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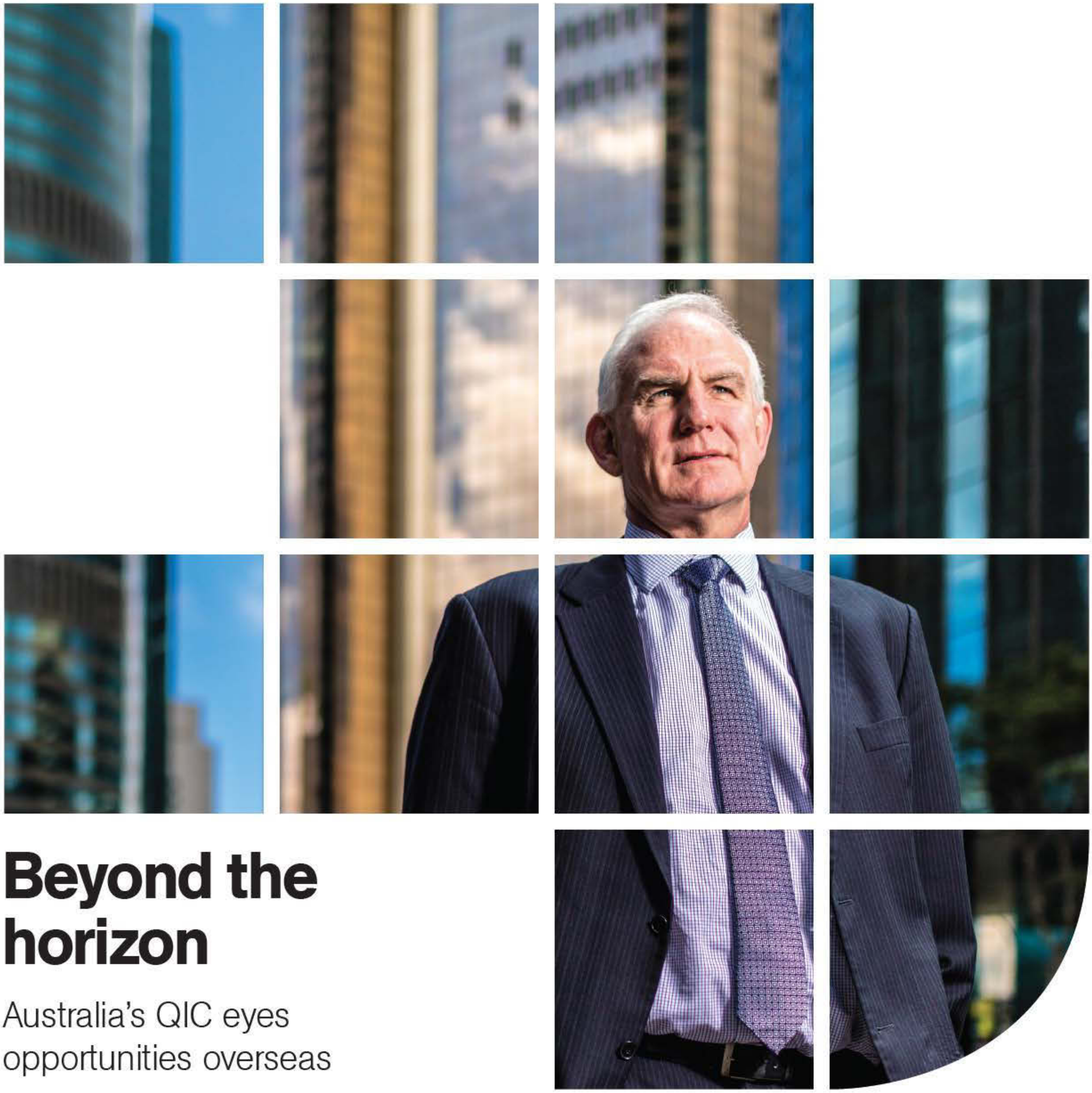


Beyond the horizon

Australia's QIC eyes opportunities overseas

Interview with Damien Frawley

A pension fund powerhouse in its home country, Australia's Queensland Investment Corporation is now setting its sights – and billions of capital – on infrastructure assets in North America and Europe. *IJGlobal* meets its chief executive Damien Frawley.

The Australian pension system features a concept – superannuation - which has led to the rise of some heavy hitting institutional investors, known as 'superfunds'. Superannuation is a system whereby employers must pay a percentage of their workers' salaries (currently 9.5% of income) into state savings schemes. On retirement, employees may be eligible to a state pension on top of their superannuation savings.

Successfully running as a countrywide, state-enforced scheme since 1992, the numbers involved in Australian superannuation are big. As QIC chief executive Damien Frawley explained: "There's about a A$2.2 trillion pot of superannuation savings in Australia. The way the system is designed [means] it's regulated to grow at 9.5% each year. When you do the numbers, you realise it's a very significant amount that has to be invested."

Superannuation funds under management are now larger than the capitalisation of the Australian Stock Exchange and Australia's gross domestic product. The funds' investors – Australian pension savers – have extensive choice, with over 500 superannuation funds in existence. Legislative changes in the past decade have also allowed employers to establish their own funds. "Superfunds are a competitive space," Frawley admitted. "We can't all do the same thing – their members can move pretty quickly between superfunds since the government introduced choice. It's contingent on the superfunds to be looking at where the best sources of income are going to come from, and they'll be conscious that they won't all want to do the same thing."

QIC's strategy

In its home country, QIC is a major investor. Founded in 1991 by the Queensland government to take care of its pension savings, QIC has since grown to become one of Australia's largest wholesale fund managers, with almost A$75 billion of assets under management. It is now setting its sights on infrastructure beyond Australia as a means of diversifying and growing the business.

Frawley said that the size of QIC has compelled it to expand internationally. "It becomes an issue where you can spend that money. That's why I think a lot of the big superfunds in Australia have almost been forced to start to view their portfolio through a global lens as opposed to just a domestic one. Whilst there's a lot of opportunity domestically in infrastructure and real estate, it's also very competitive."

> "A lot of the big superfunds in Australia have almost been forced to start to view their portfolio through a global lens"

Frawley's career began in another highly competitive arena, international rugby union. The Queensland native played for Australia between 1986 and 1988, before leaving the Wallabies for the banking sector. His first role was as a corporate foreign exchange dealer at Citibank. He then moved up through positions at Barclays Global Investors and Merrill Lynch before settling in Sydney as CEO of BlackRock Australia. In 2012, his home state called him back via the offer of the chief executive role at QIC.

Frawley made reorganising the structure of the QIC team and improving internal communication immediate priorities when he took up the role. "There were people in different teams going to meet the same clients without realising, staff going in and out the office lobby who didn't know each other," he said.

QIC invests across five main areas: infrastructure, real estate, liquid strategies, private equity and multi-assets. Liquid strategies account for the lion's share of QIC's investments, with around A$30 billion under management while real estate accounts for another A$20 billion. The other three areas have traditionally represented much smaller investment shares. But after making some strategic hires, Frawley turned his attention to growing the superfund's infrastructure allocation.

An early domestic infrastructure investments by QIC was the A$3 billion acquisition from the state government of major toll road network Queensland Motorways in 2011. QIC sold off the business last year for some A$7 billion to a consortium of investors from Australia and the United Arab Emirates. Following the sale, QIC's infrastructure allocation halved to A$6.5 billion, leaving an opportunity for growth.

Maiden international fund

IJGlobal met with Frawley at QIC's London office in early November. He was touring Europe to meet would-be investors in QIC's maiden international infrastructure vehicle, its A$2 billion

Pauline Vamos

Global Infrastructure Fund (GIF).

Europe is as yet relatively unfamiliar territory for QIC's infrastructure practice. Its European portfolio comprises a 19.7% slice of Spanish ports operator GMTCB and an 8.7% stake in UK utility Thames Water. In North America, its market penetration is similarly slight, with a trio of investments in California's Long Beach court house, the CampusParc car parking business and a Canadian medical research facility.

This is all set to change with QIC's launch of GIF. The fund, launched in the spring of this year, has already reached A$900 million in investments. Contributions have come from international pension and sovereign wealth funds, and fellow Australian superfunds, QIC global head of infrastructure Ross Israel said.

First close on the fund will happen in two phases. The first phase, which covers contributions from southern hemisphere investors, closed in August. The second phase is mooted for early 2016 for northern hemisphere investments, as regulatory approval for the fund has only just been achieved for these jurisdictions.

The open-ended fund has an A$1.75 billion cap. It operates a hybrid structure where, despite the evergreen nature of the fund, investors have the option to exit eight years after the five-year investment period. A final close is planned within 18 months after first close. The fund, which will chase a 10-12% rate of return, has the ability to make investments in Australian dollars, Euros, Sterling and US dollars.

Despite its global name, 60% of the investments made by the fund will be in Australia. There is an estimated A$800 billion financing gap in the Australian infrastructure market, and the secondary infrastructure market is a buoyant one, fuelled in part by an ambitious national privatisation programme. In the 2014 budget the federal government launched a A$5 billion asset recycling initiative, which provides financial incentives for states to privatise existing assets.

It is perhaps unsurprising, then, that the first planned purchase using GIF I funds is on home soil. A $1.78 billion acquisition of the Iona Gas Storage asset in Victoria, Australia, has been agreed with Chinese power company CLP. Frawley says he is hoping the deal, which will be funded using direct capital from QIC as well as the GIF fund, will close early in 2016.

The sale garnered a significant amount of local press when it was announced in October this year, not least because it was seen as an indicator of the competitiveness of the secondary market for infrastructure assets in Australia. The acquisition price represented a multiple of 40x on the $45.8 million pre-tax profits posted by Iona in 2014. Such multiples are becoming increasingly common. Association of Superannuation Funds of Australia (ASFA) chief executive Pauline Vamos said: "There is a concern that due to competition between funds over good infrastructure assets in Australia, they may be overpriced."

Frawley declined to go into details about how QIC calculated its offer price,

Ross Israel

but warns that there is much more to a valuation than profits. "It's a large purchase," he conceded, but added that the asset was a good one with which to kick off the investment phase of the fund. "We own an existing pipeline from central Australia down to Adelaide on behalf of an existing client already, so we understand the economics and the metrics. Also when you look at the areas that natural storage facility services, there's a lot of population and it's a large and growing population. The economics of that deal and the thematics were strong enough to satisfy us that that was a very good asset."

He said that investments outside of Australia could start taking place from 2016, with deployment and further fundraising happening in tandem. "Fund raising is just one skill. We have to show new investors that we know how to deploy capital as well". Of the fund's 40% foreign allocation, Frawley said QIC is "fairly geographically agnostic. We're looking

Superannuation fund activity

Investment activity of five superannuation fund in Australia during 2015

Name of fund	Transaction Name	Investment	Sector
Australian Super	Perth Airport Refinancing 2015	20.58	Transport
	Etihad Stadium Refinancing	25.95	Social & Defence
	New South Wales Ports Refinancing 2015	354.36	Transport
Retail Employees Superannuation Trust	M5 South West Refinancing 2015	92.24	Transport
	Etihad Stadium	25.95	Social & Defence
HOSTPLUS	Sydney International Convention Centre Refinancing	473.08	Social & Defence
UniSuper	Crown Castle Australia acquisition	382.84	Telecoms
Statewide Super	Etihad Stadium Refinancing	25.95	Social & Defence

in OECD countries across the transport, utilities and energy and PPP space."

US partnership

The fund is not the only way the investor is taking towards a more global approach. In May it formed an A$1 billion Asia-Pacific infrastructure partnership with the California Public Employees' Retirement System (CalPERS), one of the largest public pension funds in the United States.

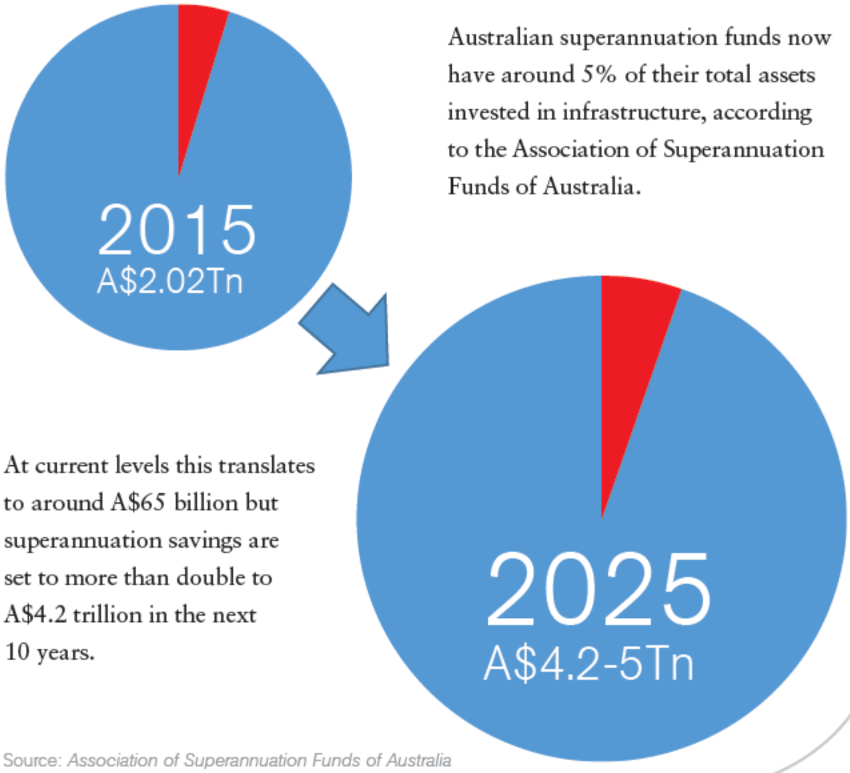
Head of infrastructure Ross Israel told *IJGlobal* it is hoped that the CalPERS investment will help raise the profile of the QIC in the US. QIC also hopes that the presence of a major US fund on its roster will draw in other, smaller US pension funds to their co-investments. "We want this to give credibility to our US strategy. We are well known in Australia, but we want to firmly position ourselves in the US investor universe," Israel said.

The partnership marks not just QIC's increasingly international interests, but those of CalPERS. The tie-up is the pension fund's first Asia-Pacific infrastructure commitment.

Despite the overseas charm offensive, Frawley said there are no immediate plans to create similar alliances in the near term. He favours slow growth. "One of the advantages of us being relatively late to the European and US infrastructure market is that we've had the chance to watch and learn from others," he said.

QIC will face challenges at home as well as abroad. There are significant investment opportunities coming up on home soil, with the upcoming Melbourne port sale and airport privatisations likely to attract attention. Frawley notes however that the market is looking increasingly crowded. "We've got Canadians, we've got Europeans, Middle East, Asians, all bidding for Australian infrastructure." This gives greater justification for expanding internationally. Frawley says QIC will likely take long-standing domestic clients with them into global markets, either as part of GIF or on separate mandates. "We have Australian clients who also need to deploy money into infrastructure. It's

A significant slice of a growing pie



Australian superannuation funds now have around 5% of their total assets invested in infrastructure, according to the Association of Superannuation Funds of Australia.

At current levels this translates to around A$65 billion but superannuation savings are set to more than double to A$4.2 trillion in the next 10 years.

Source: *Association of Superannuation Funds of Australia*

important that they look for opportunities globally, because sometimes they'll get outbid domestically". Superfunds are growing in sophistication to counteract growing competition. Frawley said: "A big theme that is playing out in the domestic super market is around internalisation of investment management and research. There are very large pots of capital that they're managing and there has been a trend of the big funds internalising investment capability". He said that is due to a desire to drive down costs to members and take more control of the investment management.

> "We want to firmly position ourselves in the US investor universe"

QIC are by no means the only Antipodean investors looking further afield. "When you look at equity allocations in balanced portfolios in Australia, the shift from the home country bias that used to exist around Aussie equities has changed significantly in the last few years," Frawley said. "Today the equity bucket in a balanced fund is very much favouring a more global allocation as opposed to just a domestic allocation."

Vamos says the average Australian superannuation fund now has "around 5% of its total assets invested in infrastructure. This is far greater than pension funds in the rest of the world, which have an average of less than 1% of assets invested in infrastructure."

According to Vamos that 5% translate to roughly A$65 billion of investment. Funds also hold investments in listed infrastructure companies and infrastructure debt through their fixed interest portfolios.

This growing confidence in the asset class means superfunds are likely to appear with increasing regularity on transactions around the world. "It's just going to get more global by the day, in terms of where they deploy capital," Frawley concluded. ■