First State Investments
首域投資

Global Listed Infrastructure

Monthly Review and Outlook

October 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 declined by -2.9% in October. Calendar YTD returns remain positive, at +12.4%.
- Ports were the best performing sector, supported by robust volumes; pipelines lagged on lacklustre earnings numbers.
- Latin America and Japan were the best performing regions. Oceania underperformed for a second consecutive month.

Market review

Global listed infrastructure declined in October against a backdrop of mixed quarterly earnings numbers, higher bond yields and political uncertainty ahead of the US Presidential election. In USD terms, the FTSE Global Core Infrastructure 50-50 index ended the month down 1.9% as global equities dipped 1.9%.

The best performing sector was **Ports**, which gained on positive volume data. The next-best performing sectors were **Utilities** on the appeal of their defensive, low risk, capex driven earnings growth and stable dividend streams. **Towers** (flat) were supported by their lack of economic sensitivity, underpinned by structural growth in demand for mobile data.

Pipelines gave up ground as the sector's strong rally since early 2016 lost momentum on mixed quarterly earnings announcements and a lower oil price.

Latin America was the best performing region, led higher by Brazil's water and electric utilities. **Oceania** underperformed as Sydney Airport (-10%, not held) and Auckland Airport (-10%, not held) lagged on valuation concerns.

Fund review

In USD terms, the Fund fell 2.9% in October[1], 102bps behind its benchmark index.

The best performing stock in the Fund was German airport **Fraport**, which rallied on the view that authorities may allow it to raise airport fees at Frankfurt Airport; and on hopes that a recently received US$270 million compensation payment from the Philippines government could be paid to investors as a special dividend. **Japan Airport Terminal** climbed on strong growth in international arrivals in September, particularly from China, at Haneda, Narita and Kansai airports. AENA also gained as capacity growth on Asian, US and UK routes supported volumes across its network of high quality Spanish airports.

The portfolio's utility holdings performed relatively well in an uncertain market environment. Larger UK and US names including **NextEra Energy, Eversource Energy, PG&E, SSE** and **Dominion Energy** held up. These companies continue to derive low risk earnings growth by investing in much-needed transmission infrastructure; and by participating in the accelerating shift towards renewable energy.

Smaller gas-focussed utilities including **Tokyo Gas, UGI Corp** and **Rubis** also gained. Tokyo Gas rallied on positive September volumes led by a 7% increase from its industrial segment, on higher gas demand for power generation. UGI Corp announced it expects 2016 earnings to be at the upper end of its guidance range, despite unusually warm weather in 2016 impacting demand. Normalised weather in 2017 could underpin further earnings growth.

The worst performing stock in the Fund was **Eurotunnel**, which fell on growing concerns that a 'hard Brexit' could affect demand for its unique, long concession life infrastructure asset. The positive impact of a 14% increase in truck volumes on its vehicle shuttle service in 3Q was partially offset by a surprising 10% fall in Eurostar passengers.

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

North American rail companies underperformed. **Union Pacific** fell post a poor 3Q result and concerns that lower freight volumes may be eroded its pricing power. Easier volume comparisons are likely to provide a tailwind in coming quarters. **Kansas City Southern** lagged on disappointing 3Q earnings, as flooding on its rail network in Louisiana pushed costs higher and weighed on volumes. Stable, low-risk. Japanese passenger rail operator East Japan Railway climbed after announcing 2Q earnings results in line with consensus.

Australian toll road operator **Transurban** also fell as September quarter earnings showed that traffic growth in its key market of Sydney declined to a lower-than-expected 3.5%.

Energy pipeline company **Kinder Morgan** lagged after a weak 3Q result and concerns that its current strategy of de-gearing and balance sheet repair may take longer to achieve than initially hoped. Elsewhere in the sector, Canadian peer **TransCanada** fared comparatively well as the market continued to digest the implications of its recent takeover of **Spectra Energy**. **Enbridge Inc (flat)** held up ahead of its 3Q earnings results, scheduled for early November.

The Fund added to its Pipelines exposure by initiating a position in **Enterprise Products Partners**, a US$57 billion market cap, high quality operator run by a well-regarded and experienced management team. Its assets include approximately 51,000 miles of pipelines and 200 million barrels of storage capacity. The company has a strong balance sheet, pays a distribution yield of ~6% and has a robust earnings growth profile based on exposure to US energy exports and growth in Natural Gas Liquids.

The Fund sold its shares in large cap US electric utility **Duke Energy** as positive returns during our extended holding period moved it lower within our investment process.

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 outlook for the Fund is positive. Tailwinds for the asset class overall include ongoing structural drivers (such as demand for mobile data or renewable energy); and shifting asset allocation from low-yielding bonds and volatile equities towards real assets. Potential headwinds could include a sharp rise in interest rates; and political and regulatory interference, particularly at times close to elections.

Accordingly the Fund has an underweight exposure towards the interest rate sensitive utilities, especially those with lower earnings growth outlooks. Overweight exposure has been maintained to growth infrastructure such as the toll road sector, which contains high quality, low risk companies generating robust cash flows and trading at discounts to intrinsic value. We also favour mobile towers, on the view that the market continues to underestimate mobile data growth and overestimate potential risks to free cash flow for these strategically positioned, well-managed infrastructure companies.