

## Water Investing: Tapping into a Source of Resilient Growth

By Hubert Aarts

March 19, 2018



The water investment story is diverse and growing, and the drivers behind this growth are strengthening – and look set to do so for decades. Water also presents a far broader investment opportunity than might first be considered. It consists of the pipes, pumps, and meters that form infrastructure, the technology and software that monitors and controls the infrastructure, and the treatment technologies that make water safe for humans to drink.

### What is driving growth in the water sector?

We have been researching and investing in the broader water universe since 2002, and within this period, the number of companies in the water value chain has grown significantly. Behind this is an increasing demand for water, paired with an ever-tightening global supply of this finite resource. At the same time, concerns over global water quality and safety are moving up the agenda of governments worldwide.

## Drivers of water demand

- Population growth, higher disposable incomes and higher living standards in developing markets, is increasing water consumption.
- Increasing urbanization, particularly in developing regions, and further industrialization requires substantial new water infrastructure.
- An urgent need to replace and modernize much of the existing water infrastructure in developed countries to ensure efficient delivery and water safety, driven by tightening government regulation.
- Extreme weather events such as storms, droughts and flooding are becoming more frequent and can have pronounced effects on water infrastructure and demand for clean water.

## Technology developments

---

As well as an increase in demand, technological advances are changing the ways in which water is managed and used, giving rise to a range of investment opportunities. For example, advanced metering solutions are growing at nearly twice the rate of traditional water meters. Smart meters play a critical role in more effective metering and pricing of water, and are key to reducing water use and detecting leaks.

Utilities are being forced to focus on more effective management of their infrastructure, particularly reducing leakage rates and avoiding catastrophic failures. Leakages are a major issue. In the United States, nearly 6 billion gallons of treated water is lost nationwide, due to leaking pipes<sup>1</sup>. One approach to solving this problem is through improved integration of sensors and monitoring.

Smart pump technology is also developing rapidly, including the launch of waste water pumping systems with integrated intelligence. These systems can adapt performance in real time and provide feedback to pumping station operators, increasing efficiency and reliability, and making them simpler and cheaper to run than the traditional technologies.

## Extreme weather events and the water investment implications

---

Scientific consensus is that the frequency and intensity of extreme weather events is increasing<sup>2</sup>. The winter storms that battered the East Coast at the end of 2017, and the series of events that saw Californians suffer droughts, wildfires, flooding and mudslides lend weight to this concern.

While the immediate response to flooding requires systems to pump and transport water, longer-term planning around storm resilience typically requires huge investment in water infrastructure, too. For example, water treatment facilities may require upgrading to address contamination during tidal surges and flood conditions.

## Cyclical and defensive benefits

---

The performance of cyclical stocks is very much dependent on how the wider economy is performing, whereas defensive stocks are more likely to offer stable earnings in any economic environment. Water-focused stocks offer investors a way to balance their portfolio between the

two, and to optimize for attractive returns as appropriate.

Cyclical stocks include companies that produce relatively commoditized products, such as pumps, pipes and valve manufacturers, which see increased demand in economies with infrastructure spending commitments and/or a tightening of environmental regulations.

Defensive stocks include water treatment companies, which typically supply products such as membranes and filters, often on a repeat purchase model so the buyer is tied to buying replacements from the equipment supplier. The equipment has predictable replacement cycles and provides manufacturers with relatively stable earnings profiles. This is also the case for suppliers of mission-critical water chemicals which, while low cost from a monetary perspective, are crucial from a process and safety standpoint. Rather than relying on new capital investment for growth, water chemical companies tend to have clear earnings visibility due to the importance of their product in existing processes.

## Water sector investing: experience matters

---

Over fifteen years' experience of investing in the water sector gives us the insight to identify, in our view, promising companies, and the ability to tap into the resilient growth of this sector, which we believe to be a multi-decade investment opportunity.

For information about the **Pax Global Environmental Markets Fund**, which invests in companies that are developing innovative solutions to resource challenges – including water, energy, waste, and sustainable food & agriculture – visit the Fund page [here](#).

---

1. <https://www.infrastructurereportcard.org/wp-content/uploads/2017/01/2017-Infrastructure-Report-Card.pdf>
2. [https://www.ipcc.ch/pdf/special-reports/srex/SREX-Chap3\\_FINAL.pdf?dm\\_t=0,0,0,0,0](https://www.ipcc.ch/pdf/special-reports/srex/SREX-Chap3_FINAL.pdf?dm_t=0,0,0,0,0)

*The statements and opinions expressed are those of the author of this report. All information is historical and not indicative of future results and subject to change. This information is not a recommendation to buy or sell any security.*

PAX007776

---

## Hubert Aarts

Hubert Aarts is a Co-Portfolio Manager of the Pax Global Environmental Markets Fund and has been involved in the Fund since its inception in 2008.

© 2018 Impax Asset Management LLC. All rights reserved.

Pax World Funds are distributed by ALPS Distributors, Inc. ALPS Distributors is not affiliated with Impax Asset Management LLC.

