KEYNOTE INTERVIEW

The evolving net-zero opportunity

Supportive regulation is good for the health of the sustainable infrastructure ecosystem and makes it easier for private equity players to step in, says Infracapital's Alexia Savva

Investment amounting to trillions of dollars is needed to make the energy transition a reality over the coming decades. It's no surprise, then, that infrastructure has risen to prominence in recent years as an asset class rich with opportunities.

However, finding those investments with strong sustainability metrics across the board – and with valuations not caught up in the hype – is easier said than done, explains Alexia Savva, head of responsible investment at Infracapital. A changing regulatory landscape and issues such as greenwashing complicate the picture further.

So, what factors need to be front of mind for infrastructure investors weighing up sustainable and energy transition-focused opportunities?

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Q Significant financing is needed to facilitate the global energy transition. Where are the best investment opportunities as a result?

We see an enduring investment gap requiring private capital investment. The International Energy Agency estimates that a cumulative $150 trillion is required by 2050 in order to limit global warming to a 1.5C increase. That means the investment opportunities are vast, especially given that we are also grappling with constrained balance sheets for both governments and corporates. The bulk of that required investment will therefore need to come from the private space.

Looking specifically at Europe, most of the continent's emissions are generated by just a handful of sectors – including transport and industrials, each of which contributes circa 25 percent of Europe's total emissions. We are seeing opportunities to invest here that are both attractive from an investment

point of view, as well as when considered as an opportunity to contribute to wider decarbonisation efforts. This includes themes like the electrification of heating, biomass, hydrogen, carbon capture and storage, and so forth.

In transportation, for instance, there continues to be a regulatory spotlight on the sector's efforts to decarbonise. Mandated transition timeframes in Europe, a modal shift from road to rail, and the need to decarbonise logistics, such as through green shipping and sustainable aviation fuels, are among the main drivers of this change. We aim to invest behind these sustainability trends where they are supported by strong macro tailwinds and robust infrastructure characteristics.

One example is our investment in Inland Terminals Group, an inland barge operator in the Benelux region that we have been invested in since 2021. Transitioning cargo supply from trucks to barges delivers a 75 percent carbon saving, and we have been working with the business to further advance the electrification of its operations for commercial and environmental benefit, including the launch of the world's first hydrogen barge with partner Nike last year.

Q How challenging is it to integrate other sustainability considerations, such as biodiversity, human rights and a just transition, when investing in climate solutions?

We cannot address the climate challenge in isolation, because other elements of sustainability are inextricably intertwined with it.

For example, there are a number of minerals – such as cobalt and lithium – that are key to the energy transition, in particular when it comes to energy storage and solar assets. Accessing these minerals can raise numerous human rights issues, though, around indigenous people's rights, labour rights, access to water and so on. We need to have robust policies and practices in place, coupled with proactive industry engagement, to ensure we protect vulnerable communities and take all these things into consideration when delivering the infrastructure needed to reach net zero.

Some of these challenges touch the whole infrastructure industry. For instance, there is a lack of diversification in the solar supply chain when it comes to some of the specific components required for solar PVs. So, how do we work together as an industry to encourage and foster more sustainable practices? Obviously, we work in a very competitive industry, but there are ways we can work with others to really move the dial on some of these shared issues.

Biodiversity is also a central component of achieving net zero, and we have seen a greater emphasis being placed on this in recent years. This has highlighted a challenge that investors have been facing for some time, which is that it is difficult to put an economic value on natural capital for the purposes of infrastructure investing. This is gradually changing thanks to things like the Taskforce on Nature-related Financial Disclosures' recommendations, but the more we can monetise these factors, the more thoroughly integrated

Q Infrastructure is known for its exceptionally long time horizons. Is that difficult to align with the urgent need for progress on the energy transition?

The energy transition will not happen overnight. While there is a requirement to build new infrastructure over the long term, it's also about transitioning existing businesses and their assets, and that work has started.

Looking at the industrial and transport sectors again, to achieve long-term value creation, these companies need to develop their transition pathways. That means mitigating risk and searching for value-accretive opportunities. In some cases, businesses will need to revisit their overall purposes and diversify their revenue streams.

Regulation can play a role in accelerating these transition timeframes. It's essential that we marry up that need to build new infrastructure with the changes required to existing businesses and assets.

sustainability considerations will be within the investment decision-making process.

Q How have the various sustainability regulations in capital markets affected investors? Are these helping when it comes to finding sustainable investment opportunities, or is there an element of overregulation?

A range of mechanisms have been introduced to support private sector engagement. This includes NextGenerationEU, which is the EU's largest ever stimulus plan. This aims to bridge the funding gap in areas that infrastructure managers like us play into, using things like tax incentives, corporate power purchase agreements and other forms of subsidies. These measures facilitate investment and make Europe a particularly compelling infrastructure market.

When we look at other regulatory updates, these are not just aimed at funds but are also designed to compel change among the underlying companies. This kind of regulation increasingly aligns with our sustainability goals, giving businesses and their investors confidence to innovate and transition to more sustainable models.

We have seen a wave of these kinds of regulations, including the SFDR, the CSRD and all the other acronyms which have been introduced to encourage greater transparency in the financial sector and corporates alike. There is certainly benefit to these regulations, but it is important that there is close interaction between regulators and the investment world to ensure that those regulations that aim to direct capital towards sustainable practices are fit for purpose.

Q To what extent is the hype around sustainable investments causing challenges, such as excessive valuations or greenwashing?

There have been several moves recently to mitigate the risk of greenwashing, such as the FCA's anti-greenwashing regulations in the UK and the EU's SFDR. These have all tried to enhance transparency, via greater disclosures on risk, outcomes, what managers intend to do, and so on. The push for better and more accurate data isn't without its challenges, but it moves us away from sustainability being purely qualitative in nature, which is something that has historically left the sector open to excessive claims, valuations and greenwashing.

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In terms of valuations, it is challenging that there are still a number of factors linked to sustainability that are hard to monetise. A strong sustainability proposition can drive value in terms of differentiation, brand strength, a diverse and inclusive workforce, and these can be hard to put a specific value on. We are seeing real value in those businesses that are leaders in their areas from a sustainability perspective. They are demanding greater multiples at the point of exit, but it is difficult to put an exact figure on that.

It is really important to dig into sustainability claims at the due diligence stage. We want to see if there is data to back up any claims, and we want to see if the sustainability aims in an asset are commercially viable to achieve. With increasing regulation, and the demand for more – and more accurate – data, I am sure it will get much easier, as investors, to see who has just been paying lip service to sustainability.

Q What is the outlook for the energy transition's role in UK and European infrastructure investment?

There are significant investment opportunities in the UK and Europe, with decarbonisation driving growth beyond the renewables sector. For instance, we are looking at biogas, energy storage and hydrogen: there is a wide range of opportunities across many sectors.

The energy sector is in the middle of an unprecedented low-carbon transition, with policymakers having to balance affordability with security of supply. This transition is not without its challenges for investors, due to factors such as technological uncertainty and delays. We do expect momentum to accelerate further, but investing here will remain a question of coupling sustainability characteristics with where we see proven infrastructure characteristics.

In the UK in particular, we have seen decades of underinvestment in infrastructure. As a proportion of GDP, for example, investment in the UK's infrastructure is much lower than in the other G7 economies. Investment of around £40 billion per annum ($52 billion; €48 billion) in new assets is required to meet the UK's net-zero target of 2050, and the government wants at least half of that to come from the private sector, which makes for a significant investment opportunity.

Other factors are also stimulating this opportunity. We have seen a push for UK pension capital to contribute to infrastructure projects, political commitments to remove obstacles, and cross-party objectives aligned to the needs of infrastructure investments. We are looking at ways we can develop our own strategies to target and address these investment needs in the UK. ■