Blurred lines: Shaping the smart real asset sector of the future

James Muir explores the increasing convergence of property and infrastructure investment under the 'real assets' umbrella

While real estate and infrastructure have co-existed under the umbrella of 'real assets' for some time, the adoption of this term has grown significantly of late. Back in 2021, we witnessed the first signs of convergence between the two asset classes when PATRIZIA acquired Whitehelm Capital, while Nuveen and Schroders also made moves into infrastructure. Fast forward three years and we are seeing a renaissance of the trend, with BlackRock's proposed acquisition of Global Infrastructure Partners the clearest sign yet of this strategic shift among General Partners (GPs).

On the one hand, this mergers and acquisitions (M&A) activity is no surprise. While real estate is regarded as a larger and more mature market than infrastructure, there are strong synergies between the two. Resilient income with inflation protection, close alignment with the long-term megatrends and the ability to drive value from a physical asset are just three shared characteristics, all of which are highly complementary in a holistic real assets strategy.

With this in mind, it is no surprise to see managers coalescing under the real assets umbrella to leverage these synergies and create long-term value for clients. For GPs, a combined investment platform undoubtedly strengthens portfolio diversification and lowers risk, which is invaluable in these volatile times. Real estate is notoriously cyclical and last year represented arguably the nadir of the current cycle, while liquidity in infrastructure remained much more resilient.

But when we talk about the convergence between real estate and infrastructure, we believe it goes beyond an M&A trend. It is far more embedded than simply two similar investment options being offered by the same GP. Instead, we are witnessing a fundamental evolution in what it means to be an investor in real assets, with managers becoming much smarter in leveraging the two asset classes to offer innovative investment solutions for their clients. And the smartest GPs are the ones unlocking these solutions at both the asset and fund level, creating a smart real asset sector of the future.

Leveraging an integrated real assets platform

With a fully integrated real assets platform, the opportunities to drive value creation and tap into long-term growth are enormous. For GPs it's about harmonising the real estate and infrastructure value chains in order to generate value at every stage of the investment lifecycle. While for Limited Partners (LPs) it's about accessing new avenues for allocating capital that focuses on innovative assets and products underpinned by the major transition megatrends of our time: Digitalisation, urbanisation, the energy transition and modern living. So where do we see the smartest managers actively driving these synergies?

On an asset level, infrastructure is both a value-driver and decarbonisation strategy for real estate portfolios, helping the sector on its journey to net zero. While photovoltaic (PV) panels have been applied to real estate for decades, the successful installation and management of large-scale solar farms on the roof space of major logistics hubs requires specialist knowledge and asset management expertise.

In the Netherlands, one of the country's largest single logistics assets – the Maasvlakte distribution centre – is home to one of Europe's biggest rooftop solar installations. The 120,000 sq.m. PV system generates a capacity of 25 Megawatt peak (MWp) a year of clean energy, which is enough to meet the annual energy needs of approximately 8,000 households. This smart combination of real estate and infrastructure not only facilitates an industrial-scale renewables project, but it also delivers significant upside potential for the underlying asset, which now makes a meaningful contribution to the energy transition.

A similar story can be seen in the electric vehicle (EV) space where charging infrastructure has been installed in car parks and at roadsides since the dawn of EVs. In isolation these assets are relatively simple to manage, but rolling out a pipeline of ultrafast EV chargers across a portfolio of prime food-anchored retail stores requires a much broader skillset.

To give an example, in Germany our real estate heritage is playing an important role in our investment in the delivery of 400 ultrafast Numbat EV charging stations across a portfolio of Tegut supermarkets across the country. With a 40-year track-record managing complex asset management projects, we are well equipped with the knowledge and know-how to add value to such a programme. To drive further synergies, we are exploring installing solar panels on the roofs of the stores, with the energy generated fed back into the batteries in the EV charging stations. By bringing the two asset classes together in an intelligent way, we are enhancing the value of our investments in a much more holistic manner.

A shift to thematic investing

With this blending of assets comes the obvious question of where these investments sit at a fund level. For us, the answer is about taking a more thematic approach to investment strategies that complement and augment single sector funds. We believe the benefits of this hybrid approach are clear: We can create a more diverse product mix that addresses the challenges of the long-term transition megatrends, while clients have access to a broader platform of attractive investment solutions.

A great example is an investment strategy based around the theme of 'smart cities.' While its core proposition is investing in digital infrastructure like fibre networks to help communities become better connected, it could also invest in tech-enabled real estate like smart buildings that plug into this underlying digital infrastructure. A thematic strategy like smart cities generates real value by leveraging a GP's footprint and expertise across multiple real asset disciplines, such as sustainability, technology and real estate. So when successfully combined, you have a product that plays a leading role in driving the major transitions to digitalise and decarbonise our expanding urban communities.

However, a thematic approach like this doesn't comes without its challenges. One fundamental hurdle to overcome is around how LPs are structured, with individual real estate and infrastructure teams commanding separate allocations. Without a clearly defined core offering of either infrastructure or real estate, a blended strategy risks finding itself without capital from either pot. But merging LP teams to have one real assets allocation would certainly support thematic investing and the early movers in this space, such as AustralianSuper, are the ones who stand to benefit the most.

But change won't happen overnight, so GPs must do more to clearly articulate how thematic strategies can work for LPs to encourage this merger. There will always be assets that sit in a grey area like data centres, but from our perspective what should matter most for clients is that they like an investment's risk profile, its long-term cash flow and its position within their wider real assets portfolio. It's then our job as a manager to explain how it supports a holistic strategy.

In some cases, regulatory change would be advantageous and this is already underway for retail investors with the increased popularity of European Long-Term Investment Funds (ELTIFs). Reforms were agreed in 2023 that would allow a broader definition of real assets as well as relaxed rules for the ELTIF's holding of those assets amongst other changes. Similarly, the federal government in Germany is expected to be close to introducing new regulations that would allow infrastructure to be incorporated into real estate funds to a maximum share of 15 per cent of the fund's total.

But ultimately, the market will always move to where the demand is. We live in a world in transition where both infrastructure and real estate are absolutely fundamental in shaping the way we live in the future – so we firmly believe the most attractive investment solutions over the coming decades will combine the two. And it will be the managers who can best leverage the synergies at both the asset and fund level who will be in pole position for driving the smart real asset sector of the future.

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