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Pillars for building better
quality investor portfolios...



The role of infrastructure in an alternatives portfolio

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PortfolioConstruction Conference 2006



Important information

Offers of interests in the Challenger Global Infrastructure Fund are contained in the current Product Disclosure Statement (PDS) issued by Challenger Managed Investments Limited: ABN 94 002 835 592 AFSL 234668 which is available on our website www.challenger.com.au and should be considered before making any decision about the product.

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Agenda

- Infrastructure is an attractive investment
 - What is infrastructure
 - Investment returns
 - Investment considerations
 - Investment risks
- Portfolio considerations – listed versus unlisted
- Role of infrastructure in a retail investor's portfolio
 - Contribution to a portfolio
- Challenger can provide infrastructure opportunities
 - Exposure to both listed and unlisted infrastructure

What is infrastructure?

Type	Explanation	Example
Patronage	Patronage is main source of revenue. Limited competition and high entry barriers	Toll roads, airports, communications
Regulated	Regulated returns to monopoly operators of essential services	Power transmission, water
Contracted	Operating assets where the output or capacity is contracted to creditworthy counterparties	Contracted power generation plant
Social	Essential community services	Schools, hospitals
Competitive	Competitive market risk e.g. supply and demand	Certain gas and electricity production

Infrastructure assets are those that underpin basic community services

Infrastructure – investment returns

Asset	Avg return IRR (1)	Cash yields (1-5 yrs)	Capital growth
Toll road (Greenfield)	12-16%	3-5% (2)	Yes
Toll road – operating	8-12%	8-10%	Limited
Airports	10-15%	5-10%	Yes
Broadcast networks	15-20%	8-10%	Yes
Regulated assets	12-18%	8-12%	Limited
Rail	12-16%	8-12%	Limited
PPP	9-13%	6-11%	Limited

Asset return profiles across the investment spectrum are shown in the table

Note

(1) Geared, nominal post tax asset returns

(2) Cash yields from greenfield toll roads are post a construction period of 3-5yrs

Key investment considerations

Location	Political, economic and legal risks
Operational	Originating and leading transactions require a local presence
Currency	Currency and interest rate hedging of foreign returns needs to be carefully managed
Legal systems	Choosing the right legal system flows closely from choosing the right country to invest in
Regulatory environment	The stability and maturity of the regime is an important factor when considering total risk
Supply	Comes down to what investments are available to invest in or can be developed into an investment opportunity

Risks of investing in infrastructure

Gearing	Risk of higher real interest rates can be managed through hedging
Inflation	Regulated assets provide a natural inflation hedge
Credit risk	Either a very wide dispersion (i.e. retail customers) or single exposure to an entity (i.e corporate)
Real tariffs	Regulated assets have revenue certainty
Volume risk	Vary depending on asset
Real cost increases	Regulated assets benefit from regulatory resets which take into account increases in costs
Exchange rate risk	Due to monopoly characteristics tend to be geographically focused
Consortium risk	Alignment of interest b/w shareholders is critical
Liquidity risk	Very illiquid unless bought through a listed vehicle

Summary - attractiveness of infrastructure

- Tendency for strong **predictable** cash flows with relatively low volatility
- **Unique** investment opportunity as the size and complexity of the assets create a natural and sustainable competitive advantage
- **Diversification** can lower portfolio risk – particularly given the relatively low correlation with other asset classes and the economy
- Potential for attractive long-term **capital growth**

Listed versus unlisted infrastructure

Listed	Unlisted
Advantages	Advantages
Easily accessed by retail investors	Can offer lower volatility
Cost of investing is lower than with unlisted infrastructure	Potential to deliver higher returns
Ability to exit investment if require funds	Highly uncorrelated to listed markets
Greater diversification can be achieved	
Disadvantages	Disadvantages
Volatility can be high (particularly over the short term)	Lack of liquidity
Fees can be higher than unlisted investments	Not as easy to access funds
Beta can be high	Risk that demand will outstrip supply

Listed infrastructure

Severn Trent



— Severn Trent

Pennon



— Pennon

Kelda



— Kelda

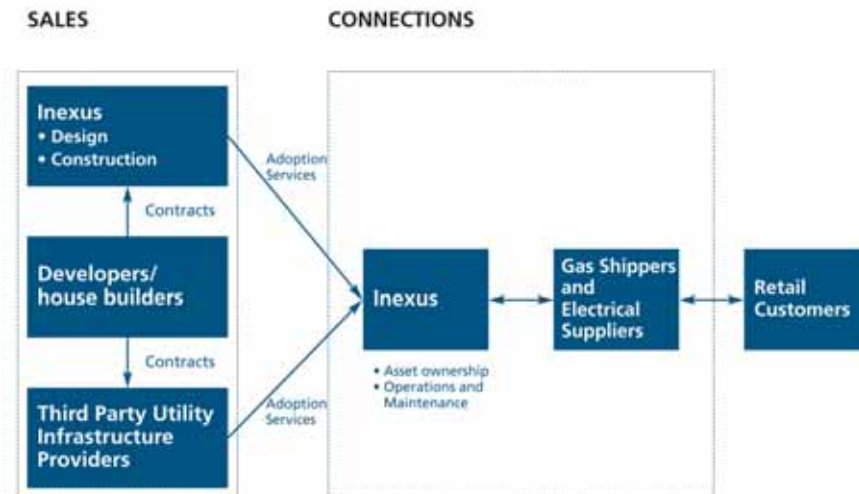
Source: Challenger and Bloomberg



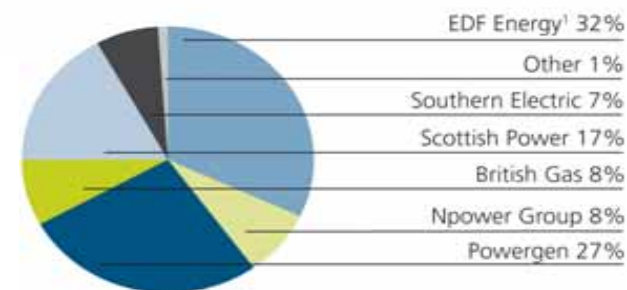
Unlisted infrastructure - Inexus

Inexus is the leading independent gas transporter in the UK

- Revenue is derived primarily from the ownership of the last mile of gas pipes and electricity cables (fully linked to inflation)
- Focuses primarily on providing services to new build domestic housing estates
- Inexus' customers are the gas shippers or electrical suppliers – it has no exposure to retail customers
- Experienced Senior Management team



Key Customers (shippers) – based on 2005 revenues



¹ Comprises London Energy and Seaboard Group

Summary - Listed versus unlisted infrastructure

- An important consideration for portfolio construction is the allocation to listed versus unlisted infrastructure assets, given each has its own characteristics and offers differing benefits and disadvantages to investors

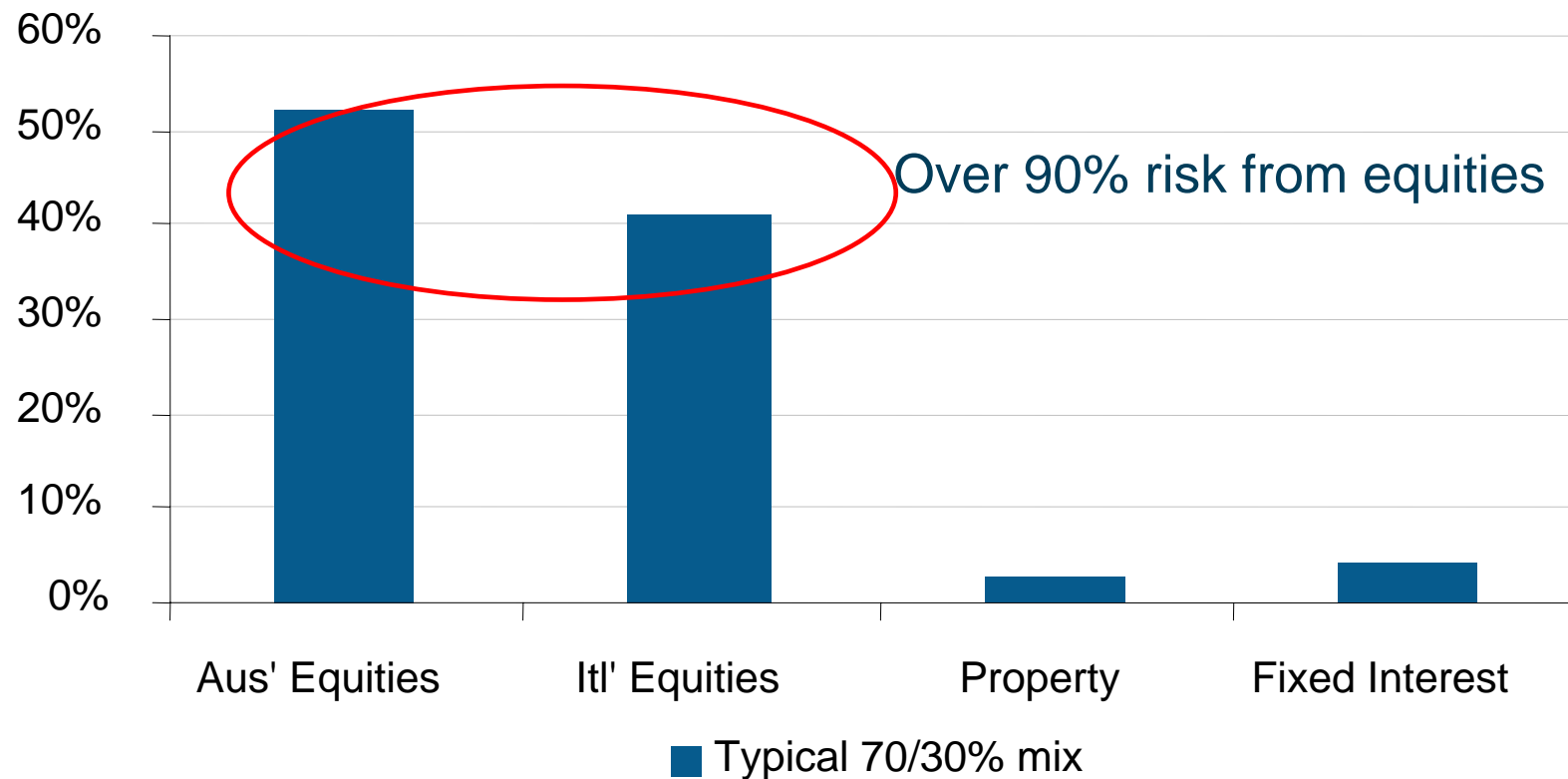
Infrastructure has a role in an investor's portfolio

- “Real diversity” suggests that funds should consider up to a 10% exposure to infrastructure.
- Sub sectors exhibit unique risk/return profiles

Source: Watson Wyatt Worldwide, September 2005

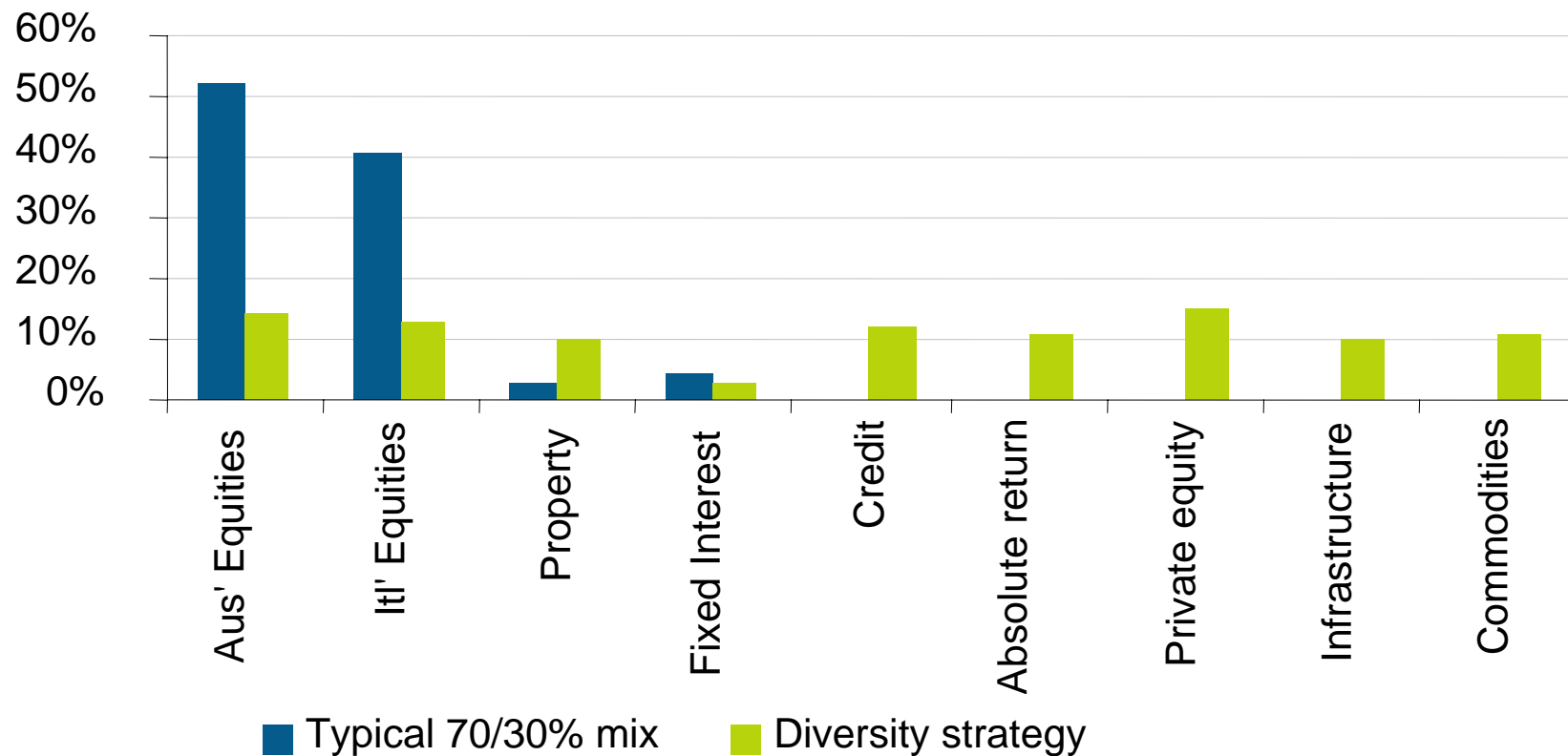
Contribution to a portfolio

Contribution to total fund risk



Source: Watson Wyatt Worldwide, September 2005

Contribution to a portfolio



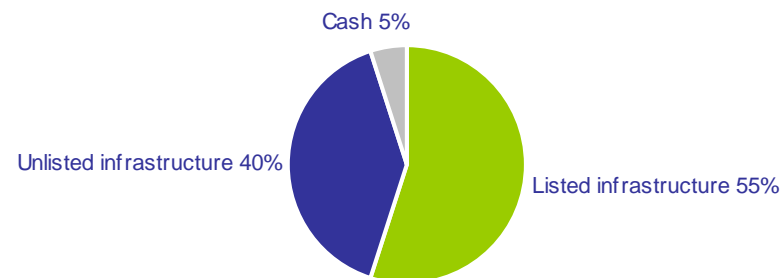
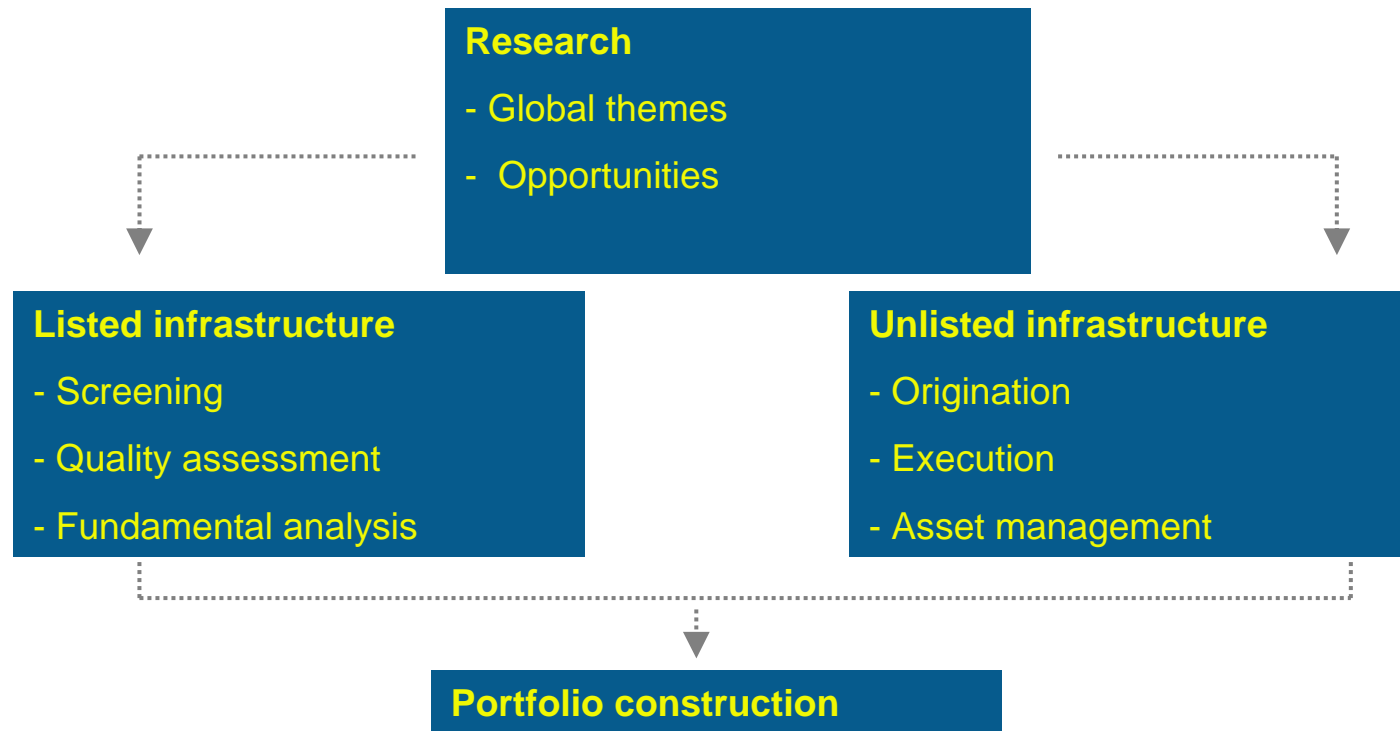
Summary – Infrastructure's role in an investor's portfolio

- Infrastructure is increasingly being viewed as a distinct asset class
- Investors should consider up to a 10% exposure to infrastructure as one component of their overall portfolio

Challenger can provide infrastructure opportunities

- **Challenger Global Infrastructure Fund** launched in May 2006
- Unlisted hybrid vehicle providing **diversified exposure** to listed and unlisted global infrastructure investment opportunities through a single investment
- The Fund will invest in quality unlisted global infrastructure assets as opportunities arise

Investment process



Key benefits of the Fund's approach

The Fund seeks to achieve the following:

- **Diversification** across listed and unlisted infrastructure assets and across industry sectors and geographically through a single investment
- **Meaningful exposure** to listed and unlisted investment opportunities available in the sector, many of which are difficult to access
- A **flexibly** managed investment, covering a diverse range of assets
- **Synergies** from researching and investing in both listed and unlisted sectors
- **Liquidity** facilitated through listed infrastructure investments, rather than via a larger exposure to cash
- Reliable **income stream** with opportunity for long-term **capital growth**

Summary - Challenger can provide infrastructure opportunities

- Challenger Global Infrastructure Fund provides exposure to both listed and unlisted infrastructure
- Assets in the portfolio are selected for their ability to provide a steady income, to provide diversification across countries and industries, and to make the most of growth opportunities along the way

Conclusion

- Infrastructure has **emerged** as a new asset class
- Exposure to infrastructure offers many **benefits** from a portfolio construction perspective
- Infrastructure is generally a **yield-generating asset class**, therefore it can be used as part of the **defensive component** within an investor's portfolio
- The unlisted Challenger Global Infrastructure Fund has been designed to make it **easy** for investors to gain exposure to this important sector

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Gizmo time

Which session are you in?

1. PIMCO
2. Principal Global Investors
3. Colonial First State
4. Deutsche Asset Management
5. Challenger Financial Services

Gizmo time

Please rate the overall quality of this session...

1. awful
2. Poor
3. Mediocre
4. Good
5. Very good
6. Great!



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