Fund Update: 30 June 2019

MAGELLAN
EXPERTS IN GLOBAL INVESTING

Magellan Infrastructure Fund (Unhedged)

ARSN: 164 285 830

Fund Facts

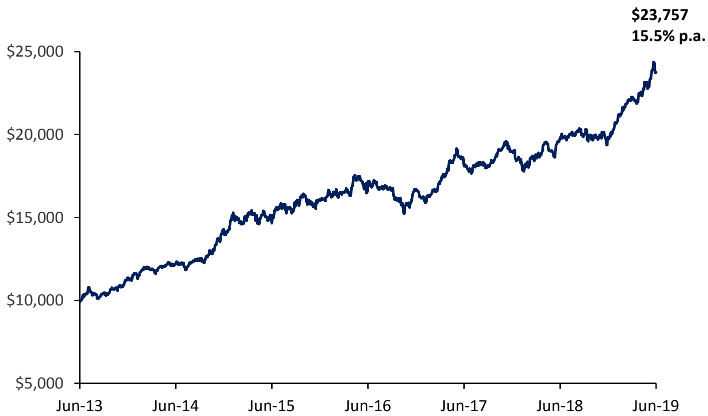
Portfolio Manager	Gerald Stack
Structure	Global Listed Infrastructure Fund (Unhedged)
Inception Date	1 July 2013
Management & Administration Fee[1]	1.05% per annum
Buy/Sell Spread[1]	0.15%/0.15%
Fund Size	AUD $936.8 million
Distribution Frequency	Six Monthly
Performance Fee[1]	10.0% of the excess return of the units of the Fund above the higher of the Index Relative Hurdle (S&P Global Infrastructure Index A$ Unhedged Net Total Return) and the Absolute Return Hurdle (the yield of 10-year Australian Government Bonds). Additionally, the Performance Fees are subject to a high water mark.

[1]All fees are inclusive of the net effect of GST

Fund Features

- Benchmark-unaware exposure to global listed infrastructure
- Conservative definition of core infrastructure
- Relatively concentrated portfolio of typically 20 to 40 investments
- Maximum cash position of 20%
- $10,000 minimum investment amount.

Performance Chart growth of AUD $10,000*



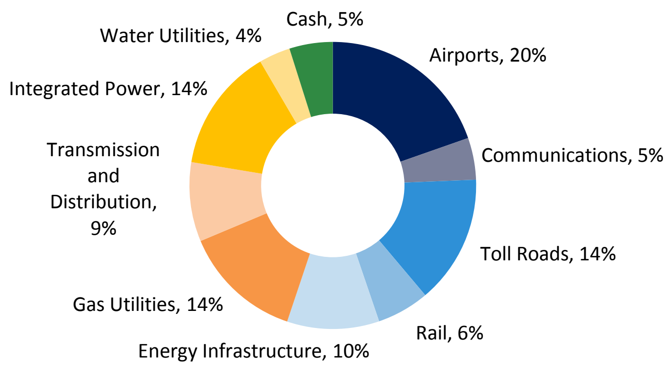
Fund Performance*

	Fund (%)	Index (%)**	Excess (%)
1 Month	4.1	4.0	0.1
3 Months	7.0	6.2	0.8
6 Months	19.7	19.8	-0.1
1 Year	20.2	16.9	3.3
3 Years (% p.a.)	11.4	9.9	1.5
5 Years (% p.a.)	14.2	10.7	3.5
Since Inception (% p.a.)	15.5	12.3	3.2

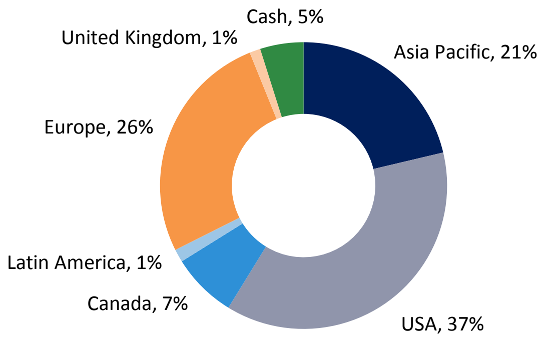
Top 10 Holdings

	Sector#	%
Transurban Group	Toll Roads	6.2
Atmos Energy Corp	Gas Utilities	5.9
Aena SME SA	Airports	5.3
Enbridge Inc	Energy Infrastructure	5.0
Xcel Energy Inc	Integrated Power	4.9
Aeroports De Paris	Airports	4.7
Atlas Arteria	Toll Roads	4.4
Sempra Energy	Gas Utilities	4.3
Eversource Energy	Integrated Power	4.0
Crown Castle International	Communications	3.7
	TOTAL:	48.4

Sector Exposure#



Geographical Exposure#



Sectors are internally defined. Geographical exposures are by domicile of listing. Exposures may not sum to 100% due to rounding.
* Calculations are based on exit price with distributions reinvested, after ongoing fees and expenses but excluding individual tax, member fees and entry fees (if applicable). Fund Inception 1 July 2013.
** S&P Global Infrastructure Index A$ Unhedged Net Total Return spliced with UBS Developed Infrastructure and Utilities Net Total Return Index (AUD). Note: as the UBS Developed Infrastructure and Utilities Net Total Return Index (AUD) ceased to be published from 31 May 2015, it was replaced by Magellan on 1 January 2015 with the S&P Global Infrastructure Index A$ Unhedged Net Total Return.

Fund Commentary

The portfolio recorded a positive return for the quarter. Stocks that added the most on a contributions basis included the investments in Aena of Spain, Transurban, Auckland International Airport and Canadian Pacific. Aena rose 14% after Spain's biggest airport operator upgraded its traffic guidance for the year on a strong first quarter and strong capacity growth for the summer schedule in Europe. Transurban added 14% when investors turned to longer-duration assets as the Reserve Bank of Australia cut the cash rate from 1.5% to 1.25% in June and flagged more cuts to help the slowing economy. Canadian Pacific rose 12% as investors judged that the railway operator's weather-affected first-quarter earnings wouldn't stop the company achieving double-digit earnings growth for the fiscal year. Auckland Airport jumped 21% supported by a rotation to defensive names on weaker economic data and as the Reserve Bank of New Zealand cut interest rates to a record low 1.5%.

The only stock that detracted on a contributions basis was the investment in ADP of France. ADP lost 8% after France's constitutional court suspended the further sale of the government's 50.6% stake in the operator of Paris's airports ahead of a possible referendum on any sale proposed by political parties opposing the sale.

Movements in stock prices are in local currency.

Key Stock in Focus – Evergy

Evergy: A US electricity utility formed from a merger to save customers money.

In mid-2018, two regulated electric utilities in the US, Westar Energy and Great Plains Energy, completed their merger. The rationale for the merger was simple – lower customer bills while generating attractive and reliable returns for shareholders. The new entity, named Evergy, now generates and supplies electricity to about one million residents in Kansas and about 600,000 people in the neighbouring state of Missouri.

To understand why Evergy is a promising investment it helps to understand the regulatory framework under which utilities operate in the US. The crux of the model is that utilities are granted a monopoly to supply their services to a specified area but, in return, regulators place a limit on the return they can earn on the capital they invest to provide these services – an investment amount known as the 'rate base'. The regulation is designed to ensure providers supply an essential service (electricity or gas) to an area at a fair price while allowing them to earn a fair return on their investment.

Management identified annual savings of about US$200 million from the merger and used a portion of these savings to gain regulatory approval. Regulators are typically wary of tie-ups such as the one that created Evergy because they want to ensure consumers are protected. To win regulatory approval, therefore, the companies that became Evergy made two promises. The first was there would be no increases to customer bills for five years (excluding a pass-through of changes in fuel costs). The other is that it would immediately give its customers a one-off rate credit of US$60 million and annual credits of US$50 million each year over the next five years.

Investors like the merger because it set up a company that is primed to generate 5% to 7% growth in earnings per share over the next five years. The company will achieve this growth target in two ways. The first is from the cost savings above those handed back to customers. The other is that Evergy intends to repurchase about 20% of its shares over the next two years, a move that will bring the company's debt levels to a level broadly in line with industry peers.

The longer-term advantage of the permanent cost savings from the merger (the US$150 million left over each year after US$50 million is passed back to customers) allows Evergy to grow its rate base – and thus earn greater profits – without needing to ask the regulator to approve higher charges for its customers. Evergy is a prime example of the best sort of regulated utility stock; namely, one that provides investors with strong underlying cash flows as well as long-term structural growth.

To be sure, Evergy comes with some risks. Cost savings are never assured, and the company might overpay for its own stock. But these risks are unlikely to derail the investment thesis for the company.

Cleaner power

Evergy's origins trace to 1909 when one of the companies that formed Westar in 1992 was founded. Evergy's assets now extend to more than 22,000 kilometres (13,700 miles) of transmission lines and 84,000 kilometres (52,200 miles) of distribution lines (the ones that reach households) that are fed electricity from its multiple sources of generation. Evergy's key sources of regulated generation are coal, natural gas and wind, which account for more than 90% of generation capacity.

Evergy says its mission is to empower a better future. To that end, the company aims that by the end of 2020 nearly half the power it supplies to homes and businesses will come from emission-free sources. In 2018, for example, Evergy retired about 1,500 megawatts of fossil generation capacity and added 244 megawatts of wind power. CO_2 emissions in 2018 were 36% below those of 2005.

The name Evergy was chosen to be a combination of 'ever' and 'energy'. Funnily enough, most Evergy customers are yet to see the new company name on their energy bills because these are still sent under the names Westar and Kansas City Power & Light, the subsidiary of Great Plains.

Later this year, Evergy will mount a marketing campaign to let its customers know about the new company. No doubt the cost savings for customers will get much publicity too.

Sources: Company filings, company website and Bloomberg.