First State Investments Direct Infrastructure

RI Asia 2014: Long-term, sustainable, fiduciary investing

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Our direct infrastructure business at a glance

Our Business

$112bn market capitalisation of parent company, Commonwealth Bank of Australia

1994 year that we began managing infrastructure investments

$3.7bn net assets under management

42 infrastructure acquisitions and divestments since 1994

27 dedicated infrastructure professionals, located in offices across Australia and Europe

13.5% Gross return on core economic infrastructure since 1994

Current assets & offices

All data as at 31 December 2013

Investment experience across major sectors

First State Investments
Colonial First State Global Asset Management

Utilities & Others

anglianwater

Stage: Brownfield
Sector: Water Utility
Acquisition: 2009

electricity north west

Stage: Brownfield
Sector: Electricity distribution
Acquisition: 2009

reganosa

Stage: Brownfield
Sector: Gas Utility
Acquisition: 2010

DIGITA

Stage: Brownfield
Sector: Broadcasting towers
Acquisition: 2012

FGN

Stage: Brownfield
Sector: Gas Utility
Acquisition: 2013

Fortum Distribution Finland

Stage: Brownfield
Sector: Electricity Distribution
Acquisition: 2013

Transportation

Brisbane Airport

Stage: Brownfield
Sector: Airport
Acquisition: 1997

Adelaide Airport

Stage: Brownfield
Sector: Airport
Acquisition: 1998

metro Transport

Stage: Brownfield
Sector: Urban Transport
Acquisition: 1995 (Exited)

Hills M2

Stage: Brownfield
Sector: Toll Road
Acquisition: 1997 (Exited)

Benefits of investing in infrastructure

Benefits of investing in infrastructure

- **Attractive risk adjusted returns:** Investing in infrastructure has achieved attractive risk adjusted returns over the long term with stable, predictable cash yield
- **Inflation protected income:** The nature of infrastructure assets means they are typically able to increase prices inline with inflation
- **Low correlation with other asset classes**
  - 0.04 with Australian equities, -0.13 with fixed income, 0.52 with unlisted property, 0.06 with A-REITS and 0.20 with listed infrastructure for 10 years ending December 2013
- **Long duration assets to match long tail liabilities**
- **Growing asset class:** Privatisation of government assets, larger private sector involvement in new infrastructure and a significant replacement cycle should make infrastructure a high growth asset class over the next decade

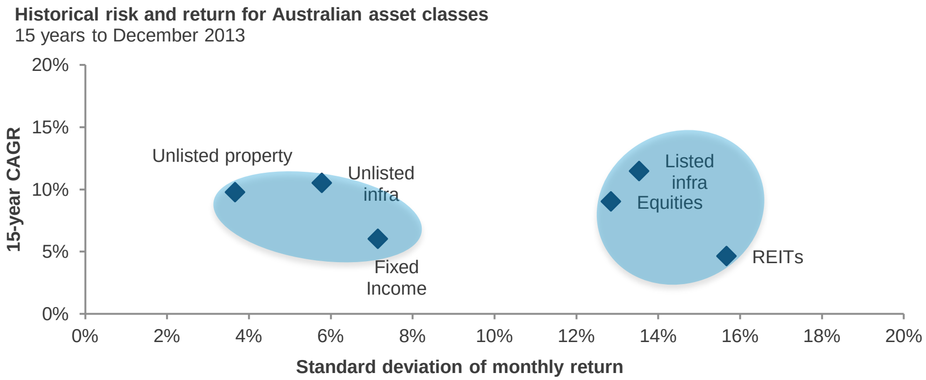
Advantages of unlisted infrastructure

- **Low volatility:** driven by both the stable nature of the underlying assets, as well as the appraisal based valuation method
- **Control:** direct holdings allow unlisted managers to exert greater influence through Board seats, resulting in active asset management at the asset level as well as the portfolio level
- **Transparency:** closer relationships with management teams and greater access to information
- **Attractive yields:** yield oriented returns underpinned by stable cash flows, with the potential for capital gains
- **Scarcity:** access to unique monopoly assets, often regulated
- **Diversification:** low correlation with other asset classes

**For the avoidance of doubt, all reference to First State Investments experience and capability in relation to infrastructure refers to both First State Investments and Colonial First State Global Asset Management in Australia. All data as at 31 December 2013*

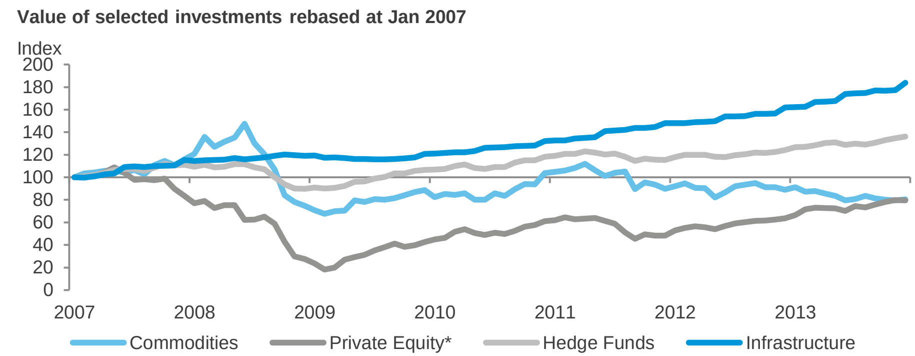
Infrastructure – an attractive investment

Attractive risk return profile



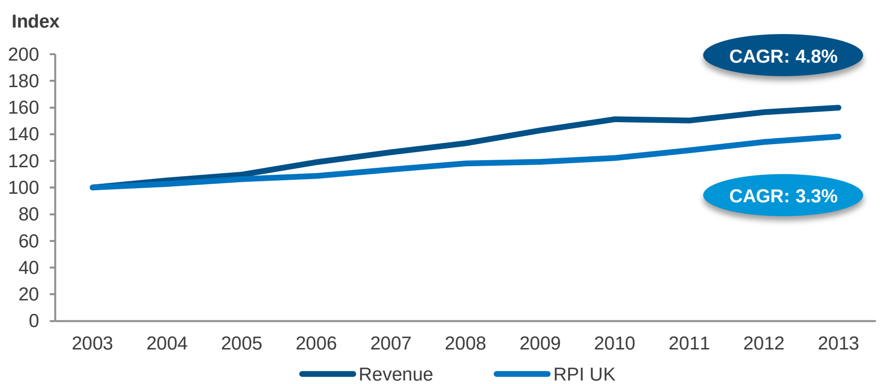
Source: CFSGAM Research, 15 year Australian return performance and standard deviation data to 30 September 2013

Stable return profile



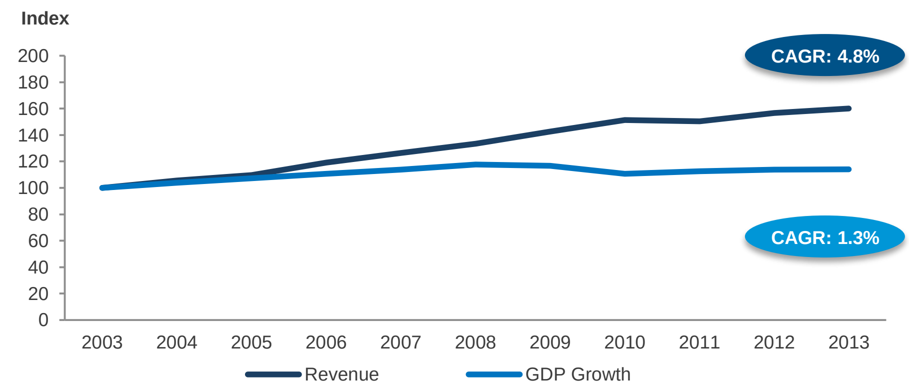
Note: Private Equity returns refer to share price returns of listed PE firms
Source: Mercer, Bloomberg and CFSGAM Research, Rebased at January 2007. All data to December 2013

Inflation protection



Source: Anglian Water Group – Annual Reports 2003 to 2012 (March 2013), UK Office for National Statistics

Resilience to economic cycles



Source: Anglian Water Group – Annual Reports 2003 to 2012 (March 2013), UK Office for National Statistics

Our investment approach

First State Investments
Colonial First State Global Asset Management

1 Core infrastructure focus

We invest in essential infrastructure assets, which typically:

- Are subject to multiple forms of regulation
- Are high-profile, and therefore have a wide and diverse set of stakeholders, often with competing agendas and priorities
- Require us to maintain our 'social license to operate'

2 Active management

Our brand of active management involves:

- Meaningful stakes in companies, giving us board representation and therefore greater influence
- Deep industry experience through our asset managers, who bring an operational and governance focus

3 Long-term investors

Unlisted infrastructure holdings are typically illiquid, so unlike a listed securities manager, we do not have the option of a quick sale in response to identification of issues (stewardship model).

Asset ownership and board representation

Asset	CFSGAM stake	Board seats[1]
AWG	32.3%	2
Brisbane Airport	26.5%	3
ENW	50.0%	3
Digita	100.0%	3
Adelaide Airport	15.3%	1
Bankstown and Camden Airports	33.3%	1
International Parking Group	37.5%	1
Reganosa	15.0%	3
Newham Hospital	50.0%	2
Somerton Pipeline	12.5%	1

How sustainability and active management create value

Operational focus encourages efficiency and sustainable processes

Long investment horizon, greater control allows us to identify and mitigate ESG risks

$$\frac{\text{return}}{\text{risk}} = \alpha$$

Responsible investing principles applied

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Our investment approach	How does it relate to responsible investment?		Portfolio examples
Long-term investment horizon	Our investment horizon means that we cannot afford to ignore longer term impacts of issues such as environmental change	E	▪ **Anglian Water's** embedded CO2 modeller tool used in network design ➢ *67% carbon reduction and project capex reduced by 25%*
Core infrastructure focus	The essential role our assets play in society means we must engage with a diverse range of stakeholders in order to maintain our 'social license to operate.'	S	▪ $1.3 bn new runway project at **Brisbane Airport** required balancing diverse interests including safety, noise, cost, environmental, regulatory and operational concerns. ➢ *Over 300 approvals with runway height at a level above 1-in-100 storm and incorporates potential climate change impacts*
Active management approach	Taking significant stakes in businesses with board representation allows us to exert real governance influence	G	▪ As 50% owner of **Electricity North West**, we were able to drive integration of outsourced service provider UUES and effectively create a standalone business. ➢ *Reconnection of labour force with network assets allows greater responsiveness to customer needs and regulatory requirements*

Leading responsible investor

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Established partnerships

FOCUSED ON RESPONSIBLE INVESTMENT.

Investor Group on Climate Change Australia/New Zealand

International Corporate Governance Network

green building council australia MEMBER

ISCA Infrastructure Sustainability Council of Australia

CARBON DISCLOSURE PROJECT

ASFIA

Principles

- ESG considerations thematically considered in overall portfolio strategy using insights from investment life cycle and broader considerations of infrastructure ESG issues
- Early signatory to the UN Principles for Responsible Investment
- UNPRI were developed by institutional investors to reflect the relevance of ESG
- In signing the Principles, we have publicly committed to adopt and implement them, where consistent with our fiduciary responsibilities

Embedded through investment process

Due diligence

- ESG issues considered using best practice guidelines at due diligence phase
- PRI and IFC Guidelines both part of investment decision making process

Operating governance

- Through active asset management, board positions are used to influence best practice ESG issue identification and management

Ongoing valuations

- Internal analyst team building their capabilities in the ESG space
- ESG are part of capabilities under consideration in the appointment of valuers and it is ensured that best practice resources in the area is implemented throughout the process

Our strategy and ESG: a natural fit

- The essential nature of **core infrastructure** assets brings a broad range of stakeholders from the wider community into play. Managing ESG issues is critical to maintain our social license to operate.
- Our **long-term investment horizon** allows us to better incorporate ESG issues into the ongoing management of investee companies.
- Our **active management approach**, where we take significant stakes in unlisted infrastructure businesses, allows us to drive the ESG agenda in order to enhance returns or reduce risks

Colonial First State
Global Asset Management

First State Investments

Appendix – Market Overview

Europe

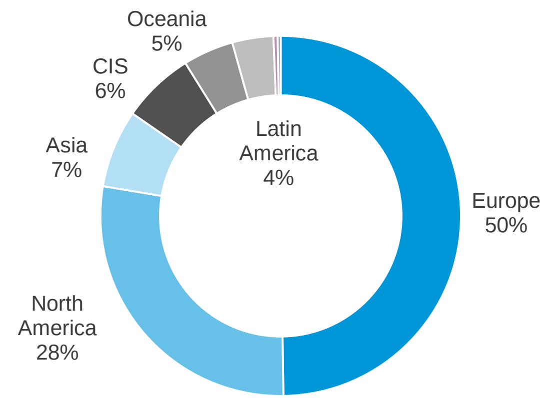
1 Unmatched depth and diversity

- **Cornerstone region for developed-market investors** – 24 of the 34 OECD members located in Europe, which rates highly on institutional criteria such as property rights and transparency.
- **Market depth** – Europe not only largest institutional infrastructure market, but is also the largest market for overall corporate infrastructure M&A, accounting for half of global deals.*
- **Multiple jurisdictions increase diversification potential**. With >30 national governments, investors are better able to diversify political and regulatory risk, and are less exposed to actions of any one government (e.g. privatisation delays)

2 Good mix of cyclical and structural drivers

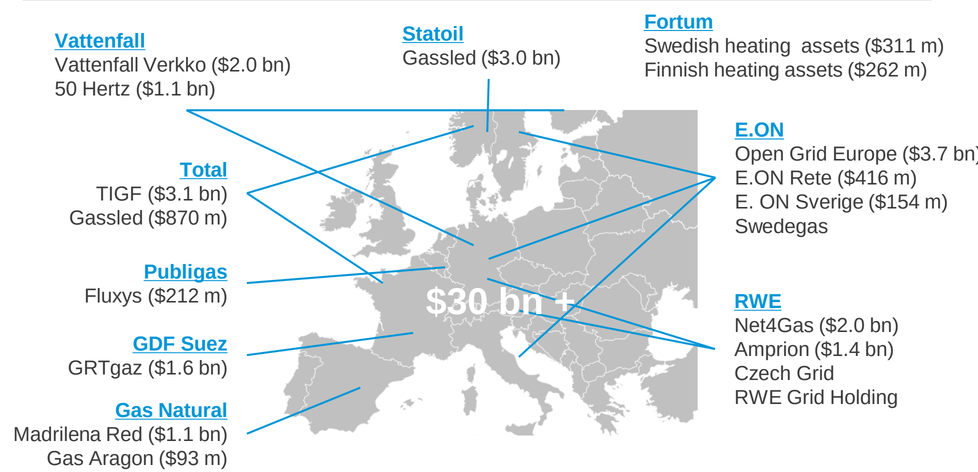
- Large European utilities **divesting assets**, due to:
  - Financial pressures: repairing debt-laden balance sheets
  - Strategic reasons: exiting lower-margin 'non-core' activities
  - Regulation: unbundling of vertically-integrated utilities
- New EU-wide **renewables target** of 27 per cent of energy from renewables by 2030 announced in early 2014. Less prescriptive, but more market-based than previous version.
- **Privatisations** will continue to present opportunities, particularly in southern Europe.
- **Contractors** recycling capital from mature assets into greenfields

Corporate infrastructure activity by region*



Source: CFSGAM Research and Zephyr

Selected energy utility divestments (2010-13)**



* Excludes institutional. private equity and MLP deals

Source: CFSGAM Research and Zephyr. **Sales to financial buyers only.

Australia

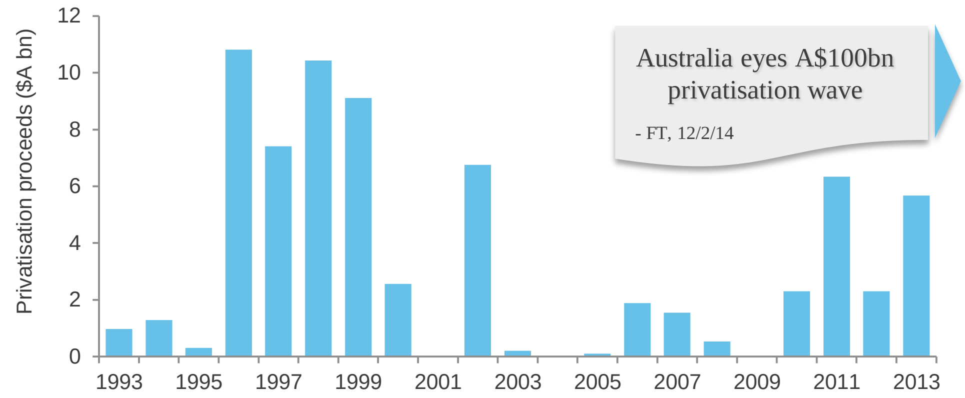
1 Highly attractive investment destination

- **Established infrastructure market** – long history of infrastructure privatisations, second only to the UK in this regard
- **Enviable economic fundamentals** – two decades of uninterrupted GDP growth. AAA credit rating and low sovereign debt levels. Strong ties to Asian region.

2 Deal pipeline: stronger for longer

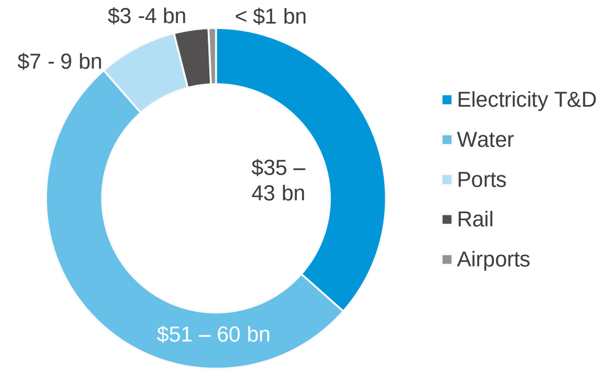
- **Privatisations**: after initial wave of privatisations in mid to late-1990s, Australia is now the in the early stage of a second wave of privatisations.
- More than **$100 billion** of assets remain on Federal and State government balance sheets.
- Peaking of the **resources boom** is adding impetus to rationalisation efforts, and sale of non-core assets by corporates
- **Capital recycling** model of brownfield privatisation proceeds being reinvested into greenfield infrastructure should ensure greater **continuity** of infrastructure investment opportunities
- **Mature market**: listed assets and secondary market transactions as institutional investors rebalance their portfolios

Australian infrastructure privatisations



Various sources, CFSGAM Research

Publicly-owned infrastructure by sector



North America

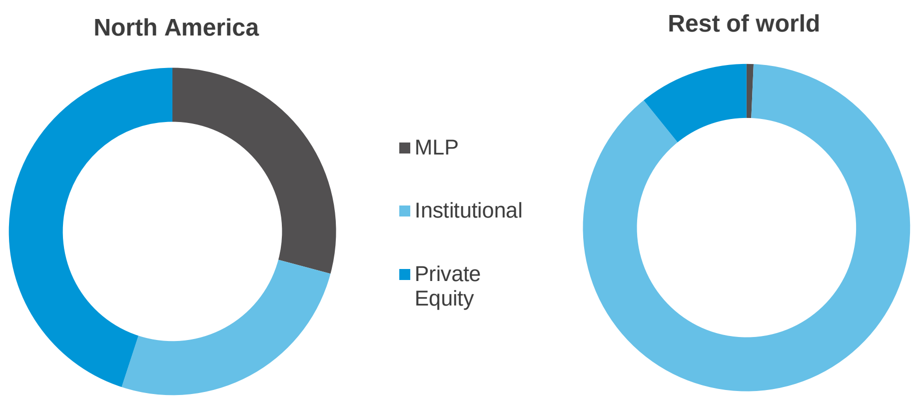
1 Institutional landscape is unique

- ‘Traditional’ institutional infrastructure investors* less prolific in North America due to prevalence of private equity firms, MLPs and alternative financing sources such as tax-exempt bonds
- **MLPs**: Master Limited Partnerships have grown rapidly over the past decade, with market capitalisation of ~$400 billion. Mainly house lower-risk, high-yield midstream oil and gas assets, but non-traditional assets are increasingly being placed into these structures.
- **Private Equity** – these investors typically have higher return hurdles, and therefore target higher-risk sectors such as generation assets.

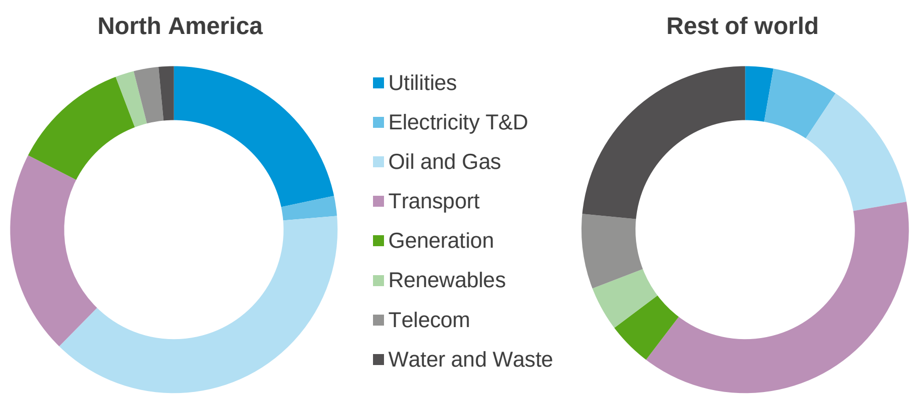
2 Short-term obstacles, medium-term potential

- **Energy**: INGAA estimates over $250 billion is needed on new energy infrastructure between 2011 and 2035, with shale gas creating new investment opportunities.
- **Transportation**: many states have enacted PPP legislation, with greenfield transport projects currently underway. Brownfield privatisations will require further political will, with several ‘false dawns’ so far.
- **Water**: US water sector mainly publicly-owned, fragmented and has marginal economics. Consolidation and reform to encourage private financing could transform the sector.

Infrastructure activity by acquiror type



Institutional infrastructure activity by sector



* According to our definition, this includes pension funds, sovereign wealth funds, insurers and dedicated infrastructure funds

Source: CFSGAM Research and Zephyr

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