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NATIXIS INVESTMENT MANAGERS

Covid 19:

What is the impact on infrastructure debt worldwide?

Europe, The Americas and APAC are the three largest infrastructure markets in the world. While there is a timing difference between these markets in terms of the spread of Covid-19, our analysis of the situation for infrastructure debt remains the same, whatever the region.

Infrastructure debt is very resilient….

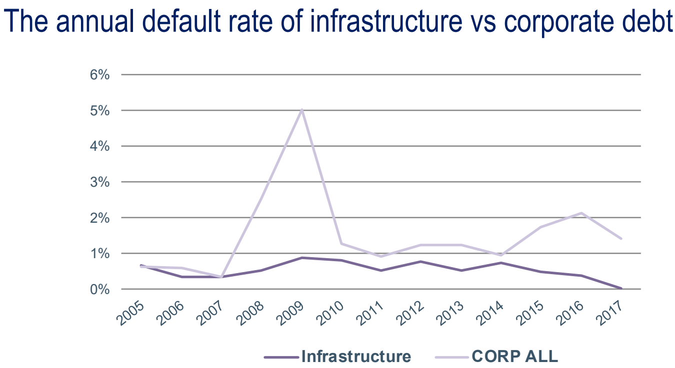
Infrastructure, as an "essential" asset for the economy, is better protected than other sectors. Electricity, energy, water, telecom and transportation remain vital for the economy of each country. As a consequence, **infrastructure and especially infrastructure debt is usually very resilient in periods of crisis.**

This has been demonstrated during previous crises…

In March 2020, Moody's released its annual study on "Default and recovery rates for project finance bank loans, 1983-2018". This study underlines the following points:

- "**The average 10-year cumulative default rate (CDR) is stable at 5.5% and remains at its lowest level since the study's inception**. By comparison, corresponding CDRs for Baa3-rated corporates are 5.1% and those for Ba1-rated corporates are 9.5%";
- **"Ultimate recovery rates for project finance bank loans average 77.9%** (Basel), consistent with the March 2019 study."

The graph below illustrates the annual default rate of Infrastructure compared to corporate debt and **the resilience of infrastructure debt compared to corporate debt** during the last two Financial Crises.



Source: Moody's default and recovery rates for project finance bank loans study dated of March 18, 2019 and Annual Default Study: Corporate Default and Recovery Rates, 1920-2017

The Covid-19 crisis will test this resilience….

Previous crises, i.e., subprime and sovereign, began as "financial crises", with resulting impacts on the economy. **The Covid-19 crisis is different:** it has a direct impact on the economic activity of each country and on global trade. This could then result in financial and sovereign crises.

At this stage, we anticipate the following **direct impacts on the infrastructure sector:**

- **Demand:** slow down in demand; i.e., traffic, electricity /oil consumption;
- **Prices:** impact on unregulated markets such as commodities;
- **Supply chain:** constraints on construction, labor, etc.

As a consequence, **some sectors or companies such as the following will be more impacted** than others:

- **Transportation infrastructure** with traffic risks (airports, roads, railways);
- Sectors or companies **requiring strong supply chains or labor force** (in frastructure in construction or transformation plants);
- **Energy infrastructure** with a merchant component (due to the impact of oil and electricity on prices).

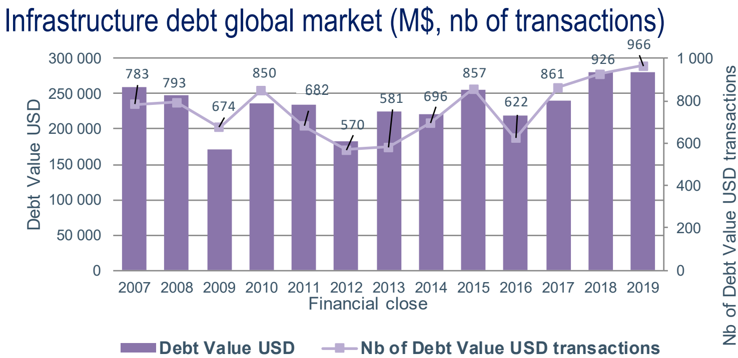
There may also be more **indirect impacts** such as:

- **Cost of liquidity** for banks and **access to liquidity** for corporates;
- **Country risk** evolution and potential **downgrades**.

Nevertheless, **infrastructure is a heterogeneous sector,** and the impact of the crisis may differ depending on: **sectors, operating & supply importance, seniority and security package**.

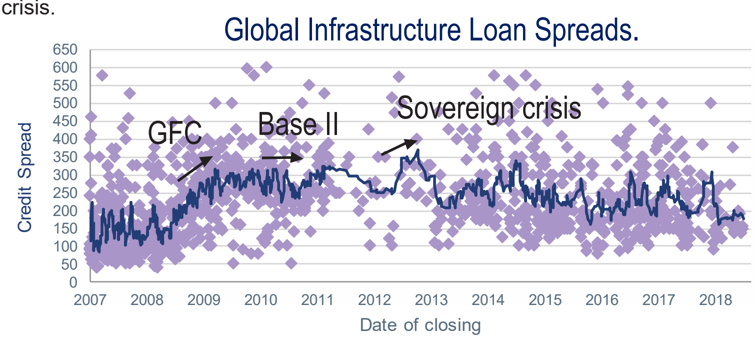
As of today, we anticipate three likely outcomes:

1 **2020 market volume of new transactions will decrease** (some financing packages are already delayed) **compared to 2019 but we expect a shift of deals from 2020 to 2021**, as this was observed during the previous crisis.



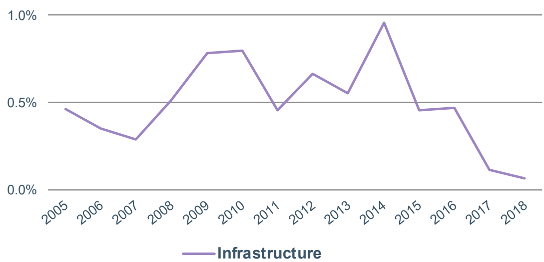
Source: Infrastructure Journal and Ostrum AM, data as of end 2019.

2 **Pricing will increase** due to (i) **increase in cost of liquidity** and (ii) update of **risk assessment** on some sectors such as **transportation**, as this was observed during the previous crisis.



Source: Infrastructure Journal and Ostrum AM, data as of end 2018.

3 **Some downgrades for the transactions or sectors most at risk**; however, **we do not anticipate major payment defaults** in 2020, at least not in Europe at this stage.



Source: Moody's default and recovery rates for project finance bank loans study dated of March 9, 2020

We are closely monitoring the evolution of the following factors:

- **The lock-down situation** around the world, especially in the US but also in developing countries;
- National and international (EU, G7, G20) **economic support plans;**
- **The liquidity situation** for corporates and banks;
- **Sovereign bond** r**atings** and **pricing**.

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