Results analysis: BBGI Global Infrastructure

BBGI's availability-style holdings proved robust in H1...

Update
06 September 2023

- **NAV total returns for BBGI fell modestly by 1.4% in the first half of 2023. This was mainly due to foreign exchange movements and a change in the discount rate, itself largely caused by interest rate hikes in the UK impacting UK assets, which are 33% of BBGI's portfolio. Despite this small decline, the trust has delivered a strong track record of 8.8% annualised NAV total returns since IPO in 2011. At the end of the period, the shares traded on a 6.6% discount to NAV.**

- **BBGI saw strong operational performance of its globally diversified portfolio of 56 high-quality, 100 per cent availability-style infrastructure assets. BBGI maintained a consistently high asset availability rate of 99.9%. As at 31/08/2023, the trust was fully operational.**

- **Cash receipts for the trust were ahead of projections, with no material lockups or defaults reported. BBGI also maintained strong cash dividend cover of 1.68x in H1 2023 and reaffirmed dividend targets of 7.93 pps for 2023 and 8.40 pps for 2024, representing a 6% increase year-on-year, and a dividend target of 8.57 pps for 2025. All dividends are expected to be strongly cash-covered.**

- **The negative valuation effects on the trust's NAV were partly mitigated by increased deposit and inflation rates. BBGI's proportional share of cash holdings in portfolio companies stood at approximately £385m as at 30/06/2023. Interest paid on these holdings has risen substantially over the past two years and averaged approximately 4.5% during the period. Changes in short and long-term deposit rate assumptions resulted in an increase to NAV of approximately 1.2%.**

- **BBGI's discount rate increased by 0.3% to 7.2% during the period. The weighted average risk-free rate of the BBGI portfolio stayed flat during the period at 3.8%. As such, the trust's discount rate includes a 3.4% risk premium, arguably a conservative figure given the resilient availability-style assets the trust invests in and their high-quality inflation linkage.**

- **The trust's inflation linkage also rose in the period to 0.6x. This means that for every 1% that inflation increases above the levels assumed by BBGI, returns should increase by 0.6%. This is achieved primarily by inflation linked contracts that BBGI has with its public sector counterparties and which are then mirrored with the subcontractors.**

Analysts:

David Kimberley
david.k@keplerpartners.com

- **BBGI Chair Sarah Whitney said: "As an internally-managed investment company, our leadership team's alignment of interest with our shareholders is clear. In this period of economic volatility, we will continue to be disciplined in our approach to capital allocation and will only consider transactions that are accretive to our shareholders. BBGI has not been immune to the uncertain market and economic backdrop that has impacted investor sentiment on almost all UK listed investment companies. The board does not believe the current share price adequately reflects the value of the portfolio and its high-quality inflation linkage, nor does it reflect our strong financial position and operational performance."**

Kepler View

BBGI Global Infrastructure (BBGI) provides investors with access to a portfolio comprised solely of availability-style assets, backed by AAA/AA government and government-backed counterparties. These are public infrastructure assets that generate revenue as long as they are available for use, meaning they are not subject to the price elasticity of demand or the regulatory risks that demand and regulatory-based assets can be susceptible to. The contracts underpinning these investments have strong inflation linkage, which acts in a mechanical way, as cash flows increase in line with a relevant price index.

Despite seeing a small fall in its NAV, performance in the first half of this year in many ways demonstrated how resilient BBGI's portfolio can be. The large majority of the small NAV decline was attributable to changes in FX rates that were not fully covered by the trust's hedging strategy, and a 50bps increase in UK interest rates. With the UK currently representing about a third of the BBGI portfolio, this fed into a higher discount rate for the portfolio as a whole, which rose from 6.9% to 7.2% in the first half of the year. As much as investors may like them to, it is hard to see what BBGI could have done to offset these macroeconomic performance drivers.

However, the factors that are under their control look more positive. The trust's long-term returns remain strong, with annualised NAV total returns steady at 8.8% since IPO in 2011. BBGI remains on track to pay its target dividend of 7.93pps this year, representing a 6% year-on-year increase. That is fully covered at 1.68x from cash generated by the underlying portfolio. The trust's substantial cash holdings in portfolio companies, totalling approximately £385m, are also starting to generate meaningful revenue, with the managers securing competitive deposit rates that average approximately 4.5%.

Although investors have been understandably fearful of the large levels of debt that some infrastructure investors make use of, BBGI's loans are taken out at the individual portfolio company level and are non-recourse. Loans are overwhelmingly fixed rate and amortised over the lifespan of the project, meaning they are not subject to the sort of refinancing risk we see in much of the property sector. Indeed, of the 56 projects that BBGI is invested in, only one is subject to refinancing risk for a tranche of the debt and even in this instance BBGI has hedged the underlying base rate and only the loan margin is subject to negotiation.

With a weighted average risk-free rate of 3.8% across the BBGI portfolio, the trust's current discount rate means there is an implied risk premium of 3.4%. With the trust trading at an 11.6% discount to NAV as at 31/08/2023 , we think the trust offers a compelling mix of downside protection and upside potential. The trust's high quality inflation linkage and AA/AAA counterparties offer strong protection against further volatility and unexpected inflation spikes. At the same time, if we are entering a more benign environment and have reached the end of the rate hiking cycle, the trust's high dividend yield may start to look more attractive again, potentially resulting in a tightening of the discount.

Click here to read the HY report on RNS

Click here to read our latest research on BBGI

Click here to add BBGI to your watchlist

Disclaimer

This report has been issued by Kepler Partners LLP. **The analyst who has prepared this report is aware that Kepler Partners LLP has a relationship with the company covered in this report and/or a conflict of interest which may impair the objectivity of the research.**

Past performance is not a reliable indicator of future results. The value of investments can fall as well as rise and you may get back less than you invested when you decide to sell your investments. It is strongly recommended that if you are a private investor independent financial advice should be taken before making any investment or financial decision.

Kepler Partners is not authorised to make recommendations to retail clients. This report has been issued by Kepler Partners LLP, is based on factual information only, is solely for information purposes only and any views contained in it must not be construed as investment or tax advice or a recommendation to buy, sell or take any action in relation to any investment.

The information provided on this website is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject Kepler Partners LLP to any registration requirement within such jurisdiction or country. In particular, this website is exclusively for non-US Persons. Persons who access this information are required to inform themselves and to comply with any such restrictions.

The information contained in this website is not intended to constitute, and should not be construed as, investment advice. No representation or warranty, express or implied, is given by any person as to the accuracy or completeness of the information and no responsibility or liability is accepted for the accuracy or sufficiency of any of the information, for any errors, omissions or misstatements, negligent or otherwise. Any views and opinions, whilst given in good faith, are subject to change without notice.

This is not an official confirmation of terms and is not a recommendation, offer or solicitation to buy or sell or take any action in relation to any investment mentioned herein. Any prices or quotations contained herein are indicative only.

Kepler Partners LLP (including its partners, employees and representatives) or a connected person may have positions in or options on the securities detailed in this report, and may buy, sell or offer to purchase or sell such securities from time to time, but will at all times be subject to restrictions imposed by the firm's internal rules. A copy of the firm's Conflict of Interest policy is available on request.

PLEASE SEE ALSO OUR TERMS AND CONDITIONS

Kepler Partners LLP is authorised and regulated by the Financial Conduct Authority (FRN 480590), registered in England and Wales at 70 Conduit Street , London W1S 2GF with registered number OC334771.