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TAKING FLIGHT

How investing in infrastructure helps our cities soar

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Taking Flight

How investing in infrastructure helps our cities soar

By Gregory Smith and Sarah Borg-Olivier, InstarAGF Asset Management Inc.

Sound infrastructure – roads, transportation, electricity and water systems – is necessary for communities and countries to thrive, and is a major driver of where companies and people choose to live, work and do business. Infrastructure quality can accelerate or erode an economy, so investing in it is an urgent priority.

While the federal government has shifted more attention and dollars to infrastructure in recent years, the amount of available financing falls far short of what's required to close the funding gap for critical infrastructure, a deficit estimated to range up to $570 billion. A key challenge is that municipalities are responsible for more than 60 per cent of public infrastructure assets but only collect about eight cents of every tax dollar paid in Canada. As a result, much of our infrastructure remains chronically underfunded.

Further, more than 80 per cent of the Canadian population resides in urban areas, making the vibrancy and economic potential of our cities fundamental to the country's overall prosperity. While our cities are highly livable by global standards, many lack a strong urban agenda and the revenue tools to rebuild and expand infrastructure. These challenges are accentuated by Canada's showing in the 2014 World Economic Forum global competitiveness ranking, with our infrastructure quality rank dropping to 15th and innovation performance coming in 24th.

Quality infrastructure underpins a city's appeal, which in turn attracts the capital, entrepreneurs and talent that future growth depends on. And there is a close link between infrastructure quality and innovation: innovation in how infrastructure is financed, built and delivered; and the innovation necessitated by the inherent challenges of large-scale infrastructure development, where increasing urbanization, demographic shifts, technological change and sustainability imperatives create a number of pressures.

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Infrastructure innovation

Billy Bishop Toronto City Airport, which is owned and operated by PortsToronto, is a great example of how infrastructure and innovation work in tandem and a study of how public and private sector cooperation contributes to urban renewal and new economic opportunities. Billy Bishop Airport is a unique collaboration between federal and municipal levels of government and the private sector. Toronto Island has an aviation legacy that dates back 75 years, with the current shape of the airport emerging in 2006 when private capital-backed Porter Airlines launched its business from the island with just two aircraft and one route to Ottawa. Less than 10 years later, Porter is consistently rated one of the best small airlines in the world – supporting the thesis that private capital-backed companies grow at five times the rate of traditionally-financed companies. For its part, Billy Bishop Airport is ranked as one of the best airports in North America by the Skytrax World Airport Awards. And in spring 2015, PortsToronto will open its new pedestrian tunnel underneath Lake Ontario, complementing the airport's existing ferry service and enhancing ease of access for passengers. This innovative project is the first public-private partnership (P3) in Canada to be procured without a government guarantee.

Conveniently located just minutes from downtown Toronto, Billy Bishop Airport has emerged as an essential transportation gateway that facilitates the regional, national and cross-border connectivity and integration of Toronto with other major urban centres, translating into increased movement of people and goods, and elevating the city's intellectual and commercial capacity. This new ease of connectivity generates dollars through growth in local economic activities and gross domestic product, and, accordingly, creates substantial value for the region and, by extension, the country.

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Indeed, Billy Bishop Airport, which hosted 2.4 million passengers in 2014, delivers more than $2 billion in total annual economic impact to Toronto and the surrounding region and directly and indirectly supports 6,500 high-quality jobs.

Private capital's role in infrastructure renewal

The integral role of private capital at Billy Bishop Airport was reinforced recently by Porter's sale of its passenger terminal, a state-of-the-art building it constructed in 2010, to Nieuport Aviation Infrastructure Partners, a consortium of private infrastructure equity investors. This sale attracted significant interest from Canadian and international infrastructure investors keen to participate in the only opportunity in Canada – and one of few globally – to invest in an airport.

More broadly, this widespread interest reflects growing local and international investor appetite for private infrastructure investments. Institutional investors are drawn to the infrastructure asset class for its attractive risk-return attributes, which typically include stable long-term cash flow throughout the economic cycle. According to Preqin, institutional investors' average current allocation to infrastructure has increased from 3.5 per cent of their total assets under management (AUM) in 2011 to 4.3 per cent in 2014, with the average target allocation increasing from 4.9 per cent to 5.7 per cent over this period. More than 67 per cent of investors plan to increase their allocation over the longer term, delineating infrastructure as a distinct subset of the private capital sector.

The terminal transaction also signals that there is a real opportunity for our cities and country to more effectively tap this growing, global pool of capital. Canadian institutional investors are trailblazers in private infrastructure investment, allocating on average 5.2 per cent of their AUM to infrastructure. Canada's pension plans are amongst the most successful direct infrastructure investors in the world with multi-billion-dollar, international portfolios. In the middle market, a number of Canadian infrastructure fund managers are emerging to supply capital to domestic projects and assets where smaller equity cheques are required, including partnering with municipalities. And foreign investors continue to be drawn to Canada's private capital sector generally and to infrastructure renewal initiatives specifically, reflecting both the quality and breadth of the opportunities available here as well as our stable financial, legal and regulatory environment.

Further, Canada is a leader in public-private partnerships, an innovative asset delivery model that enables governments to build higher quality infrastructure more efficiently and at a substantially lower cost to taxpayers. More than 200 infrastructure projects have been delivered through this model to date, representing more than $70 billion of capital investment. In jurisdictions such as Australia and the United Kingdom, where P3s have been in use for more than two decades, there is abundant evidence that P3s reduce the risks of infrastructure delivery while amplifying the economic benefits generated by infrastructure investments. Here in Canada, in a 10-year period P3s have generated $92.1 billion in total economic output and more than 500,000 full-time equivalent jobs, and saved taxpayers a total of nearly $10 billion in costs, according to the Canadian Council for Public-Private Partnerships.

How infrastructure fosters growth

These statistics – and the success of infrastructure assets such as Billy Bishop Airport – clearly demonstrate that the private sector plays a critically important role in improving and accelerating infrastructure and innovation, and in fostering competitiveness and quality of life. A strong base of high-quality, modern infrastructure assets is the bedrock of our economy, enabling us to attract talent and capital. Over time, these inflows lead to economic diversification, which will help the country more effectively withstand and navigate both sudden and simmering economic shifts such as the oil and gas shock currently roiling Alberta, the decline of the auto sector in Ontario or the waning forestry industry in British Columbia.

Infrastructure will continue to capture the headlines as the demand and need for investment intensifies. Doing better on both infrastructure and innovation is a defining challenge for Canada in the 21st century, and rising to it requires a real and lasting partnership between the public and private sectors to deliver the physical structures and services we depend on, and to reap the significant social benefits of infrastructure investment: more vibrant communities, reduced income inequality, and greater opportunities for all. The ability of our cities and future generations to thrive and take flight depends on it. ■

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