Strategy Update: 30 September 2018

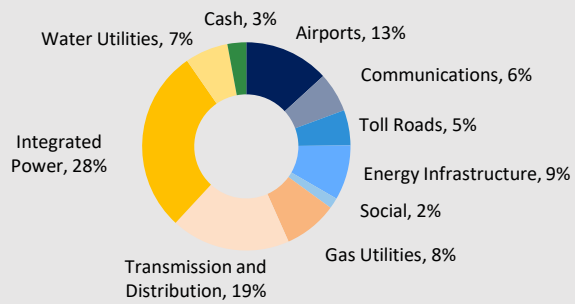
Magellan Core Infrastructure (AUD Hedged)

Portfolio Manager	Strategy Inception Date	Total Strategy Assets	Total Infrastructure Assets [1]
Gerald Stack	17 December 2009	AUD $6,224.4 million	AUD $11,290.8 million

Objective	Approach
Capital preservation in adverse markets	Diversified rules-based portfolio applying our proprietary infrastructure classification
Pre-fee return of CPI plus 5%p.a. through the economic cycle	Benchmark unaware
	Highly defensive, inflation-linked exposure

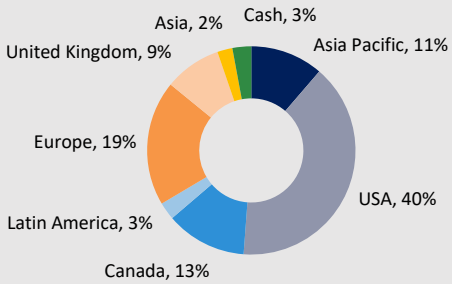
Top 10 Holdings[2]	Sector[2]	%
Fortis Inc	Transmission and Distribution	3.0
National Grid PLC	Transmission and Distribution	3.0
Aena SME SA	Airports	3.0
Transurban Group	Toll Roads	2.8
Sydney Airports	Airports	2.8
TransCanada Corp	Energy Infrastructure	2.8
Enbridge Inc	Energy Infrastructure	2.7
Power Assets Holdings	Integrated Power	2.3
Red Electrica De Espana SA	Transmission and Distribution	2.3
Snam Rete Gas SpA	Gas Utilities	2.2
	TOTAL:	26.9

Sector Exposure[2]



AUD 5 Year Risk Measures[4]	Against Benchmark[5]	Against Global Equities
Upside Capture	1.2	0.6
Downside Capture	0.9	-0.2
Beta	0.9	0.3
Correlation	0.9	0.3

Geographical Exposure[2]



Cumulative Performance[3]	3 Months (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)	7 Years (% p.a.)	Since Inception (% p.a.)
Composite (Gross)	-0.4	1.1	9.5	12.9	14.1	14.3
Composite (Net)	-0.6	0.4	8.7	12.1	13.3	13.5
Global Infrastructure Benchmark	-1.5	-1.1	7.9	8.9	10.5	9.0
Excess (Gross)	1.1	2.2	1.6	4.0	3.6	5.3
MSCI World NTR Index Hedged to AUD	5.5	12.9	14.7	12.5	15.8	12.8

Annual Performance[3]	CYTD (%)	2017	2016	2015	2014	2013	2012	2011	2010	2009*
Composite (Gross)	-1.0	15.4	10.6	7.9	28.0	16.7	16.3	15.6	15.9	1.9
Composite (Net)	-1.5	14.6	9.8	7.2	27.1	15.8	15.5	14.8	15.1	1.9
Global Infrastructure Benchmark	-2.6	14.4	14.1	-5.4	22.9	18.5	9.1	4.7	5.7	0.9
Excess (Gross)	1.6	1.0	-3.5	13.3	5.1	-1.8	7.2	10.9	10.2	1.0
MSCI World NTR Index Hedged to AUD	6.9	19.8	10.4	3.8	12.3	31.8	18.8	-2.3	12.6	1.1

1 Comprised of all Infrastructure Strategies.
2 The data is based on a representative portfolio for the strategy. Refer to the GIPS Disclosure below for further information. Sectors are internally defined. Geographical exposure is by domicile of listing.
3 Returns are for the Core Infrastructure Hedged to AUD Composite and denoted in AUD. Performance would vary if returns were denominated in a currency other than AUD. 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.
4 Risk measures are for the Core Infrastructure Hedged to AUD Composite before fees. The Global Equity Index is the MSCI World NTR Index (hedged in USD).
5 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 (hedged to AUD) and from 1 January 2015 onwards, the benchmark is the S&P Global Infrastructure NTR Index (hedged to AUD). Note: the UBS Developed Infrastructure and Utilities NTR Index (hedged to AUD) ceased to be published from 31 May 2015, replaced on 1 January 2015 with the S&P Global Infrastructure Index NTR (hedged to AUD).
* Returns are only for part year.

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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 (AUD Hedged) and from 1 January 2015 the benchmark is S&P Global Infrastructure Net Total Return Index (AUD Hedged). The benchmark changed because UBS discontinued their index series.
The UBS Developed Infrastructure & Utilities Index Net Total Return (AUD 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 (AUD 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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For the purpose of complying with GIPS, the Firm is defined as all discretionary portfolios managed by MFG Asset Management.

The Global Core Infrastructure Hedged in AUD composite is a global strategy investing in strictly defined or "pure" infrastructure companies (typically 80-120). The filtered investment universe is comprised of stocks that 1. generate reliable income streams, 2. benefit from inflation protection and 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 composite is 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 negative return over the quarter.

The biggest detractor was Atlantia following the collapse of a bridge on a tolled road in Genoa. The bridge that collapsed was a tolled section of the A10 motorway that was operated under a concession contract by Autostrade per l'Italia, an 88% owned subsidiary of Atlantia of Italy. The newly formed left-right populist Italian government blamed Atlantia for being derelict in its duties to maintain the bridge. The government appears to have commenced a process that could lead to it revoking the single concession that governs Autostrade per l'Italia's toll-road network in Italy. We have removed Atlantia from the portfolio following internal analysis, including meetings with Italian legal and political experts, that led us to conclude that the range of financial outcomes that Atlantia faces is wide. Thus, we no longer believe the financial returns to shareholders are as reliable and predictable as we require of stocks held in the strategy given our central tenet of capital preservation.

Other stocks that lagged on a contributions basis included the investments in National Grid of the UK and Enbridge of Canada. National Grid lost 5.6% after upheavals in the ruling Conservative Party over how the UK might leave the EU raised the prospect of the UK having a Labour government that has said it would nationalise utilities, possibly at a price well below the prevailing market value of these stocks. Enbridge fell 10% over a quarter during which the oil and gas pipeline operator said it would spend about US$7.1 billion (in new shares) to buy shares it doesn't own in three North American units so as to simplify its corporate structure.

The stocks that contributed the most included the investments in Grupo Aeroportuario del Sureste of Mexico and PG&E and Edison International of the US. Aeroportuario del Sureste rallied 21% on higher traffic numbers – passenger traffic in the company's nine Mexican airports rose 4.8% in the second quarter to 8.3 million. PG&E gained 8.1% and Edison rose 7.9% after Californian lawmakers in September passed a law that will help these utilities pay for billions of dollars of liabilities possibly incurred when power lines were blamed for fires that damaged the state last year.

Key Stock in Focus – Atmos Energy

Atmos Energy: The natural gas company stands out because its high earnings growth is unusual for a utility.

The US sources just under 30% of energy needs from natural gas whose cheaper price and environmentally friendly traits are expected to increase demand for an energy source that comes out of the ground clean, ready to use and can be easily transported to customers presuming the network is up to standard.

Natural gas, as an essential service, is regulated. The 'regulatory compact' is that utilities are deemed the sole provider in an area and are assured of a reasonable return on their investments (termed the 'rate base' in industry jargon). As such, US regulators allow gas utilities to increase the price of connections in small steps over time to compensate for the money spent on equipment. To smooth their returns, regulators allows gas utilities to pass on costs. These costs include operational and maintenance expenses and, crucially, the cost of natural gas – thus, customers bear the cost if gas prices climb but gain the benefit when gas prices fall. (In Australia, gas utilities can't automatically pass on fluctuations in the gas price.) The certainty of returns makes US natural-gas utilities an attractive risk-reward proposition for investors.

But there's one major issue with natural gas in the US. The network needs upgrading. Most of the pipes that transport gas across the US are old. Parts of the network could prove dangerous because leaky gas is flammable. In 2010, a gas explosion in the San Francisco suburb of San Bruno sent flames more than 1,000 feet (300 metres) high and eight people died when their homes where engulfed in fire. Understandably, a nationwide push is underway in the US to upgrade old gas pipelines. But it takes time and money.

This is the industry context in which to place Atmos Energy, the US's largest fully regulated natural-gas-only distributor. The Dallas-headquartered company that earned US$1.2 billion (EBITDA) profit in fiscal 2017 distributes gas to more than three million homes and businesses in eight southern US states via a network that is 70,000 miles (115,000 kilometres) long. Most of Atmos's activity is centred in Texas, where the company is the largest gas distributor. In addition, the company operates one of the biggest intrastate gas transmission pipelines in Texas and manages storage assets.

Of prime importance is that Atmos is spending US$8 billion from 2018 to 2022, about 80% of which will be used to upgrade its pipelines. This means the company's rate base is expected to nearly double over that time and regulators will be more amenable to agree to higher prices on Atmos connections. Atmos's plan to eventually overhaul about 40% of its pipeline network make the company one of the most compelling long-term investment opportunities among utilities in our universe, which we limit to the most reliable of utility and infrastructure stocks.

The company does have its challenges. A low-risk stock with a steadily rising earnings outlook that offers income streams (a dividend stock) is more vulnerable to rising interest rates. Atmos estimates that 6,100 miles (9,800 kilometres) of its pipeline warrant immediate replacement. To emphasise the danger, leaks from the ageing pipelines earlier this year forced people in Dallas to evacuate their homes. Such incidents have fortunately been rare and serve to highlight why Atmos must make its ageing network safe and efficient. The company, which has exceptional safety record, can look forward to years of regulatory-sanctioned price increases on a larger rate base. The fact that Atmos is not exposed to shifts in gas prices or changes in demand (say, a warm winter that leads to lower heater use) makes the company a low-risk investment.

Old company, old pipelines

Atmos can trace its history back to 1906 in Texas, which holds significance for the age of its pipelines. The company estimates that 29,000 miles (47,000 kilometres), or 42%, of its network was built before 1970 when the US first passed regulations imposing minimum standards on gas pipelines. About 13,000 miles (21,000 kilometres) of Atmos's pipelines were made before 1940.

The company operates as three arms: the regulated distribute division that delivers gas, the regulated pipeline segment the handles the transport and storage of gas, and the non-regulated division that services customers.

Atmos's plan to replace the ageing steel, cast iron and plastic pipelines is expected to lead to price increases that will ensure earnings growth of about 6% to 8% p.a. on a rate base that will nearly double in five years. We estimate that Atmos's 'rate base' will nearly double in value from US$6.6 billion in 2017 to US$11.8 billion in 2022 due to its investment program as it replaces about 750 to 1,125 miles (1,200 to 1,800 kilometres) of old pipelines each year over the next five years.

Even after about 6,000 miles (9,600 kilometres) of pipeline are upgraded over the next five years, that will still leave about 22,000 miles (35,000 kilometres) of network to be upgraded after 2022. This suggests that the company will keep spending money to upgrade its network and generate earnings growth for at least for the next 25 years. That means investors can look forward to steadily rising profits from a company that has proved reliable for investors in recent decades.

The company has delivered 34 consecutive years of higher dividends and 15 years of growth in earnings per share. It targets annual earnings growth of 6% to 8% and a dividend yield of about 2%. The popularity of natural gas and the company's capital expenditure are likely to add to Atmos's record of keeping happy its investors.

Sources: Company filings and website.