First State Investments
首域投資

Global Listed Infrastructure

Monthly Review and Outlook

September 2016

- First State Global Listed Infrastructure Fund invests in global listed infrastructure and infrastructure-related securities.
- Investing in shares in a single sector may expose the Fund to greater volatility than investing in multiple sectors. The value of the Fund may be impacted by risks associated with listed infrastructure including changes in environmental regulations. It is possible that the entire value of your investment could be lost.
- All or part of the Fund's fees and expenses may be paid out of capital resulting in an increase in distributable income and effectively a distribution out of capital. Similarly in certain circumstances dividends may be paid out of capital. This amounts to a partial return of an investor's original investment, or from any capital gains attributable to that original investment, and may result in an immediate decrease of the Net Asset Value per share.
- You should not base your investment decision solely on this document. You should not invest unless the intermediary who sells it to you has advised you that the Fund is suitable for you and explained how it is consistent with your investment objectives.

Key highlights:

- The Fund gained 1.4% in September, 20 bps behind of its benchmark and 80 bps ahead of global equities.
- The best performing sector was Pipelines, due to significant takeover activity. Ports and Toll Roads lagged.
- Japan was the best performing region as investors were attracted to the value on offer in its infrastructure stocks. Oceania was the worst performing region on Toll Road and Utility underperformance.

Market review

Global listed infrastructure delivered positive returns to investors in September. In USD terms, the FTSE Global Core Infrastructure 50-50 index rose 1.6%, while global equities finished the month 0.6% higher.

Pipelines performed particularly well as Canada's Enbridge Inc made a US$28 billion bid for US peer Spectra Energy. The move comes after a US$13 billion acquisition of Columbia Pipeline Group by TransCanada earlier this year. Regulator and community resistance to greenfield projects is making existing pipeline networks more valuable, driving speculation that the sector may see further corporate restructuring and takeover activity.

The next-best performing sector was **Railroads**. US freight rail operators were supported by management teams' reiteration of the sector's strong pricing power at the latest industry conference. September's better than expected ISM manufacturing reading provided a positive data point. Japanese passenger rail recovered from recent underperformance ahead of the scheduled US$3.8 billion privatisation of Kyushu Railway Company – Japan's largest IPO so far this year.

The worst performing sector was **Ports**, which consolidated recent gains. However the sale of the Port of Melbourne by Victoria's state government to a consortium of investors for a higher-than-expected A$9.7 billion highlighted the underlying strength of demand for these long life, tangible assets.

The best performing region was **Japan**, whose electricity and gas utilities rallied following several months of underperformance. **Oceania** lagged on concerns that US interest rate rises could impact its high yielding utilities, airports and toll road stocks.

Fund review

In USD tern, the Fund rose 1.4% in September[1], behind its benchmark index by 20 bps.

The best performing stock in the Fund was pipeline operator **Spectra Energy**, which rallied sharply following the takeover offer from **Enbridge Inc**. The deal will create the largest energy pipeline and storage company in North America, and highlights the high quality of Spectra's existing pipeline networks, as well as the growth potential of its future projects. The Fund's other pipeline holdings, **TransCanada** and **Kinder Morgan** advanced on heightened investor interest in the sector, while higher oil prices provided a further tailwind.

US freight rail operators **CSX** and **Union Pacific** gained on stabilizing volumes and indications of a favourable domestic economic backdrop. **Kansas City Southern** lagged on news that this quarter's earnings would be affected by flooding in Texas, and by teachers union protests which disrupted operations on its Mexican rail networks earlier in the year. Japanese passenger rail operator East Japan Railway climbed as investors looked past a dip in August passenger revenues caused by typhoon disruption, to focus on the company's stable business model, high quality infrastructure assets and the growth optionality associated with its central Tokyo property portfolio.

Gains in the utilities sector were led by gas utility **Rubis**, which rose on better than expected H1 earnings results. A combination of recent acquisitions and organic earnings growth delivered profit growth at each of its four business divisions. The results imply that an upgrade

[1] The Fund's calendar year performance: -5.7% (2015); 12.3% (2014); 17.3% (2013); 10.4% (2012); 1.2% (2011).

to FY earnings is likely. The UK's **National Grid** increased as the process to sell a majority stake in its gas distribution assets gathered pace. The latest bidder to emerge is Cheung Kong Infrastructure, the parent company of Hong Kong-listed Power Assets Holdings, which already owns substantial UK utility assets. SSE is going through a similar process with its gas distribution assets, Scotia Gas Networks.

The worst performing stock in the Fund was **China Merchant Ports** (-6%) which fell after weaker than expected organic growth and persistent margin pressure impacted H1 earnings. Following gains in recent months driven by signs that global trade volumes were beginning to improve, **Cosco Shipping Ports** also declined.

The Fund's airport holdings underperformed. **Japan Airport Terminal** lagged as Chinese tourist spending continued to fall. **Fraport** was impacted by lower Asia Pacific passenger numbers – a theme common to several European airports and airline operators. Mexico's **GAP** dipped despite consistent double-digit passenger volume growth. Spain's **AENA** was the exception; the stock was propelled higher as the market looked past political uncertainty to focus on consistently robust Spanish tourist volumes.

The Fund sold BBA Aviation as two material catalysts – the sale of its aircraft refueling business ASIG, and a growing market awareness of the synergies associated with its recent merger with Landmark Aviation – played out. The resulting share price outperformance led us to sell.

A position was initiated in Japanese gas utility **Tokyo Gas**. Uncertainty about the proposed de-regulation of Japan's residential retail gas market has weighed on its share price over the past 12 months, moving it higher within our investment process. The company now trades on modest valuation multiples compared to US peers, and offers the prospect of reasonable returns in Japan's low interest rate environment.

Outlook

The Fund invests in a range of global listed infrastructure assets including toll roads, airports, ports, railroads, utilities, pipelines and mobile towers. These sectors share common characteristics, like barriers to entry and pricing power, which can provide investors with inflation-protected income and strong capital growth over the medium-term.

Our largest overweight position is in the toll road sector. Revenues are robust, with consistently high operating margins of between 60% and 80%. We believe that the market does not yet fully appreciate these companies' ability to grow earnings through contracted toll increases, additional growth projects, concession extensions and organic traffic volume growth.

Our largest underweight position is in US utilities. Some companies in this sector face challenging regulatory environments; are trading at full valuation multiples; or derive a significant portion of their revenue from merchant coal generation, which now faces a vicious cycle of declining market share, reduced revenues and rising costs.

Our main holdings in this sector are made up of companies that are at the forefront of renewable build-out such as NextEra Energy and Xcel Energy; an area of the market that is experiencing a virtuous cycle of falling costs, improving productivity and growing market share. We also have exposure to companies which are participating in the build-out of much needed transmission infrastructure such as Eversource Energy and Dominion Resources.