All eyes on energy and infrastructure investment

The new government has already placed its focus on infrastructure and energy investment, with its proposed creations of Great British Energy (GBE) and a National Wealth Fund (NWF). What do these mean for these sectors, and what opportunities do they provide for pension funds as investors?

The new government is committed to economic growth powered by greater private sector investment – pension funds clearly have a significant role to play. The design of the state institutions designed to crowd in pension capital for UK 'nation-building' projects will be crucial: Namely how the new players i.e. Great British Energy (GBE) and the National Wealth Fund (NWF) interact with the existing UK Infrastructure Bank (UKIB) and British Business Bank (BBB).

There continues to be a major focus from the government on the demand side of the equation – consolidating UK pension funds so they become natural allocators to private markets. This is reasonable. Where UK pension funds are already significant investors in these asset classes it is the larger funds in the lead. But there are many small UK funds, so scaling up makes sense.

But more attention should be paid to the supply side, to the creation of a pipeline of investable assets. This demands public monies – largely taxpayer guarantees – to underwrite new technology risk and to structure nascent 'green' markets. This, as well as the 'structuring' role to be played by the state backed financing institutions whether GBE/NWF/UKIB/BBB, is the key to success in crowding in new pension capital. After all, there is no shortage of things to be done in the UK, if we are to deliver 2030 net zero targets, never mind 2050. Good financing models can unlock the capital needed for these new projects.

IFM Investors executive director, public affairs Europe, Gregg McClymont

Robust and well-maintained infrastructure is crucial for economic growth, productivity, and competitiveness because it facilitates trade, attracts investment, and enhances quality of life. The newly elected Labour government's initiatives demonstrate the UK's commitment to addressing the country's infrastructure needs and positioning the UK as a leader in sustainable and resilient infrastructure development.

The government's next decade infrastructure strategy has a particular focus on roads, railways, and the roll out of electric vehicles (EV) charging points. This focus on modernising the transport network is key for the UK's ambition to reduce its carbon footprint, since transport currently accounts for approximately a quarter of EU greenhouse gas emissions. Additionally, the modernisation of the UK economy requires investments in technology and digital infrastructure such as gigafactories for EVs, the roll out of national 5G coverage, and the removal of barriers to new data centres. The new National Wealth Fund aims to invest £7.3 billion in UK infrastructure which should complement the public-private partnerships (PPP) for the development of electric vehicle charging networks and to help fund initiatives for heat, power plants, battery storage, and others. Overall, an estimated £29 billion could be invested to modernise the UK infrastructure.

Global X ETFs head of investment strategy, Morgane Delledonne

The National Wealth Fund will only be effective if it solely funds areas where there is genuine market failure and has the potential to unlock large amounts of private capital. Examples of these market failures include investment in new grid infrastructure urgently needed to allow the adoption of renewable energy and BESS; investment in the planning and

permitting stages of new sustainable infrastructure projects needed to bring forward the environmental and social solutions we need; and funding of the rural alt-net sector; the bank market is currently closed due to over concentration to large urban fibre builds.
Gresham House managing director, sustainable infrastructure, Peter Bachmann

Above all, those making decisions on pension scheme investments will need certainty that such assets will work in the interests of members, either in backing the pension income they have been promised or generating returns to help them create an adequate pension fund for retirement.
Royal London director of policy, Jamie Jenkins

The government's plans to establish GB Energy and launch a National Wealth Fund have the potential to accelerate public and private investment in green infrastructure.

Various attempts have been made to mobilise such investment, but the absence of a pipeline of investable opportunities and the political uncertainty in recent years has made it difficult for this to become a reality.

The introduction of these new initiatives will hopefully start to realise this ambition by putting in place a structure that provides confidence and certainty for those making long-term investment decisions.

While there is clearly a lot of detail to work through, there is potential for the National Wealth Fund to act as the investment vehicle, powering GB Energy as the engine for change in renewal infrastructure.

The launch of GB Energy and Labour's ambitious renewable energy targets, including tripling solar capacity and quadrupling offshore wind by 2030, signal a significant shift in the energy landscape.

With £8.3 billion in funding for GB Energy and an additional £60 billion in private investment being sought, there is potential for considerable expansion. Pension funds may find these developments appealing, given the long-term, stable returns often associated with infrastructure investments. However, the success of these projects will depend on overcoming hurdles such as supply chain constraints, regulatory challenges, and community acceptance. Ed Miliband (the new Secretary of State for Energy Security and Net Zero) has specifically said his focus will be on tackling the 'four horsemen' of the UK's energy transition; grid delays, planning delays, supply chain problems and the skills gap.

Labour's proposal to create a £7.3 billion National Wealth Fund, aimed at financing infrastructure projects, presents another area of interest. It is intended to drive £20 billion of private sector money into low-carbon investment in the UK economy. The track record of the UK Infrastructure Bank, which has successfully mobilised private capital, suggests that the National Wealth Fund could attract significant private investment. However, the details of how the National Wealth Fund will operate, particularly its interaction with existing schemes and its approach to private sector partnership, will be crucial in determining the level of interest from investors.
Gravis spokesperson

The new Labour government has a particular focus on infrastructure and clean energy as one of the ways to create economic growth during their time in parliament. From their manifesto and the King's Speech, we understand that the initial areas of focus will be upgrading ports and the supply chain across the UK, building automotive gigafactories and rolling out EV charge points, rebuilding the steel industry, supporting sustainable aviation fuel, and investing in carbon capture and green hydrogen production.

We understand that Great British Energy will partner with industry and trade unions to deliver clean power by co-investing in leading technologies and supporting capital-intensive projects.

It's quite clear the Labour government wants to make the UK a renewable energy power with a state-owned energy company similar to France's EDF or Denmark's Orsted.

The clear ambition is a great signal to infrastructure investors because an infrastructure asset typically has a useful life of 20-45 years, and someone investing for that period of time wants to have a clear long-term direction of travel.

We have a new government that knows what it wants to achieve and wants to work with industry to get there. While the ambition is welcome, the difficult part of any infrastructure project is delivery in line with specifications on time and on budget.

That is the difference that investors

are waiting to see – if the new government will take the necessary actions to deliver on promises such as a net-zero power grid by 2030.

Creating the right environment that shows the government is willing to do what it takes to deliver the green transition will draw large institutional investors to the UK.

Within the UK, closed corporate defined benefit schemes, which are targeting long-term self-sufficiency, could be interested in investing in infrastructure due to the long-term inflation linked and contracted income such assets can provide.

Closed schemes targeting buyout would not be interested in these investments because they are too long-term for their investment strategy.

Local government pension schemes are interested in these assets and have been investing in them over the past five-ten years. These schemes already have an allocation to green infrastructure and while they could invest more, infrastructure is only be going to be a small part of their total portfolios due to the illiquidity and risk concentration of such investments.

Hence, UK pension schemes might invest a bit more in infrastructure given the new government's ambition and focus.

However, if the government successfully addresses the challenges of red tape around planning, slow connections to the grid and skills shortages in the green energy sector, that could unlock investment from foreign investors who will see that the United Kingdom is a place where return on investment has a high certainty. Once we see evidence that this government is doing things differently, this will help to draw back big infrastructure investors who can match the scale of the government's ambitions.

Hymans Robertson senior investment research consultant, Asad Rashid

We believe the NWF can serve as a key accelerant for the UK to do its part in transitioning to a low carbon economy and promoting growth in the UK.

The NWF is a new offering/opportunity for investors and has many desirable and laudable characteristics. The most notable characteristic is the goal of supporting and nurturing new industries of the future, including the design and targeting of green infrastructure investment.

The initial c£7 billion funding injection to the NWF from the UK Infrastructure Bank is a statement of intent. This funding can be thought of as seed investor capital with the government putting its money where its mouth is.

Given the infancy of the NWF, it is not clear yet to what extent pension funds will follow and allocate capital to the NWF. If we think of the pensions industry, as a whole, as having trillions of pounds of assets, the questions are:

1. how much of that is likely to be redeployed to the NWF; and
2. what are the consequences of doing so i.e. who is losing out as a result of having money taken away from them?

In practice, the key drivers of pension scheme investment in the NWF are likely to be:

- Investor time horizon
- Long term objective of the pension scheme
- Governance capacity and skill set of those running the scheme.

The NWF will be investing a large proportion of its funding in illiquid, J-curve infrastructure assets. Therefore, the investor time horizon for those schemes that are well-funded, with a target of securing the liabilities with an insurer, is unlikely to align with an investment in the NWF.

The most likely source of pension scheme investment in the early years at least, is likely to be schemes that are:

- Open to accrual, which is predominantly public sector arrangements but also some private sector schemes.
- Closed schemes that are looking to run-on the scheme in-house

We would expect this cohort of schemes to be relatively small by number but substantial in terms on pound amounts. So, assuming a £2-3 trillion pension scheme industry in the UK, if only those that are DB and open and LGPS allocate to the NWF, that is estimated to equate to c£570 billion of assets where the investor is likely to have a sufficiently long time horizon to consider investment in NWF. Typically speaking, pension schemes would have a c5 per cent allocation to any single illiquid investment opportunity, and so it is feasible that a further c£30 billion of private investment could flow into the NWF. If this were to materialise this would ensure that the political target of attracting £3 of private investment for every £1 of public funding from the UK Infrastructure Bank would be achieved.

Macquarie Asset Management managing director, Alastair Yates