



GCP Infrastructure

Investment companies | Update | 17 August 2023

Merger to unlock compelling value?

GCP Infrastructure Investments (GCP) has announced a potential three-way merger between it, GCP Asset Backed Income (GABI), and RM Infrastructure Income (RMII). As we explore in this note, the adviser believes that this has the potential to address some of the issues that may have given rise to GCP's discount.

Following a period of NAV growth through 2022, GCP's half-yearly report for the six months ending 31 March 2023 and the recently published end-June NAV showed what looks like a period of consolidation for the fund, as falling energy prices and higher discount rates seem to have weighed on returns. GCP has moved to trade on a 34.3% discount and a 9.8% yield. Despite this, GCP's assets have continued to grow, and the adviser believes the outlook for investors remains as promising as ever thanks to a broad range of thematic tailwinds.

Public-sector-backed, long-term cashflows from loans used to fund UK infrastructure

GCP aims to provide shareholders with regular, sustained, long-term distributions and to preserve capital over the long term by generating exposure primarily to UK infrastructure debt and related and/or similar assets that provide regular and predictable long-term cashflows.

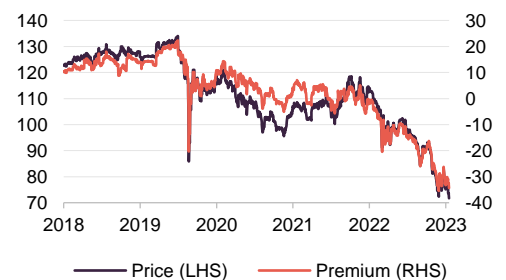
12 months ended	Share price TR (%)	NAV total return (%)	Earnings per share (pence)	Adjusted ¹ EPS (pence)	Dividend per share (pence)
30/09/2019	8.0	6.3	6.74	8.06	7.6
30/09/2020	(2.0)	(0.2)	(0.08)	7.33	7.6
30/09/2021	(7.9)	7.2	7.08	6.95	7.0
30/09/2022	(3.8)	15.8	15.88	7.11	7.0
30/09/2023					7.0

Source: Morningstar, Marten & Co. Note 1) Marten & Co's adjusted earnings per share removes the impact of unrealised movements in fair value through profit and loss. The board and the investment adviser use other alternative performance measures.

Sector	Infrastructure
Ticker	GCP LN
Base currency	GBP
Price	71.7p
NAV1	109.7p
Premium/(discount)	(34.3%)
Yield2	9.8%

Share price and premium

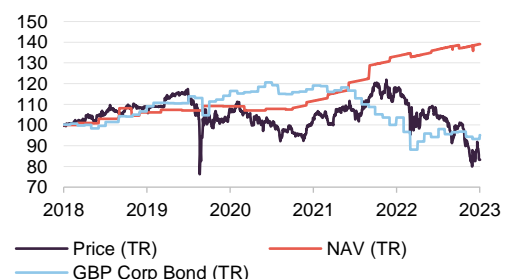
Time period 31/07/2018 to 15/08/2023



Source: Morningstar, Marten & Co

Performance over five years

Time period 31/07/2018 to 31/07/2023



Source: Morningstar, Marten & Co

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Domicile	Jersey
Inception date	22 July 2010
Investment adviser	Philip Kent
Market cap	628.4m
Shares outstanding	876.5m
Daily vol. (1-yr. avg.)	1.4m shares
Net gearing (end March 2023)	13%

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Potential three-way merger

On 11 August 2023, GCP and GABI announced that the boards of the two funds had agreed terms for a merger. Under the proposals, this would be achieved via a solvent winding-up of GABI and the transfer of its assets to GCP in exchange for the issue of new ordinary shares in GCP. The number of shares issued would be determined on a formula asset value (FAV) basis. FAVs are calculated based on the NAV of each company on an agreed calculation date, less each party's transaction costs (the adviser proposes contributing £1m towards these).

The merger would create a larger, more liquid, and efficient fund

The adviser believes that the merger would create a larger, more liquid, and efficient fund, benefitting the shareholders of both companies.

Accordingly, the announcement highlights that the focus of the enlarged vehicle in the two-year period following completion would be to reduce the combined company's existing leverage from about £150m to about £50m and to return £100m of capital to shareholders in lieu of a cash exit offer. That would absorb about £200m of the company's cash resources, cash which would flow from natural loan maturities and prepayments.

The merger would mean that the enlarged GCP would have a shorter weighted average loan life due to the considerably lower duration of GABI's portfolio. Consequently, the adviser suggests, it would be more agile and able to re-invest in accordance with the revised investment policy (discussed on page 22) at prevailing market rates (which are higher now than at any point during the life of GCP), at the same risk level, more quickly than it could prior to the proposals.

A larger fund may be less subject to selling pressure from wealth managers

It also believes that the increased liquidity of the fund, which would have a NAV of around £1.35bn, could also reduce some of the short-term selling pressure on the company's shares from larger wealth managers who, as a result of their own mergers, are acting as though they are increasingly obsessed with liquidity.

In addition to its shorter duration, the GABI portfolio is invested in a range of different asset classes outside of the immediate remit of GCP, particularly asset finance, which makes up 12% of the fund, and property, which makes up 46%. Under the revised investment policy, some of these property assets will become a permitted exposure within GCP's core portfolio.

GABI also has some problem loans that it has identified, however the adviser is comforted that both sides will revalue their portfolios ahead of the merger and any necessary impairment to valuations should be reflected in FAVs.

£0.8m of annual cost savings identified

On completion of the merger, company costs would be spread across a larger asset base, resulting in a lower ongoing expense ratio, with cost savings projected to be about £0.8m per annum. In addition, GCP would adopt a new tiered fee structure, which we outline on page 23.

RM Infrastructure Income

In addition to the GABI merger, GCP's board has also announced that it is in separate discussions with the board of RMII with the intention of agreeing a potential merger of the enlarged GCP with RMII. A further update for these developments will be provided when more information is available.

One attraction of a combination with RMII, according to the announcement, is that the RMII portfolio also has a much shorter duration than GCP's, permitting an acceleration of the portfolio re-shaping/capital returns discussed above. Given the costs identified, it would be cheaper all round if the RMII and GABI mergers could be done simultaneously.

Recent figures

Half-yearly results to 31 March 2023

Total income for the period was £35.6m

Over the six-month period ended 31 March 2023, GCP's NAV per share fell from 112.80p to 112.24p, a drop of 0.5% while shares fell from 97.8p, to 85.2p, a drop of 12.9%. Total NAV return was 2.7% while shareholder total return was -9.7%.

Dividends continued to run at an annualised pace of 7.0p per share, so that GCP is trading at a weighted average annualised yield of 9.8%. On an adjusted earnings basis, dividend cover was 1.1 times, a slight improvement from the last interim report.

Operationally, the company has continued to grow earnings, as elevated energy prices boosted the performance of GCP's renewable investments; particularly those able to fix higher prices under power purchase agreements. Total income for the period was £35.6m, and whilst this is well down on the previous year's £117.6m, the comparative period last year included material positive revaluations resulting from significantly increased electricity price forecasts. In addition, income for the fund remains well ahead of pre-pandemic returns.

As shown in Figure 1, inflation was the leading positive contributor to GCP's NAV during the six months to March 2023, due to higher inflation actuals and a higher OBR medium-term inflation forecast. An increase in the valuation of a biomass asset was the second-largest contributor, arising from higher electricity prices along with the implementation of cost efficiencies.

Figure 1: Positive factors affecting HY23 performance

	Impact (£m)	Impact (pence)
Inflation	5.8	0.66
Biomass valuation	3.1	0.35
Other upward movements	1.5	0.17
Total	10.4	1.18

Source: GCP Infrastructure Investments

On the downside, the largest detractors were the electricity generation levy, and valuation adjustments reflecting continued uncertainty in the social housing sector. Electricity price hedging arrangements had a significant impact on overall returns, offsetting £11.9m worth of negative valuation movements. In total, these valuation shifts resulted in a net fall of just £5.5m, which the manager highlights as commendable in light of the current macro volatility.

Figure 2: Negative factors affecting HY23 performance

	Impact (£m)	Impact (pence)
Actual performance	(2.1)	(0.24)
Discount rates	(2.4)	(0.27)
Tax	(1.2)	(0.14)
Electricity Generator Levy	(8.2)	(0.93)
Electricity prices	(4.7)	(0.53)
Social housing valuation	(5.2)	(0.59)
Other downward movements	(2.0)	(0.23)
Total	(25.8)	(2.93)

Source: GCP Infrastructure Investments

Q2 2023 NAV update

GCP provided a second-quarter update for the period ended 30 June 2023, which highlighted a further 2% fall in NAV. The update showed that the primary driver of this movement was the increase in discount rates, which was applied across the portfolio's three sectors: supported living, PFI, and renewable energy. The adviser noted that the increased discount rates reflect the current higher inflation and base rate environment, and recent market transactions that suggest the rising cost of debt has started to impact equity pricing. It said that this has resulted in a c.40bps increase to the weighted average discount rate used by the company to value its portfolio, leading to a decrease of c.2.5 pence per ordinary share.

The adviser also noted that further reductions in electricity prices also weighed on actual and forecast cash distributions to the company from its renewables investment portfolio, driven by decreases in short-term power prices. It said that this was partially offset by an uplift in long-term forecast power prices and continued execution of the company's hedging arrangements. In aggregate, movements in electricity price forecasts negatively contributed c.0.4 pence per ordinary share.

Operational performance drives long-term upside

The adviser believes that GCP's focus on lending to assets/projects with predictable, Government-backed cashflows has worked in its favour over the 13 years since launch and that GCP's ability to preserve capital value is highlighted by aggregate annualised downward revaluations of just 0.31% over this period. That is much lower than the annualised default rate on sterling corporate loans, and it believes that this should give investors comfort as they navigate what continues to be a difficult period for the UK economy.

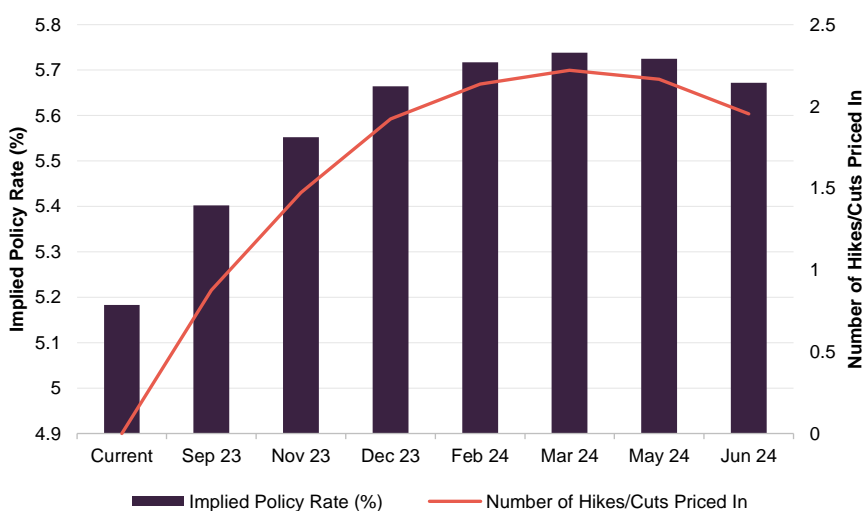
Whilst not reflected in the share price, the adviser believes that operationally, the fund has also continued to execute at a high level, with profit over the most recent financial year more than tripling from its pre-pandemic peak. Energy price volatility has been a leading contributor, and this appears to have been accelerated by the

GCP's ability to preserve capital value is highlighted by aggregate annualised downward revaluations of just 0.31% since launch

unfortunate events taking place in Ukraine, among other things; however, it believes, that the returns vindicate a long-term allocation to the renewable energy transition, which was identified by manager Phil Kent as one of the best opportunities to provide secular upside for the fund.

It goes on to say that the ability for GCP to generate sustainable cashflows from its existing asset base becomes particularly relevant at the market's current juncture, given the possibility of a structural reset in interest rates. With short-term Government debt now yielding roughly the same as infrastructure sector averages, it believes there is reduced incentive to invest solely in alternative income and the fall in risk premiums over the last 12-18 months explains much of the recent capital flight out of the sector.

Figure 3: Implied overnight rate & number of cuts



Source: Bloomberg

Whilst it thinks that this has the potential to create challenges in the short term, interest rates are expected to fall over the next 12 to 18 months, as highlighted in Figure 3, and widening discounts may offer investors attractive entry points for funds such as GCP that are able to maintain long-term structural cashflows and grow NAV through consistent operational improvement.

Market backdrop

Renewable energy infrastructure remains the main focus of the fund as investment adviser Philip Kent continues to see a disconnect between the Government's stated aims for infrastructure investment, in particular around the decarbonisation of the economy in order to meet the legally binding net zero targets, and the investment required to deliver these goals.

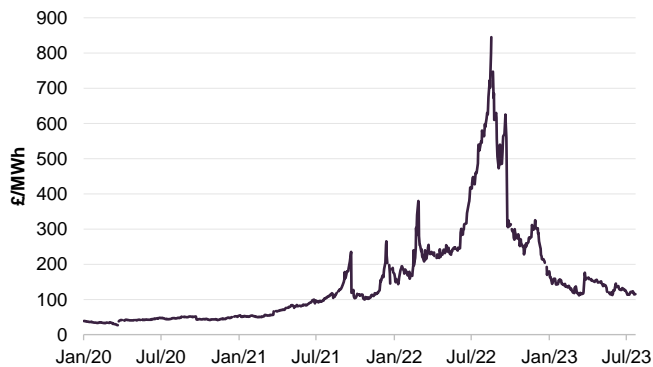
According to the Independent Committee for Climate Change, the investment required to achieve net zero is significantly greater than the actual private and public sector investment made or planned to date. Phil believes that this will create opportunities for the company to support the development of new infrastructure. In

addition, he believes there is an increased emphasis being placed on energy security which should ensure a continuation of policy support for renewable assets.

GCP's portfolio is largely focused on availability or contracted revenues so, as the adviser notes, the performance and valuation of the portfolio is not directly correlated to economic activity. That being said, the investment adviser has outlined a variety of prevailing macro factors that are influencing the outlook for the wider renewable energy sector; a mixture of both positive and negative factors which may offer greater upside potential, but also heightened volatility.

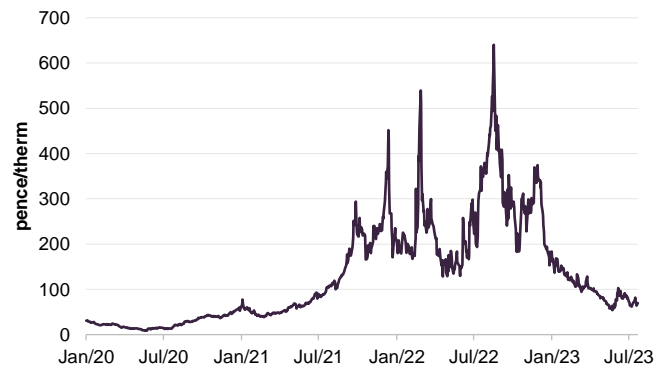
Power prices

Figure 4: UK baseload power prices



Source: Bloomberg

Figure 5: UK gas prices



Source: Bloomberg

As shown in figure 4 and 5, the last few years have been a volatile period for energy prices which the adviser notes have been impacted by a raft of factors in addition to the pandemic slow down and Ukrainian invasion, including below-average production from wind and hydro resources, and reduced output from the French nuclear fleet. It appears that volatility has begun to recede over the last few months; however, the manager claims that with the issues facing global energy production, markets appear to have priced a structural increase in long-term prices going forward. As the adviser has noted, GCP has been positively impacted by higher electricity prices, particularly relating to the net cash flows expected from renewable energy assets. However, it does point out that there do remain risks, particularly regarding the volatility of these prices and the potential impacts of energy switching towards other sources, including LNG. The investment adviser notes that they have successfully managed these risks through various hedging programmes over the last few years, as highlighted on page 4, and continue to review opportunities to hedge electricity market prices to both lock in attractive price levels relative to the original investment forecasts, and mitigate volatility in NAV.

The sensitivity of GCP's NAV to power prices is shown in Figure 18 on page 16. Phil notes that forecasts of power prices two and three years out appear to be rising.

47% of GCP's portfolio had some inflation linkage in returns

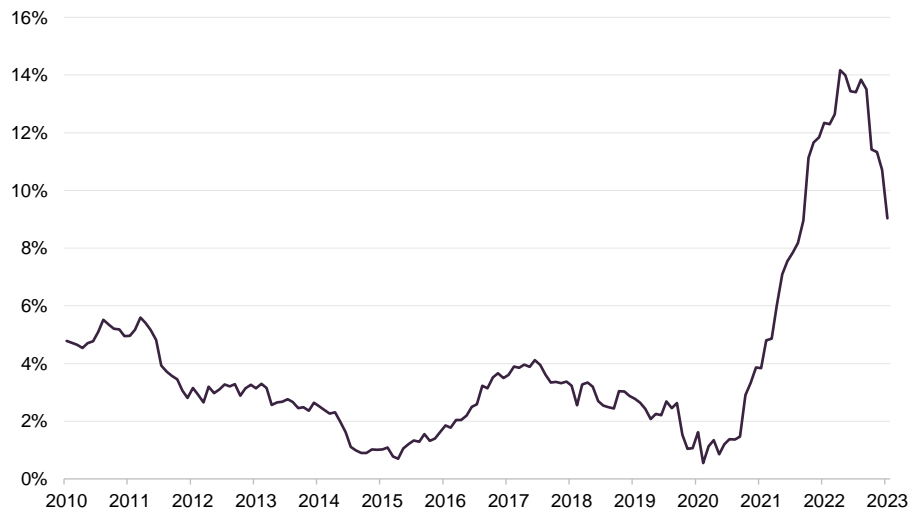
Inflation

As the adviser has pointed out, broadly speaking, higher inflation is a positive for GCP, bearing in mind that at end March 2023, c.47% of its portfolio had some inflation linkage. It highlights that the fund offers investors a way to purchase an inflation-linked, fixed-income strategy without purchasing conventional inflation-linked bonds, generally offer lower returns. This inflation linkage is structured as a direct link between the return and realised inflation (relevant to the supported living assets and certain renewables) and/or a principal indexation mechanism that increases the principal value of the company's loans outstanding by a share of realised inflation over a pre-determined strike level (typically 2.75% to 3.00%).

For those assets exposed to inflation, the adviser points out that the current market environment does have some negative impacts, particularly related to input costs, which have risen considerably for the company's anaerobic digestion investments. Inflation also appears to be affecting capex costs and this needs to be factored into GCP's assessment of the profitability of potential new investments.

Figure 19 on page 16 summarises the change in interest accruals and potential NAV impact that would be associated with a movement in inflation.

Figure 6: UK inflation – RPI



Source: ONS

UK Government policy

As shown in Figure 2 on page 5, the Government's energy profits levy had a tangible effect on GCP's profitability. The levy, which was discussed in detail in our most recent note and came into effect on 1 January 2023, runs until 31 March 2028. It requires all non-fossil fuel generators generating electricity from nuclear, renewable, biomass, and energy from waste sources to pay a tax of 45% of their excess revenue from sales of power generated in the UK above a level of £75/MWh from 2023 to April 2024, and thereafter adjusted each year in line with the change in inflation (as measured by CPI) on a calendar-year basis.

Following the announcement of the level in November 2022, the investment adviser estimated the expected valuation impact on its 30 September 2022 NAV would be 1.50 pence per share. In December 2022, when the full details of the levy were announced, the actual impact of the tax was applied to the valuation of the portfolio. This impacted the NAV by 0.93 pence per share at 31 December 2022. The difference in the estimated and actual impact arose from the manner of the application of the levy to groups, demonstrating that the assumptions used were broadly accurate.

Even with the effects of the levy, the adviser notes that broader economic trends and higher energy prices are still a net benefit for GCP and it believes these will likely provide a long-term tailwind. It also notes that the fund will be able to leverage both the public and private investment necessary to meet the UK's current legally binding climate goals. The UK Government's 2023 Green Finance Strategy outlines a framework for its transition to a low-carbon economy, and estimates that £50–£60bn of capital each year will be required to deliver these goals.

The adviser highlighted that the fund has already benefitted from one of its portfolio businesses being awarded a grant under the Net Zero Hydrogen Fund, which was set up to support the development and construction of low-carbon hydrogen plants. It says that the grant will benefit a wind farm located in Northern Ireland. A feasibility study has been undertaken in partnership with a local cement manufacturer presenting the potential to generate additional revenue alongside a life extension for the wind farm, and also to help decarbonise an intensive manufacturing process by producing low-carbon cement. If the study is successful, it is likely to both improve the returns on an existing investment and provide further attractive investment opportunities.

Other assets

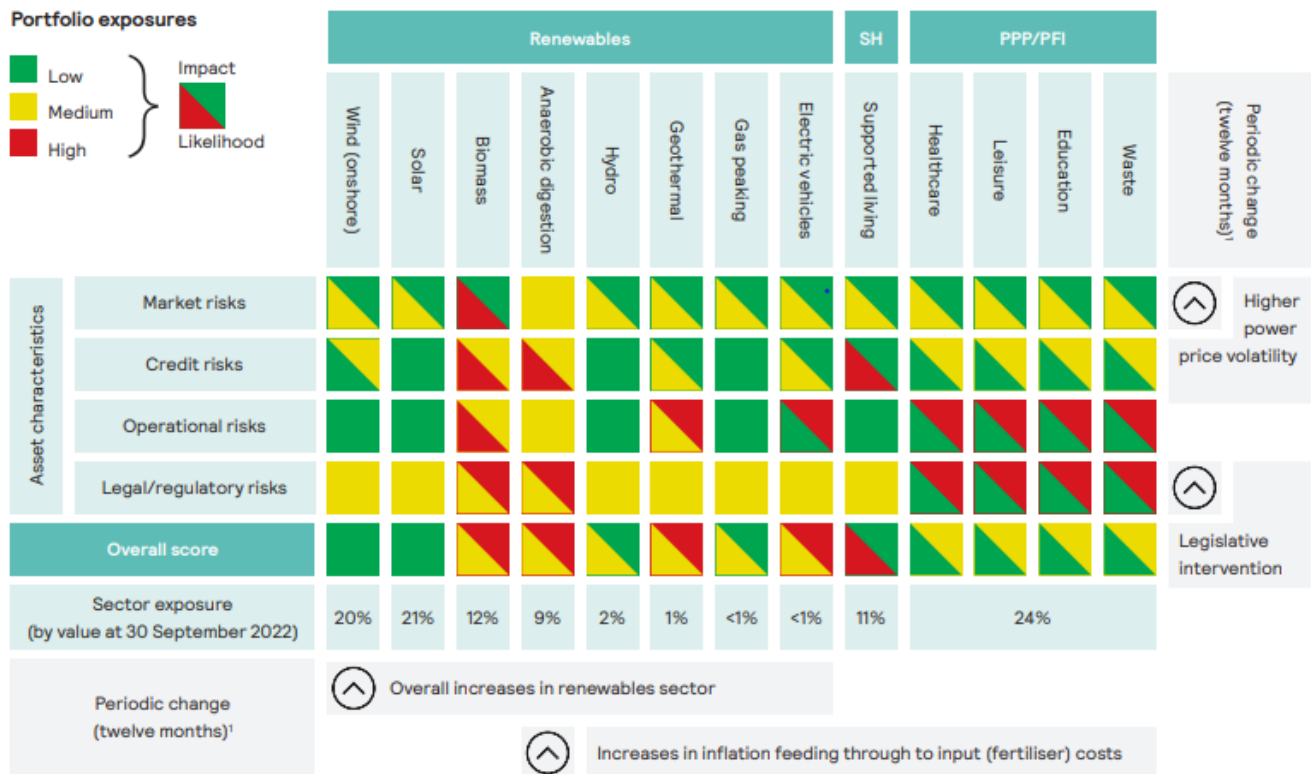
In addition to its renewable energy exposure, GCP's portfolio also includes around £260m worth of PPI/PFI investments, accounting for roughly 23% of AUM. However, the adviser has pointed out that the departure by the UK Government and the devolved governments from PPP models has all but ended primary investment opportunities in this area. It has continued to review secondary opportunities when presented, but notes that they are typically small in scale and subject to competitive bidding processes. However, it does state that further possibilities do exist for alternative funding models, including licence-based models such as the regulated asset base approach when applied to particular projects, or offshore or onshore transmission licensing frameworks.

Around 11% of the portfolio is currently invested in supported living, although the advisers has noted that GCP stopped making new investments into the sector in 2018 as an increasing number of investors put pressure on potential returns while adding to the associated risks. Since then, GCP has actively reduced its exposure to the sector.

Risk analysis

Each year in the company's annual report, GCP's investment advisor, Gravis Capital releases a risk matrix which highlights its perception of risks across the various asset classes that GCP invests in. This is shown in Figure 7.

Figure 7: Portfolio risk summary as at 31 March 2023



Source: GCP Infrastructure Investments

In GCP's annual report from September 2022, Gravis noted that there has been an increase in risk across all four asset characteristics from the previous year. According to the report, the major contributors to this were:

- the UK Government's announcement of a levy on the profits made by electricity generators, which we described earlier in this note. This has clearly increased the legal and regulatory risk for any strategy exposed to UK electricity generators;
- volatility increasing in parallel, despite the higher wholesale prices for electricity. This has led to greater uncertainty to the long-term outlook for the UK power prices, as well as the overall market structure going forward;
- anaerobic digestion projects having been hit by higher input costs – particularly fertiliser – which has hit profitability;
- the collapse of a number of electricity suppliers that acted as off-takers for renewable projects, due to the costs associated with hedging their energy prices. Fortunately, GCP has no direct exposure to any impacted supplier; and

- the wider renewable energy sector having also been hit by the global supply chain issues, with there being less availability of replacement parts. However, this has yet to materially impact output levels.

The company also provides a semi-annual risk assessment and a review of the principal risks and uncertainties in its interim report, which relates to the period ended 31 March 2023. The adviser notes that in addition to the existing principal risks and uncertainties discussed above, which it expects to remain relevant to the company for the next six months, the updated review now considers the share price discount to NAV to be a new principal risk.

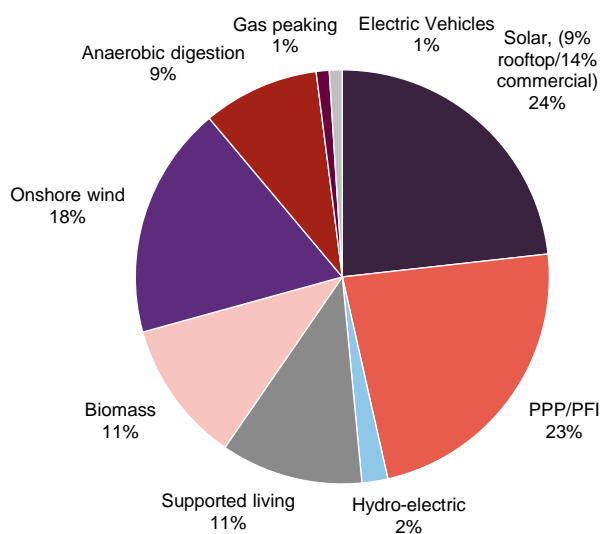
The interim risk review also noted several other changes over the period.

- The investment due diligence risk has increased due to rising uncertainty around interest rates and inflation.
- Risks associated with the availability of suitable investments and reinvestment have decreased thanks to the company's active pipeline and investment activity made during the period totalling £75.1m.
- Risks relating to the performance of – and reliance on – subcontractors have increased due to ongoing inflationary pressures and supply chain disruption.

Asset allocation

At 31 March 2023, there were 49 investments in GCP's portfolio. There has been one new investment made since we published our last note, which was a new senior loan of £7.5m to finance the purchase of a fleet of 150 electric taxis. This is discussed in more detail on page 13. The average annualised portfolio yield at 31 March 2023 was 7.9%, and the portfolio had a weighted average life of 10 years.

Figure 8: Split of the portfolio at 31 March 2023

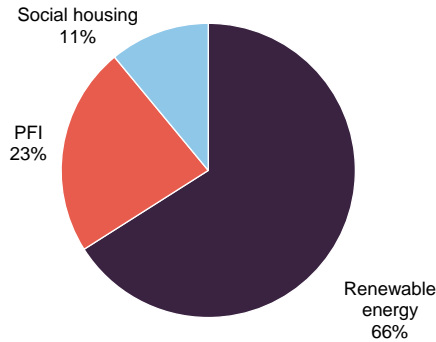


Source: GCP Infrastructure Investments

At 31 March 2023, only 1% of the portfolio was exposed to assets in their construction phase. The adviser notes that, historically, having some exposure to

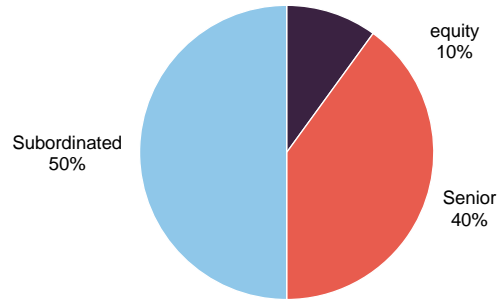
these projects has allowed GCP to capture higher returns; however, limiting this has significantly de-risked the portfolio, factoring in the impact of inflation on financing costs, raw materials, and supply chains.

Figure 9: Sector allocation at 31 March 2023



Source: GCP Infrastructure Investments

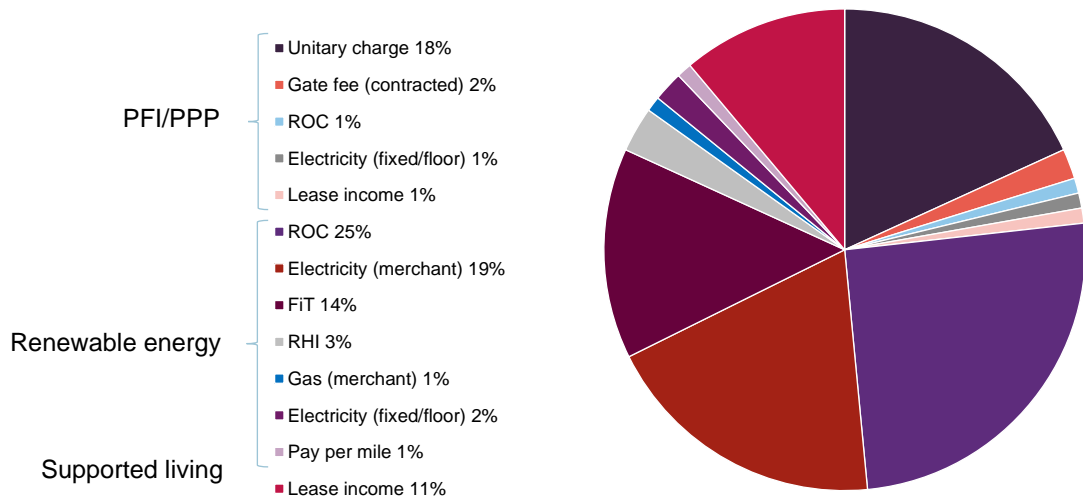
Figure 10: Security allocation at 31 March 2023



Source: GCP Infrastructure Investments

Figure 11 looks at GCP's sources of income. Renewable energy exposure accounted for 66% of income at 31 March 2023. Roughly 47% of loans by value benefit from inflation protection.

Figure 11: GCP sources of income as at 31 March 2023



Source: GCP Infrastructure Investments

Top 10 investments

Changes in GCP's top 10 largest investments since our last note have been minor, with GCP Green Energy 1 replacing GCP Solar 2 in the list.

Figure 12: GCP's 10-largest investments as at 31 March 2023

	% of total assets 31/03/23	Cashflow type	Project type
Cardale PFI	11.1	Unitary charge	PFI/PPP
Gravis Solar 1	9.2	ROC/FIT	Commercial solar
GCP Bridge Holdings	5.4	ROC/FIT/Lease/PPA	Various
Gravis Asset Holdings I	4.7	ROC/PPA	Renewables – onshore wind
Gravis Asset Holdings H	4.2	ROC/PPA	Renewables – onshore wind
GCP Programme Funding S3	4.0	ROC/RHI	Anaerobic Digestion
GCP Programme Funding S8	3.8	ROC/PPA	Biomass
GCP Biomass 2	3.7	ROC/PPA	Biomass
GCP Programme Funding S10	3.6	Lease	Supported Living
GCP Green Energy 1	3.3	ROC/PPA	Commercial solar/onshore wind

Source: GCP Infrastructure Investment

Figure 13: Top 10 revenue counterparties

Firm	% of total portfolio
Viridian Energy Supply	9
Statkraft Markets GmbH	9
Ecotricity Limited	8
Power Ni Energy Limited	7
Office of Gas and Electricity Markets	5
Smartestenergy Limited	5
Neas Energy Ltd	4
Ceres Energy Ltd	4
Good Energy Limited	4
Gloucestershire County Council	4

Source: GCP Infrastructure Investments

Figure 14: Top 10 project service providers

Firm	% of total portfolio
PSH Operations Limited	13
Vestas Celtic Wind Technology Limited	12
Solar Maintenance Services Limited	10
A Shade Greener Maintenance	8
Burmeister and Wain Scandinavian Contractor AS	8
Engie FM Limited	5
Atlantic Biogas Ltd	4
Urbaser Limited	4
Agrikomp (UK) Limited	3
Robertson Facilities Management	3

Source: GCP Infrastructure Investments

Recent investment activity

During the six-month period ended 31 March 2023, the company made seven advances totalling £75.1m: £7.5m under one new facility and £67.6m under existing facilities, increasing the number of investments to 49.

These transactions include an advanced £46.4m repayment of third-party senior debt secured against a portfolio of commercial solar projects and a portfolio of

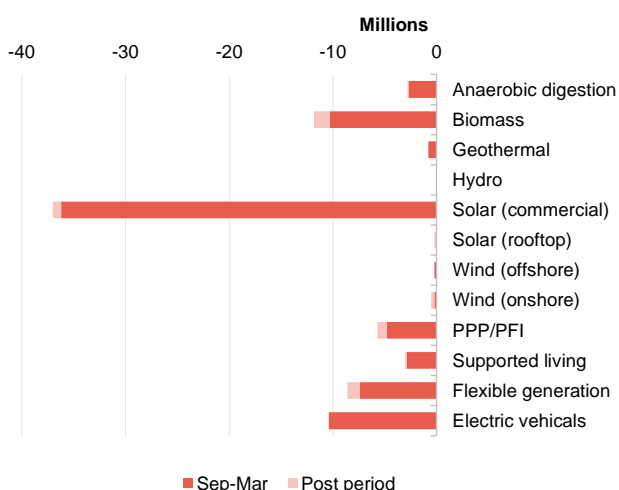
renewable and PPP assets. The company also advanced £7.4m against gas peaking plants being brought into operation by a borrower and a further £1.0m to support the ongoing development and optimisation of three anaerobic digestion plants in the period to December 2022.

Two investments totalling £10.5m were made in the electric vehicle sector in February 2023. This included a new senior loan of £7.5m to finance the purchase of a fleet of 150 electric taxis and a follow-on investment of £3.0m to grow an existing fleet. The new borrower benefitted from Government grants to reduce the effective loan to value ratio against the vehicles.

The company received 24 repayments totalling £25.0m; all of which were scheduled repayments.

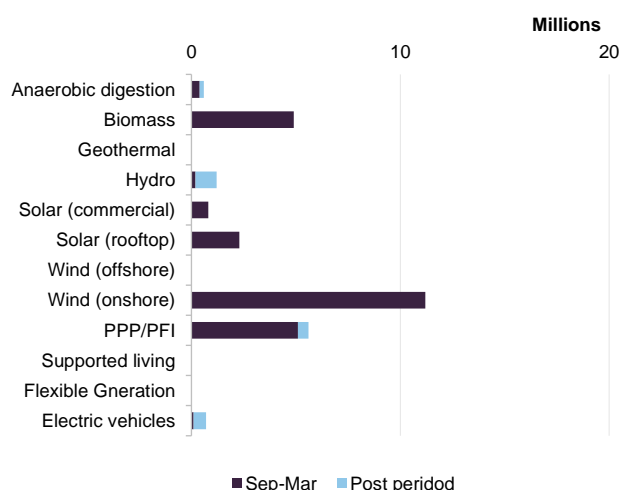
Figures 15 and 16 show the full breakdown of GCP's recent investment activity up until 31 March 2023 in addition to further advances of £2.1m and received repayments of £2.3m which were made post period end.

Figure 15: Outflows (investments)



Source: Gravis Capital Partners

Figure 16: Inflows (repayments)



Source: Gravis Capital Partners

Pipeline of potential new investments

Allowing for the investments discussed above, GCP has an active pipeline of at least £400m, which we discussed in detail in our last note. Almost half of this concerns the opportunity to finance the construction of a portfolio of c.400MW of batteries in the UK. The adviser points out that this is a compelling opportunity with an indicative return of around 8%, noting that additional opportunities include financing the aggregation of a farming and processing platform to produce a plant-based packaging material that is an alternative to single-use plastics, along with a range of other, more traditional, wind and solar investments.

The investment manager remains enthusiastic about the pipeline, due to the range of opportunities that can provide risk-adjusted returns which would be accretive to dividend coverage. However, the company also recognises that the use of cash

resources for pipeline investments must be weighed against repayment of its RCF and/or the repurchase of shares. It highlights that the latter has become an increasingly attractive option, given the discount at which the company's shares are currently trading, which the adviser believes does not reflect the fund's ongoing execution. The assessment of both these opportunities is subject to ongoing evaluation by the board.

Conservative assumptions

Figure 17: Valuation assumptions as at 31 March 2023

	GCP's approach	Most conservative	Potential impact on GCP's NAV (pence)	Least conservative
Electricity prices	Futures prices for three years and Afry four-quarter average long term	Afry Q1 2022	-0.24  8.07	Aurora Q1 2023
Capture prices (wind, solar)	Asset-specific curve applied to each project	Capture price discount of 15%	-0.66  4.81	No capture price discount
Asset lives	Lesser of planning, lease and technical life (20 to 25 years)	Contractual limitations	 2.78	Wind 30 years, solar 40 years
Indexation	OBR short-term, 2.5% RPI and 2.0% CPI long-term	2.5% RPI and 2% CPI long term	 0.35	3% plus
Taxes	25% UK corporation tax from 1 April 2023	Long term corporation tax at 25%	 1.08	25% tax only short-term

Source: GCP Infrastructure Investments

Figure 17 summarises the key assumptions used in forecasting cash flows from renewable assets in which the company is invested. GCP's advisers note that they take a conservative approach to valuations, valuing companies towards the lowest value methodologies available to them.

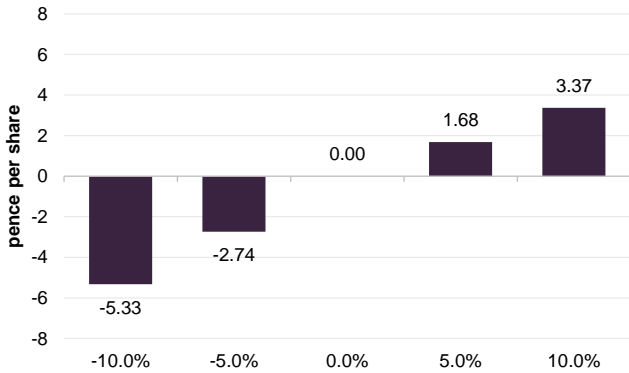
The net effect of this is that, were GCP to assume the most conservative assumptions in every category, the end June NAV of 112.24p would be reduced to 111.5p. By contrast, were GCP to assume the least conservative assumptions in each category, the NAV would have been 129.49p.

The adviser believes that such an approach reduces the likelihood and severity of any unexpected shocks to GCP's NAV, e.g. a sharp reversal in wholesale gas prices. Note that valuation metrics do not affect either the dividend pay-out or the share price yield.

Sensitivities

The investment adviser also provides a sensitivity analysis for its cash flows. Figures 18 and 19 show the impact of changes in power prices and changes in its base case inflation forecast.

Figure 18: Impact of change in forecast electricity prices



Source: GCP Infrastructure Investments

Figure 19: NAV impact associated with a movement in inflation



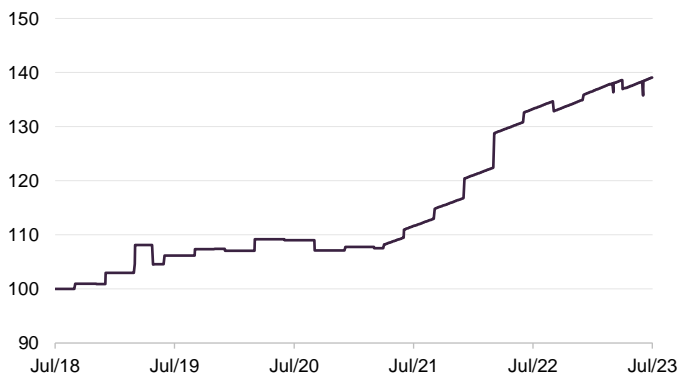
Source: GCP Infrastructure Investments

Performance

As Figure 20 shows, GCP's NAV has rallied since its plateau through the latter half of 2020/21, which the advisors believes is thanks predominantly to rising power prices during the period, with returns through 2022 the highest generated in the past five years.

Figure 21 shows the performance of the fund compared to the sterling corporate bond index, which acts as a de facto benchmark as the constituents are comparable with GCP's investments portfolio. The adviser notes that this figure provides another illustration of tangible returns generated by the GCP portfolio above direct market comparables.

Figure 20: GCP NAV total return



Source: Morningstar, Marten & Co

Figure 21: GCP NAV total return relative to sterling corporate bonds



Source: Morningstar, Marten & Co

Figure 22: Cumulative total return performance over periods ending 31 July 2023

	3 months (%)	6 months (%)	1 year (%)	3 years (%)	5 years (%)
GCP share price	(13.1)	(17.1)	(26.2)	(13.4)	(13.0)
GCP NAV	(0.9)	(0.6)	1.9	26.9	35.8
Sterling corporate bonds	(3.7)	(1.0)	(10.1)	(18.4)	(7.0)

Source: Morningstar, Bloomberg, Marten & Co

Peer group

Up-to-date information on GCP and its peers is available on the [QuotedData](#) website

GCP sits within the AIC's infrastructure sector, which is made up of four funds which invest predominantly in public/private partnership project equity (3i Infrastructure, BBGI, HICL and International Public Partnerships), two digital infrastructure funds (Cordiant Digital Infrastructure and Digital 9 Infrastructure) and one fund (Sequoia Economic Infrastructure, which, like GCP, invests primarily in infrastructure debt, but using a much broader definition of what constitutes infrastructure). We have excluded the Infrastructure India fund due to its risk profile, which the adviser believes does not align with the rest of the sector.

Figure 23: Infrastructure peer group comparative data as at 31 July 2023

	Premium / (discount) (%)	Dividend yield (%)	Ongoing charge (%)	Market cap (GBPm)
GCP	(30.8)	9.2	1.10	672
3i Infrastructure	(6.3)	3.8	1.64	2,887
BBGI	(9.6)	5.8	0.87	974
Cordiant Digital Infrastructure	(27.4)	4.9	1.10	632
Digital9 Infrastructure	(49.9)	10.9	1.10	478
HICL	(20.7)	6.3	1.09	2,665
International Public Partnerships	(17.7)	6.0	1.06	2,515
Pantheon Infrastructure	(19.0)	4.9	-	388
Sequoia Economic Infrastructure	(12.5)	8.5	0.96	1,373
Peer group median	(19.0)	6.0	1.09	974
GCP rank	8/9	2/9	5/8	5/9

Source: Morningstar, Marten & Co

Outside of DGI9, which, as the adviser points out, has suffered in part due to the ongoing rotation into higher-quality assets, GCP trades on the highest discount in the sector. This is despite offering one of the highest yields and an ongoing charge rate in line with the peer group median.

NAV performance has been modest in relation to the wider sector, as shown in Figure 24, and this may have weighed on GCP's longer-term ranking, which has traditionally been towards the top of its peer group. Still, returns over the past three and five years remain closely aligned with the median.

The relative NAV growth might perhaps explain the widening discount compared to the rest of the infrastructure sector.

GCP's focus on the UK may have also contributed, taking into account the economy's well-documented struggles with inflation, which have driven interest and therefore discount rates higher, further compounding the detrimental effects of last year's mini-budget. Inflation is trending lower, however.

Figure 24: Infrastructure peer group cumulative NAV TR performance ending 31 July 2023

	3 months (%)	6 Months (%)	1 year (%)	3 years (%)	5 years (%)
GCP	1.5	1.8	4.4	27.6	39.1
3i Infrastructure	0.8	3.2	12.8	44.7	89.1
BBGI	1.3	2.5	5.3	29.7	47.2
Cordiant Digital Infrastructure	0.9	7.4	10.4	n/a	n/a
Digital9 Infrastructure	1.3	7.2	10.3	n/a	n/a
HICL	0.7	2.9	6.2	28.9	45.9
International Public Partnerships	1.2	3.6	6.2	24.5	39.9
Pantheon Infrastructure	1.0	1.6	n/a	n/a	n/a
Sequoia Economic Infrastructure	3.1	3.7	2.3	14.8	26.5
Peer group median	1.2	3.2	6.2	28.2	42.9
GCP rank	2/9	8/9	7/8	4/6	5/6

Source: Morningstar, Marten & Co

Alternative peer group – renewable energy funds

In light of the increased weighting of renewable energy assets within GCP's portfolio, it may also be relevant to compare the company to the constituents of the renewable energy infrastructure sector. The sector encompasses a diverse range of funds which are not all directly comparable to GCP. This applies particularly to Ecofin US Renewables and US Solar Fund, which are cushioned somewhat from energy price volatility – which has been much greater in the UK and Europe – by having much-longer-term PPAs. The energy storage funds – Gore Street, Gresham House, and Harmony – and the energy efficiency funds – Aquila, SDCL and Triple Point – are also much less exposed.

The closest comparators may be Bluefield Solar, Foresight Solar, Greencoat UK Wind, JLEN Environmental, NextEnergy Solar, Octopus Renewables and The Renewables Infrastructure Group.

Figure 25: Renewable energy peer group comparative data as at 31 July 2023

	Premium / (discount) (%)	Dividend yield (%)	Ongoing charge (%)	Market cap (GBPm)
GCP	(30.8)	9.2	1.10	672
Aquila Energy Efficiency Trust	(38.8)	8.44	-	59
Aquila European Renewables	(20.8)	6.3	1.1	290
Atrato Onsite Energy	(14.9)	6.23	1.4	120
Bluefield Solar Income	(15.6)	7.12	1.02	722
Downing Renewables & Infra.	(22.6)	5.98	1.5	165
Ecofin US Renewables	(34.0)	9	1.8	67
Foresight Solar Fund	(20.2)	7.7	1.14	593
Gore Street Energy Storage	(13.5)	7.58	1.37	477
Greencoat Renewables	(7.0)	6.07	1.21	1,034
Greencoat UK Wind	(12.1)	5.98	0.93	3,393
Gresham House Energy Storage	(17.9)	5.73	1.18	735
Harmony Energy Income	(18.5)	8.39	-	217
HydrogenOne capital growth	(52.0)	0	2.51	62
JLEN Environmental Assets	(14.7)	7.18	1.18	697
NextEnergy Solar	(18.4)	8.92	1.06	553
Octopus Renewables Infrastructure	(13.9)	6.22	1.12	526
SDCL Energy Efficiency Income	(24.3)	8.08	1.02	843
The Renewables Infrastructure Group	(15.8)	6.3	0.93	2,831
ThomasLloyd Energy Impact	3.7	2.39	-	143
Triple Point Energy Efficiency	(30.4)	7.91	1.94	70
US Solar Fund	(33.2)	8.93	1.37	164
VH Global Sustainable Energy Opportunities	(23.7)	6.42	1.3	363
Peer group median	18.5	7.1	1.2	477.0
GCP rank	5/23	1/23	6/23	8/23

Source: Morningstar, Marten & Co

We have also compared GCP to the constituents of the [renewable energy sector](#)

Figure 25 shows how GCP stacks up against the renewable energy sector. GCP offers the highest dividend within this group while also maintaining one of the lowest charges. Despite this, the discount remains one of the widest in the sector.

The sector has been expanding rapidly over the last few years, and consequently many of these funds have not yet built up much of a track record, as shown in Figure 26, with only seven of the 23 funds having data out past five years.

The adviser notes that GCP's conservatively valued NAV may have dragged down its returns relative to the peer group median, with the company also suffering from its bias to debt rather than equity.

Figure 26: Renewable energy peer group cumulative NAV TR performance ending 31 July 2023

	3 months (%)	6 Months (%)	1 year (%)	3 years (%)	5 years (%)
GCP	1.5	1.8	4.4	27.6	39.1
Aquila Energy Efficiency Trust	1.1	(0.4)	2.3	n/a	n/a
Aquila European Renewables	(1.0)	0.1	12.1	n/a	n/a
Atrato Onsite Energy	2.4	3.9	n/a	n/a	n/a
Bluefield Solar Income	1.5	1.3	5.1	45.3	72.6
Downing Renewables & Infra.	1.2	0.6	4.3	n/a	n/a
Ecofin US Renewables	(2.1)	(1.4)	(3.2)	n/a	n/a
Foresight Solar Fund	1.5	1.2	6.2	58.2	63.8
Gore Street Energy Storage	1.8	7.9	12.9	47.5	n/a
Greencoat Renewables	0.2	1.3	11.3	26.4	n/a
Greencoat UK Wind	1.0	1.7	13.4	63.2	92.6
Gresham House Energy Storage	1.2	6.6	12.3	89.6	n/a
Harmony Energy Income	(5.1)	(3.6)	n/a	n/a	n/a
HydrogenOne Capital Growth	2.8	3.9	n/a	n/a	n/a
JLEN Environmental Assets	1.1	2.6	5.9	59.8	71.9
NextEnergy Solar	1.6	(4.0)	(0.1)	42.7	52.7
Octopus Renewables Infrastructure	1.3	1.0	1.8	n/a	n/a
SDCL Energy Efficiency Income	(3.0)	(1.6)	(0.9)	22.0	n/a
The Renewables Infrastructure Group	1.3	3.0	5.7	41.8	71.7
ThomasLloyd Energy Impact	(2.6)	(2.6)	n/a	n/a	n/a
Triple Point Energy Efficiency	2.7	2.0	9.3	n/a	n/a
US Solar Fund	(2.1)	(2.3)	(0.8)	16.6	n/a
VH Global Sustainable Energy Opportunities	5.0	2.4	4.1	n/a	n/a
Peer group median	1.2	1.3	5.1	44.0	71.7
GCP rank	7/23	9/23	11/19	9/12	7/7

Source: Morningstar, Marten & Co

Dividend cover

Loans made by the company are valued on a discounted cash flow basis. When a loan is first made, it is typically valued using the interest rate charged to the borrower. However, loans are often revalued by the valuation agent to reflect changes in the market rate of interest or for project specific reasons, for example.

As market rates of interest have fallen since GCP was launched, higher values have been attributed to many of the loans that it has made, uplifting the NAV. That has the effect of pulling forward the recognition of income from these loans and, on an IFRS accounting basis, reduces GCP's earnings per share and dividend cover in

subsequent years (a pull-to-par effect). For this reason, the board and the investment adviser have calculated a range of alternative performance measures. In addition, the adviser cautions that looking at measures of cashflow coverage of the dividend can be misleading. Interest accrued on loans can either be paid in cash or added to the outstanding principal and repaid when the loan matures (payment in kind or PIK). The adviser points out that this gives rise to timing differences that affect cashflow dividend coverage measures.

Figure 27 shows GCP's dividend cover ratios on two bases – normal (IFRS) earnings cover, and an adjusted figure which strips out the impact of unrealised fair value adjustments on the company's earnings, and perhaps better contrasts GCP's revenue and dividend payout.

The increase in the unadjusted earnings per share (EPS) coverage through FY2022 reflects a substantial increase in the unrealised value of GCP's assets.

Figure 27: Earnings and dividend cover

Financial year ended	Earnings per share (pence)	Adjusted earnings per share (pence)	Dividend (pence)	Dividend cover (EPS basis)	Dividend cover (adjusted EPS)
30/09/2019	6.74	8.06	7.6	0.89x	1.20x
30/09/2020	(0.08)	7.33	7.6	n/a	0.96x
30/09/2021	7.08	6.95	7.0	1.01x	0.99x
30/09/2022	15.88	7.11	7.0	2.27x	1.02x
30/09/2023 (six months to 31 March 2022)	2.91	3.8	3.5 (of 7.0p full year target)	0.8x	1.1x

Source: GCP Infrastructure Investments, Marten & Co

Emergence of a wide discount

Over the past 12 months, GCP's shares have traded on an average discount of -16.9%, a high of -0.5%, and a low of -35.5%. At 31 July 2023, the discount to the end June NAV was -32.1%. This has dropped from our previous note, published at the beginning of the year, where the average 12-month discount was just -5%. Historically, the fund has traded at a long-term premium that was as high as 20% prior to the pandemic.

Several factors have been discussed in this report which may have contributed to the company's discount (see pages 6, and 18). These have focused predominantly on rising interest rates which the adviser notes have put upward pressure on discount rates, as well as the relative attractiveness of other assets, including risk-free Government debt. Still, it points out, these macro factors have weighed on the entire income sector and do not explain the extent of GCP's discount, which is wider than the vast majority of its peers.

Figure 28: GCP discount over five years ending 31 July 2023



Source: Morningstar, Marten & Co

Fund profile

Regular, sustainable, long-term income

Renewable energy projects, PFI/PPP-type assets and specialist supported social housing

GCP Infrastructure Investments Limited is a Jersey-incorporated, closed-ended investment company whose shares are traded on the main market of the London Stock Exchange. GCP aims to generate a regular, sustainable, long-term income while preserving investors' capital. The fund's income is derived from loaning money at fixed rates to entities which derive their revenue – or a substantial portion of it – from UK public-sector-backed cashflows. Wherever it can, it tries to secure an element of inflation-protection.

In practice, GCP is diversified across a range of different infrastructure sectors although its focus has shifted more towards renewable energy infrastructure over the last few years. It has exposure to renewable energy projects (where revenue is part subsidy and part linked to sales of power), PFI/PPP-type assets (whose revenue is predominantly based on the availability of the asset) and specialist supported social housing (where local authorities are renting specially-adapted residential accommodation for tenants with special needs).

As part of the GABI merger discussed on page 3, GCP Infrastructure's board will propose an amendment to the trust's investment policy in recognition of the evolution that has occurred in the infrastructure landscape over the 13 years since IPO and to maximise the pool of attractive investment opportunities available moving forward. The amendment will require that at least 75% of GCP's total assets will:

1. benefit from public-sector backed, contracted, or predictable cash flows;

2. have no construction risks;
3. have a high standard of sustainability by reference to: (a) meeting a credible minimum standard for environmental and/or social sustainability; or (b) align with a specified environmental and/or social sustainability theme; and
4. are located in the UK.

The updated arrangement will also include a continuation vote at the company's AGM in 2028 and every four years thereafter.

The portfolio managers of the enlarged GCP will continue to be Philip Kent, Ed Simpson and Max Gilbert.

If the merger proceeds, the basis for calculating the adviser's fee would move from a flat fee of 0.9% on fixed assets to 0.9% on the first £1.3bn and 0.8% thereafter.

The investment adviser

More information is available on the investment adviser's website graviscapital.com

Gravis Capital Management Limited (Gravis) is the fund's AIFM and investment adviser and will continue to operate as such under the new arrangement. It is also investment manager of GCP Asset Backed Income, and advises VT Gravis Clean Energy Income Fund, VT Gravis UK Listed Property Fund, VT Gravis UK Infrastructure Income Fund, and VT Gravis Digital Infrastructure Income Fund. Gravis has assets under management of approximately £3bn.

At 31 March 2023, the key management personnel of the investment adviser, together with their family members, held 1,012,479 ordinary shares in the company, up from 952,614 shares at 30 September 2022.

Gearing

The company's original revolving credit facility from 29 March 2021 has been expanded from £165.0m to £190.0m. This is set to expire on 29 March 2024 and the investment adviser is liaising with the existing lending group in order to refinance the RCF in advance of the date of expiry. As at 31 March 2023, the total amount drawn on the RCF was £154m, compared to £99m at 30 September 2022.

Previous publications

Readers interested in further information about GCP may wish to read our previous notes (details are provided in Figure 29 below). You can read the notes by clicking on the links below or by visiting our website.

Figure 29: QuotedData's previously published notes on GCP

Title	Note type	Publication date
Stable income, uncertain times	Initiation	30 January 2020
Rebased dividend	Update	1 June 2020
Compelling yield	Annual overview	11 January 2021
Penalised for being conservative?	Update	1 July 2021
The future is brighter and greener	Annual overview	18 January 2022
Improving outlook and room to grow	Update	19 July 2022
Green is good	Annual overview	7 February 2023

Source: Marten & Co



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