

Infrastructure – to build or not to build?

Governments around the world are throwing money into roads, schools, bridges and any other form of building that could help resurrect the global economy. Nick Raynor, Investment Adviser looks at the benefits of doing this and which companies could benefit from this generous offering.

The OECD (Organisation for Economic Co-operation and Development) recently estimated that around \$40 trillion would need to be spent to deliver vital infrastructure projects including life-critical projects (energy, water and transport) by 2030. To date, the amount of money that governments have announced they are prepared to throw at these projects only just scratches the surface. But it's no longer just our infrastructure that's at threat; there are also hundreds of thousands of jobs at stake in this sector and without government intervention a great number of these—and other jobs which could benefit from this spending—could be at risk. That's why governments across the world now see infrastructure spending as a way of improving the economy as well as improving our world.

So what is being done?

Well, £13 billion of public sector spending on infrastructure and public buildings has been brought forward by the UK Government. And the money that is being made available isn't just going to the construction companies; it's also flowing through into many other areas. So it's not just the contractors that benefit but also several other sectors including the engineering, support, IT and other business infrastructure companies that help complete the contracts.

Government supported projects include the £16 billion (current estimated cost) Cross Rail project which will see 118km of track run from Maidenhead and Heathrow through two 21km tunnels under central London. This line is expected to bring an additional 1.5 million commuters to within a 60 minute travelling distance from London's key business districts. Construction starts in 2010 and the construction partners are expected to be announced at the end of April 09.

In the US, President Obama has already set aside \$27.5 billion for highway construction, and \$20 billion for air, rail and public transportation with the intention of providing a quick stimulus to the US economy. In Italy, nearly €18 billion has been made available for infrastructure projects including the high-profile Messina Bridge project that will link the Italian mainland to the island of Sicily. France has also recently announced that €18 billion will be made available for infrastructure projects.

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However there are areas of the world where we are starting to see a slowdown in building projects. For example in the Middle East—where there has been a tremendous amount of growth in the past 5 years—spending has started to dwindle.

So which companies will benefit from this new cash bonanza?

We look at some companies which we feel are best placed to profit:

Balfour Beatty could benefit from both the US and the UK stimulus packages. Recent profits rose to £249 million and the company had an order book at the year

end of nearly £13 billion along with £200 million of cash. Almost a quarter of its revenues is now derived from the US; recent deals collectively worth \$480 million include the building of a jail and property for the US Navy.

The London Olympics has also proved a successful hunting ground for Balfour; contracts won so far include the Aquatics Centre and Team Stadium. The contract for the Aquatics Centre includes the construction of a huge land bridge that will be the main gateway into the Olympic Park; the budgets for the Centre and the land bridge are £242m and £61m respectively. We feel there are more contracts to come from the Olympic project and Balfour is well placed to compete for them.

Balfour was recently admitted into the FTSE 100 which reflects the company's current strength and potential. It could be attractive to investors looking for a reasonable yield.

Carillion also operates in multiple international markets. Currently it employs 50,000 people across the UK, the Middle East, Canada and in the Caribbean. Because of its geographical diversity, Carillion can cope with the downturn that is being currently experienced in Dubai as was recently confirmed when its Middle East operations won contracts from Abu Dhabi.

Like Balfour, Carillion has already won a contract for the 2012 Olympics; it won a £350 million contract for the Media Centre in August of last year and is well placed for further Olympic contracts.

Recent results showed pre-tax profits gaining 55% to £157.5 million as revenue increased to £6.2 billion. If Carillion can keep growing at this rate it may not be long until they also take their place in the FTSE 100.

Babcock International is also worth a closer look. It has strong ties with the UK Government through defence contracts and also has a large exposure to Network Rail. **Costain** is one of the smaller companies within this sector but we regard it as a higher risk company after the shares ran into trouble several years ago. Since then, Costain has re-modelled itself and come through harder times to now have a war-chest of £350 million for acquisitions and an order book worth over £2 billion.

The awarding of infrastructure contracts will also benefit related sectors. This could include consultancy firms such as WSP or Atkins WS. Of the two, **Atkins WS** would be our preferred play as its shares have

been very weak lately. There has been a notable reduction in its Middle East business, but this could change with the new money being made available by governments worldwide. The company has been restructured over the last six months; it expects this to affect revenue rather than profitability.

Equipment hire firms such as Speedy Hire and Ashtead could also benefit where contractors prefer to hire rather than purchase expensive plant equipment. Of the two, **Ashtead** could be the more attractive as they have greater exposure in the US.

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economies of the spending countries and safeguard jobs should prove successful. And it brings a bonus: improved future living standards. But it also begs a question. How long can global governments continue these expensive plans and proposals if the real objective is not met and economies continue to struggle?

Find out more

For more information on infrastructure-based investments contact our Advice team on 01296 41 43 45.

