Strategy Update: *31 December 2021*



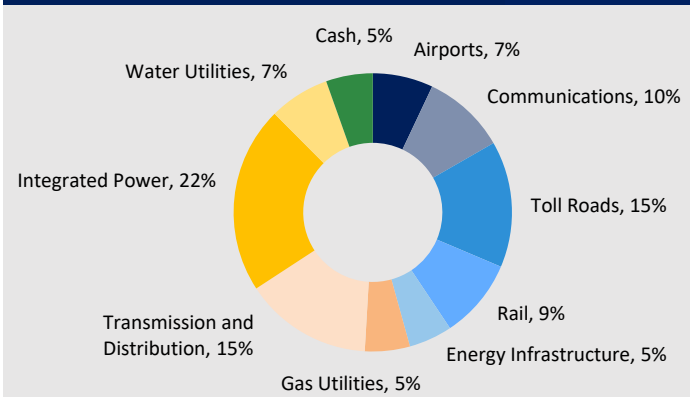
Magellan Global Select Infrastructure (AUD Hedged)

Portfolio Manager	Strategy Inception Date	Total Strategy Assets	Total Infrastructure Assets[1]
Gerald Stack	1 July 2007	AUD $10,162.7 million	AUD $20,565.2 million

Objective	Approach
Capital preservation in adverse markets	Concentrated 20-40 stock portfolio applying our proprietary infrastructure classification
Pre-fee return of CPI plus 5-6%p.a. through the economic cycle	Valuation driven benchmark-unaware strategy
	Highly defensive, inflation-linked exposure

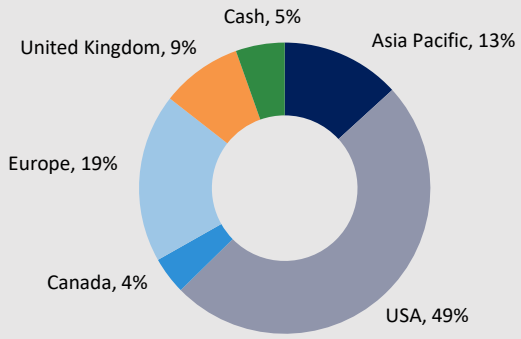
Top 10 Holdings[2]	Sector[2]	%
Transurban Group	Toll Roads	6.8
American Tower Corporation	Communications	4.9
Crown Castle International	Communications	4.8
Sempra Energy	Integrated Power	4.6
Vinci SA	Toll Roads	4.6
Eversource Energy	Transmission and Distribution	4.4
Red Electrica Corporacion	Transmission and Distribution	4.2
Enbridge Inc	Energy Infrastructure	4.1
Dominion Energy Inc	Integrated Power	3.9
Xcel Energy Inc	Integrated Power	3.9
	TOTAL:	46.2

Sector Exposure[2]



AUD 5 Year Risk Measures[3]	Against Global Equities	Against Infrastructure Benchmark[4]
Upside Capture	0.6	1.0
Downside Capture	0.5	0.7
Beta	0.6	0.7
Correlation	0.7	0.9

Sector Exposure[2]



3 Year rolling returns[5] (measured monthly)	1 Year	3 Years	5 Years	Since Inception
Against the Infrastructure Benchmark[4]				
No. of observations	12	36	60	139
Average excess return (% p.a.) (Gross)	2.1	3.8	4.3	5.2
Average excess return (% p.a.) (Net)	1.3	3.0	3.5	4.3
Outperformance consistency (Gross)	100%	100%	100%	99%
Outperformance consistency (Net)	92%	97%	98%	97%

Performance[6]	3 Months (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)	10 Years (% p.a.)	Since Inception (% p.a.)
Composite (Gross)	8.8	16.6	9.7	9.6	12.7	9.3
Composite (Net)	8.6	15.7	8.8	8.7	11.8	8.4
Global Infrastructure Benchmark	4.5	13.7	7.8	6.0	8.7	5.4
Excess (Gross)	4.3	2.9	1.9	3.6	4.0	3.9
MSCI World NTR Index (A$ Hedged)	7.8	23.7	20.0	13.9	14.5	8.4

Annual Performance[6] (%)	2021	2020	2019	2018	2017	2016	2015	2014	2013	2012	2011
Composite (Gross)	16.6	-10.7	26.8	0.6	18.9	7.8	12.6	24.0	19.1	16.8	12.4
Composite (Net)	15.7	-11.4	25.8	-0.2	18.0	7.0	11.7	23.0	18.2	15.9	11.5
Global Infrastructure Benchmark	13.7	-11.9	25.3	-6.7	14.4	14.1	-5.4	22.9	18.5	9.1	4.7
Excess (Gross)	2.9	1.2	1.5	7.3	4.5	-6.3	18.0	1.1	0.6	7.7	7.7
MSCI World NTR Index (A$ Hedged)	23.7	10.3	26.7	-7.4	19.8	10.4	3.8	12.3	31.8	18.8	-2.3

1 Comprised of all Infrastructure Strategies.
2 The data is based on a representative portfolio for the strategy. Refer to the end of the document for further information. Sectors are internally defined. Geographical exposure is by domicile of listing. Exposures may not sum to 100% due to rounding.
[3] Risk measures are for the Global Select Infrastructure Hedged in AUD Composite before fees. The Global Equity Index is the MSCI World NTR Index (A$ Hedged).
[4] The Benchmark or Global Infrastructure benchmark is comprised of the following: from inception to 31 December 2014 the benchmark is UBS Developed Infrastructure & Utilities NTR Index (A$ Hedged) and from 1 January 2015 onwards, the benchmark is the S&P Global Infrastructure NTR Index (A$ Hedged). Note: the UBS Developed Infrastructure and Utilities NTR Index (A$ Hedged) ceased to be published from 31 March 2015, replaced on 1 January 2015 with the S&P Global Infrastructure NTR Index (A$ Hedged).
[5] Rolling 3-year returns are calculated in AUD and rolled monthly for the duration of each period shown. The average excess return is then calculated for each period, with outperformance consistency indicating the percentage of positive excess returns. Strategy inception is 1 July 2007.
[6] Returns are for the Global Select Infrastructure Hedged in AUD Composite and denoted in AUD. Performance would vary if returns were denominated in a currency other than AUD. Strategy inception is 1 July 2007. Refer to the GIPS Disclosure section below for further information. Composite (Net) returns are net of fees charged to clients and have been reduced by the amount of the highest fee charged to any client employing that strategy during the period under consideration. Actual fees may vary depending on, among other things, the applicable fee schedule and portfolio size. Fees are available upon request.

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The Global Infrastructure Benchmark is comprised of the following: from inception to 31 December 2014 the benchmark is UBS Developed Infrastructure & Utilities Index Net Total Return (A$ Hedged) and from 1 January 2015 the benchmark is S&P Global Infrastructure Net Total Return Index (A$ Hedged). The benchmark changed because UBS discontinued their index series. The UBS Developed Infrastructure & Utilities Net Total Return Index (A$ Hedged) is a market capitalisation weighted index that is designed to measure the equity performance of listed Infrastructure and Utility stocks. Index results assume the reinvestment of all distributions of capital gain and net investment income using a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties. The index is hedged to Australian dollars.
The S&P Global Infrastructure Net Total Return Index (A$ Hedged) is a market capitalisation weighted index that is designed to track 75 companies from around the world diversified across three infrastructure sectors energy, transportation and utilities. Index results assume the reinvestment of all distributions of capital gain and net investment income using a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties. The index is hedged to Australian dollars.

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The Global Select Infrastructure Hedged in AUD composite is a concentrated global strategy investing in strictly defined or "pure" infrastructure companies, (typically 20-40). The filtered investment universe is comprised of stocks that 1. generate reliable income streams 2. benefit from inflation protection and 3. have an appropriate capital structure. The investment objective of the strategy is to minimise the risk of permanent capital loss; and achieve superior risk adjusted investment returns over the medium to long-term. The portfolios are hedged to Australian dollars with Forward contracts. The composite was created in December 2011.

To achieve investment objectives, the composite may also use derivative financial instruments including, but not limited to, options, swaps, futures and forwards. Derivatives are subject to the risk of changes in the market price of the underlying securities instruments, and the risk of the loss due to changes in interest rates. The use of certain derivatives may have a leveraging effect, which may increase the volatility of the composite and may reduce its returns.

A copy of the composite's GIPS compliant presentation and/or the firm's list of composite descriptions are available upon request by emailing client.reporting@magellangroup.com.au

The representative portfolio is an account in the composite that closely reflects the portfolio management style of the strategy. Performance is not a consideration in the selection of the representative portfolio. The characteristics of the representative portfolio may differ from those of the composite and of the other accounts in the composite. Information regarding the representative portfolio and the other accounts in the composite is available upon request.

AUD is the currency used to calculate performance.

Strategy Commentary

The strategy recorded a positive return in the December quarter. Stocks that contributed the most included the investments in Crown Castle International, Norfolk Southern and CSX Corp of the US. Crown Castle gained after the tower operator announced it had increased its dividend by an annualised 11% a share when it delivered healthy third-quarter earnings. Norfolk Southern climbed after the Atlanta-based railway operator's third-quarter report showed railway operating revenues increased 14% to US$2.85 billion. CSX rose after the Florida-based railroad and transport company's third-quarter report showed revenue rose 24%, driven by growth across all business lines.

The stocks that detracted the most were the investments in Aena of Spain, Transurban of Australia and Royal Vopak of the Netherlands. Aena, the world's largest operator of airports, declined as the new covid-19 variant disrupted travel. Transurban fell as investors worried about the potential impact of the surge in covid-19 infections in New South Wales, priced in interest rate rises sooner than had been flagged previously by the Reserve Bank of Australia after a report showed inflation reached 3% in the 12 months to September, the ceiling of the central bank's target, and the company reached a settlement with the Victorian government and its contractors regarding the allocation of cost overruns on its West Gate Tunnel project that was larger than investors expected. Royal Vopak slid as the backwardation in oil markets continued, even as the storage terminal operator reported a solid third-quarter result that topped expectations.

Stock contributors/detractors are based in local currency terms.

Stock Story: Dominion Energy

Dominion Energy, a US regulated electricity and gas company, first invested in solar power in 2013. Now the utility that services nearly seven million customers in 16 US states has, at 2,300 megawatts, the third-biggest solar generation capability in the country. In home state Virginia, Dominion is building a further 3,700 megawatts of solar capacity as part of a drive to create another 16,000 megawatts of this renewable source of power by 2035.

Commencing in 2023, the company is spending US$10 billion to build wind turbines more than 40 kilometres out to sea off the Virginia coastline. By generating 2,640 megawatts of power, the offshore wind farm is expected to power 650,000 homes and businesses.

Such steps and others are part of Dominion Energy's commitment to achieve net-zero emissions by 2050. The company, which earned US$14.2 billion in revenue in fiscal 2020, has already reduced its carbon footprint by 42% over the past decade or so.

The other relevant timeline that helps explain why Dominion Energy has come on to Magellan's investment radar is a shorter one, that shows how a company owning regulated and unregulated power assets largely turned itself into a highly regulated utility company. This was done through two mergers with utilities and by selling most of the unregulated assets.

The metamorphosis started in 2016 when Dominion Energy came together with Utah-based natural-gas utility Questar. Three years later, Dominion Energy fused with South Carolina-grounded electricity and natural-gas utility SCANA. The sale of the company's merchant generation and gas transmission and storage assets has taken place over the past five years.

The result is that 88% of Dominion Energy's operating earnings now come from state and federally regulated utility subsidiaries compared with 40% in 2006. The remaining 12% of earnings flow from zero-carbon, long-term contracted power-generation assets; namely, from Dominion's nuclear power plant in Connecticut, its interest in a liquified natural-gas facility on the Virginia side of Chesapeake Bay, and a portfolio of solar-generation assets.

To see why Dominion Energy's shift to being a regulated utility with a focus on sustainable energy is of interest to investors, it helps to understand how utilities are regulated.

The key feature of utilities is they are monopolies in their vicinities. To stop utilities using this power to overcharge their customers, governments and utilities have developed a 'regulatory compact'. Under this deal, monopoly utilities must invest the money required to provide the essential service in a safe and reliable manner. In return, utilities are allowed to recover their costs and earn a 'fair' return. The amount invested on which a utility can earn a fair return is driven by the capital invested and is known as its 'rate base'. As approved capital spending drives their long-term earnings, utilities seek to maximise the amount of regulator-approved investment as defined by the rate base, while also managing customer bill impacts.

Under this regulatory framework, Dominion Energy is a promising investment for two reasons. First, given the legacy of unregulated assets, the company's stock trades at a discount to other highly regulated peers. We expect this discount to close over time as investors come to appreciate the predictable income stream from its regulated assets that in rate-base terms are valued at about US$42 billion. (About 77% of rate base is attributable to the electricity utility and the rest to gas, while Virginia and South Carolina subsidiaries account for a significant majority of regulated operations – representing about 52% and 20% respectively.)

The other reason Dominion Energy is a promising investment is the long-term relatively low-risk earnings growth we expect from the company's assets. This is being supported by regulators and legislators who are pushing utilities to invest in renewable forms of power generation because they help governments meet their decarbonisation goals and lower bills for users. The total cost of electricity of the solar farms being installed by Dominion Energy, for example, is lower than the variable costs of the coal power plants they are replacing.

The company thus has the regulatory ok to boost its rate base by spending a lot of money on green energy, which provides the company with strong capital growth prospects. Over the next five years, Dominion Energy intends to spend US$26 billion in emissions-reducing capital. By 2035, the utility could spend as much as US$72 billion to achieve regulatory-approved environmental goals.

The company's capital investment plan is expected to drive long-term earnings growth of 6.5% per annum. The combination of such capital and earnings growth on top of the predictability of the company's income stream are why we hold Dominion Energy in the infrastructure fund.

Now to the risks. The biggest one for utilities is that regulators regularly reassess their allowed rates of returns. But Dominion Energy has largely settled its allowed return for its Virginia and South Carolina electricity subsidiaries for the medium term. Execution is another risk, especially given the magnitude of Dominion Energy's investment plan. Some plans might never happen. Dominion Energy, for example, was recently forced to abandon its joint-venture Atlantic Coast Pipeline project due to delays from never-ending legal challenges that nearly doubled the cost of the project in the six years since it was announced. But that venture was peripheral to the company's regulated utility business.

The risks thus appear contained. To the benefit of investors, Dominion Energy has changed much since it first invested in solar power in 2013. The utility promises to transform itself much more in coming years, most likely for the benefit of investors as well as society.

Source: Company filings and website.