**, the primary quantitative tool in portfolio construction is excess return, on which our stock-ranking system is based. As such, driven by valuation, the Investment Committee initiated positions in Brazilian electric utility Auren Energia, Chinese port operator China Merchants Port Group, Philippines electric utility Aboitiz Power and Thai airport operator Airports of Thailand.

The strategy also used the opportunity to crystallise some gains by exiting Malaysian electric utility Tenaga, Chinese port operator Shanghai International Port Group, Indian energy infrastructure companies Gujarat Gas and Gujarat State Petronet and Philippines infrastructure conglomerate Metro Pacific Investments Corporation.

Quarterly Stock Highlight

This quarter we review Mexican communications company Telesites.

Telesites is a Mexican communications company with communication towers distributed across Mexico.

Telesites rents space on its towers on long-term contracts with duration of 5–7 years. Most of the company's contracted communication towers distributed so far have been with Telcel (owned by Mexico America Movil). These contracts are adjusted for Mexican inflation and, given the financial strength of mobile carriers, the revenue stream is highly predictable.

We believe Telesites is well-positioned to take advantage of both the potential increase in tower densification in Mexico and the gradual conversion of their tower portfolio into a FIBRA structure. A FIBRA structure has significant tax benefits for Telesites whereby local investors are exempt from paying tax on distributions. Over the last years Telesites began the gradual process of ceding towers into a FIBRA, thereby generating significant value for shareholders.

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