EDHEC BUSINESS SCHOOL

Mr Steven Maijoor

Chairman

ESMA

103 Rue de Grenelle

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Nice, September 21, 2017

Dear Chairman,

EDHEC Infrastructure Institute is a component of EDHEC Business School, a not-for-profit academic organisation that is one of the Tier 1 business schools worldwide.

As with every major academic institution, research is a core activity for EDHEC. Since 2005, the positioning of our research in finance has been to build a bridge between academic research results and the practices and questions of professionals.

As such, EDHEC has often participated in the public debate on regulatory questions and your organisation has often had occasion to refer to the work of our institution, whether it be the relevance of taxes on financial transactions, the short selling ban or the regulation of final indices and ETFs.

More recently, in 2013, EDHEC participated actively in the calibration of capital requirements for infrastructure investment as part of EIOPA's work, by showing that these investments, due to their level of interest and especially due to their risk profile, deserved special treatment on the part of the regulator.

It is as part of this recognition of the specific characteristics of infrastructure that we approach you through this open letter that is intended to draw your attention, and that of investors, to the risks that investment in so-called `listed infrastructure' can represent. To develop the arguments that are presented succinctly in this letter, we are publishing a new position paper, which you will find enclosed with this letter, summarising our research.

In this position paper, we document the dangerous rise of the so-called listed-infrastructure asset class, an ill-defined series of financial products initially targeting retail and increasingly institutional investors, which now represent close to a third of investors in such products.

Promising to deliver the benefits of an 'infrastructure investment narrative', listed infrastructure has been growing by 15% annually for a decade, reaching USD57bn of assets under management (AUM) today.

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But serious research shows that listed infrastructure is failing to deliver on its many promises and, in our view, the number of false claims made about listed infrastructure products is high enough to consider a case of mis-selling.

Our review of the marketing documentation for 144 listed infrastructure products representing 85% of the sector by AUM concludes that such products typically make near-identical claims compared to private infrastructure products.

However, our and others' research shows repeatedly that listed infrastructure, as it is proposed to investors today, exhibits high drawdown and volatility, does not have better risk-adjusted performance than broad stock market indices and can typically be explained away by a series of well-known factor-tilts available to investors throughout the stock market.

We also find that active listed infrastructure managers have invested in close to 1,900 different stocks over the past decade, many of which cannot possibly be considered to be 'infrastructure' under any definition.

In such a context of false promises, the growth of listed infrastructure products is problematic because of the damage that their proliferation will eventually do to proper infrastructure investing.

We believe in the potential of infrastructure debt and equity investment for asset owners. We also see no reason why – in principle – some of the products used to access the characteristics of underlying infrastructure assets could not be listed on public markets.

Today, however, a large number of listed infrastructure products that can be commercialised in the form of mutual funds, or even of exchange-traded funds, will disappoint. They are comparatively expensive compared to traditional funds and will leave investors without the promised low-risk, stable, inflation-linked returns that characterise the pay-offs of real infrastructure investment. As a result, these `fake' infrastructure investment vehicles could give a bad name to infrastructure investing in general.

This `fake infra'–as we call it–could reverse years of educating investors about the potential of infrastructure assets as sources of portfolio diversification and liability-hedging instruments.

As such, it may jeopardise the involvement of institutional investors in the next generation of public-private partnerships that underpins so much of the national infrastructure plans being put forward by most OECD governments.[1]

Listed infrastructure managers are not all equally responsible for the state of the sector described in this paper. Some have been involved in trying to create access to infrastructure businesses through listed products honestly and for a long time, but at this stage it is impossible for investors to be able to tell the difference between these products, because they all have the same qualifiers.

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[1] Common listed infrastructure indices have a 20% tracking error with private infrastructure equity indices such as the ones published by EDHEC*infra* (BBG:EIPEE)

As a result, we strongly recommend stricter regulatory oversight of these products including the obligation to include the word 'listed' in their name to avoid misleading investors, as well as the obligation to include information in marketing documents and information kits warning investors that listed infrastructure may not deliver the same performance as unlisted infrastructure investments.

These precautions will *de facto* be an incentive for investors to distinguish between the different forms of investment in infrastructure and to conduct in-depth due diligence with respect to the products that are offered to them.

With our thanks in advance for your attention to this letter,

Yours faithfully,

Noël Amenc

Professor of Finance, Associate Dean for Business Development, EDHEC Business School

Frédéric Blanc-Brude

Director, EDHEC Infrastructure Institute

Encl. EDHEC Infrastructure Institute Position Paper: The Rise of "Fake Infra"