World Pensions Council
The International Association of Pension & Social Security Funds

ARPINGE S.P.A. Press Conference

'Pension Investment in Real Assets'

Wednesday **10th September 2014**

Auditorium dell'Ara Pacis **– Rome**

Pres. by **M. Nicolas J. Firzli**, Director-General & Head of Research, **World Pensions Council**

I. Macro/Policy Context: 'Age of Austerity'… + Views of Supranational Thought Leaders

II. Pension Investment in Infra: Facts & Figures from Leading Jurisdictions (US, Can., Aus.)

III. WPC-SLGE Infrastructure vs. Other Real & Non-Listed Assets Mapping

IV. Pension Infra Investment "Platforms" or Other Pooled Vehicles: Australia, UK, (large/established) and New Developments in the US, Holland, World Bank GIF…

V. Why Infrastructure Makes (a lot of) Sense for Pension Funds: "*Self-Interested*" Financial Economics Utility of Real Assets

I. Macro/Policy Context: 'Age of Austerity'… + Views of Supranationals

- only the beginning: longevity risk combined w/ *'durably low(er) returns'* across 'cla
  → more difficult for pension schemes to reach funding levels e.g. by 2024 in Italy '

- 1945- 1949 "1st Age of Austerity" short hiatus: Treaty of Paris (1951) and Marshall Plan (1948-1952) restarted world growth engine → Unlikely to happen this time as we're faced with a "perfect storm"
  - US unable.., EU div. & exp.., EM growth pains e.g. Brazil 2013 riots started by transport infra crisis
  - … INT. RATES DURABLY LOW → ECB, FED QE "*KILLING PENSION RETURNS*" (Firzli, 2012)

La svolta di Draghi spinge la corsa ai bond

Spread ancora in calo a 132 punti, euro a 1,296 dollari

La liquidità messa sul piatto dalla Bce con le ultime misure sta indirizzando gli investitori sui bond dell'Eurozona, in particolare i Paesi periferici: lo spread BTp-Bund è sceso a 132 punti, con il decennale italiano che rende il 2,25%, minimo storico; i Bonos spagnoli sono al 2,04% mentre i tassi dei bond irlandesi sono negativi fino alle scadenze biennali. Borse tiepide, euro a 1,296 dollari.

Lops, Mancini e Merli › pagina 3

L'ANALISI

Se la Bce toglie peso al rating dei Buoni

di Vittorio Carlini

Ann. Return–Northern Hemisphere PF
60% Bonds + 40% Stocks (Listed Eq.)

- **1982-2007: ARR ≈ 9.0% p.a.**
- **2007-2013: ARR ≈ 3.5% p.a.** *gross*
  … w/o counting management fees
  barely ≤ 2.% US CPI Inflation

- World Bank: Infra part of "WDI" indicators started in 1997 …. But no much reflection/action on PF investment in real assets until 2013/2014 when started devising the soon-to-be launched GIF platform
  - G. Inderst & F. Stewart pol.paper : "*challenges fr. stretched gov. finances, restrict. on bank lending*"

- OECD: seminal 2009 paper "*Pension Fund Investment in Infrastructure*" by G. Inderst for OECD PPU
  - "*Data explaining the size, risk, return and correlations of this diverse asset class is therefore limited, making PF investors cautious…. Involves new types of invest. vehicles and risks to manage* "

- EU Comm. ECFIN Dir. and EIB w/ Italian thought leaders Marco Buti (DG) and G. Chiarion Casoni ("L3)
  - Initially EU member-states no interest ! → No much the EU Comm. could do!
  - 2014: Changing for the best ⟶ EIB + leeway to facilit. and co-finance deals w/ PFs

II. Pension Invest. in Infra: Facts & Figures fr. Leading Jurisdictions

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- "Core" traditional invest. ↔ bonds & stocks still account for the vast majority of AuM > 92% (Mainland) Europe, Japan "responsible" for the preservation of the *old asset alloc. status quo*

- "Alternative invest." incl. "Real Assets & Infrastructure" = still in minority / in most cases < 8%

- Early entrants = Canada, Australia + few cash-rich US states/cities Alaska, Texas, California

- Why Them? "…*large, resource-rich, and under-populated req. massive infra spending since mid-19th century, **FAMILIARIZING** Govt. and private sector early w/ **COMPLEX** financial, tech. and legal processes underpin. infra. investments…*" (Firzli & Bazi 2011)

- US = global trend setter The world is changing, and it's changing fast : in past ten years, large US PFs increased avg. alloc. to alternative invest include infra fr ≈ 5% to ≈ 17%+ *remarkable* Δ

- In Canada, Australia, large US states/municipalities, % allocated to Real Estate is generally equivalent to (or a little bigger than) % allocated to Infrastructure and Private Equity

  ≠ Italy and other European countries where Real Estate is dominant "non-traditional" asset

- PENSION FUNDS ≈ 40% of all investors in infra asset class, excluding projects directly funded & developed by Govts, munies and public authorities → N°1 INVESTOR categ. > insurers, SWFs…

III. Infrastructure vs. Other Real & Non-Listed Assets Mapping

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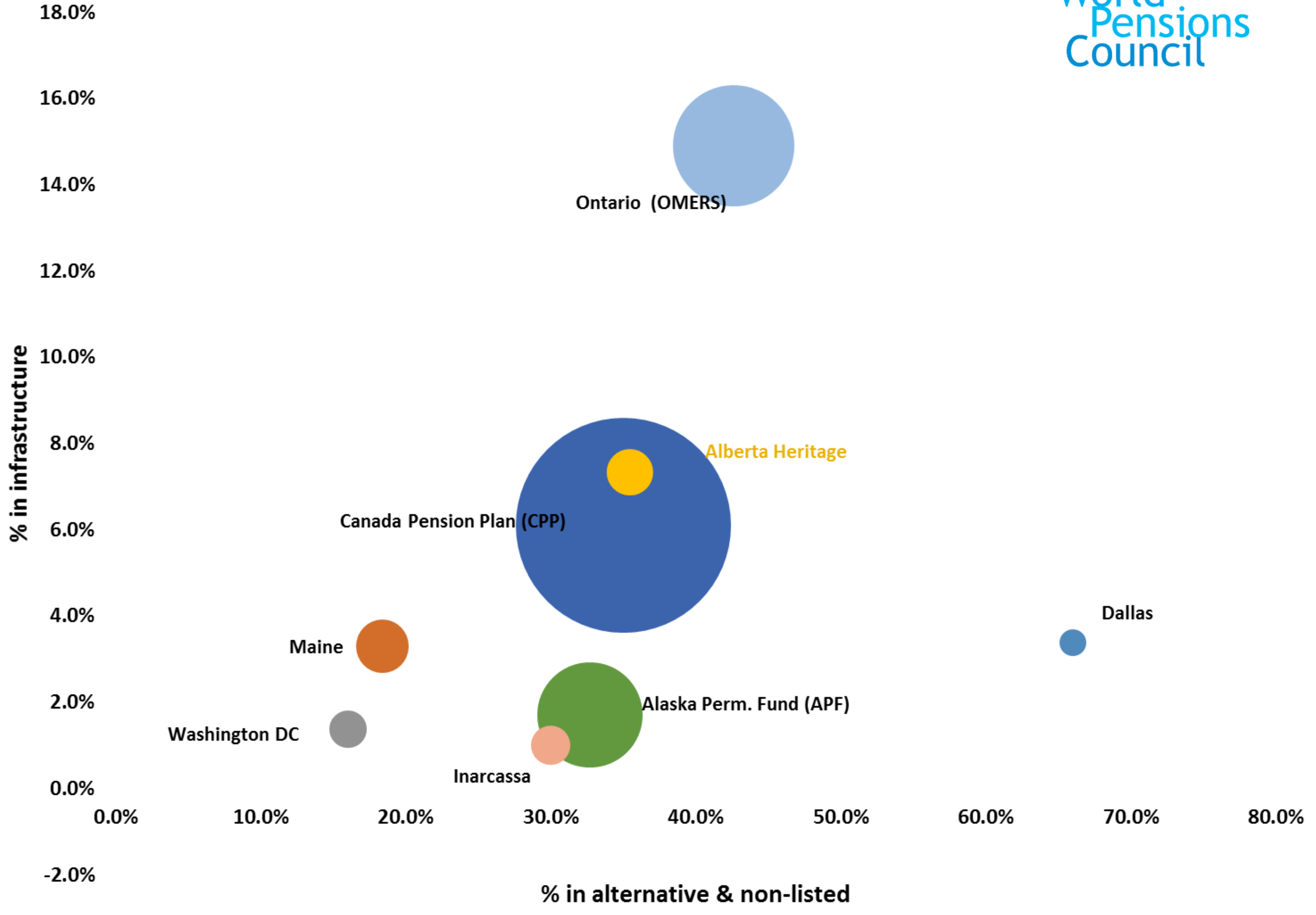

IV. A Look at Some Pension Infra Investment "Platforms" : UK, Australia, US, Holland, World Bank GIF…

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Large Can. and US pension funds either enter/make deals directly or externalize (all or parts of) their infra investments to asset managers (typically Aus. or US or Fr. Companies)

- **Australia/IFM started initially as a "platform" of sorts**
  - **Founded in 1995 by a group of pension funds (called "*superannuation funds*"** in Australia)
  - **Initially only invested domestically in Aus. with "moderate profits" collaborative ethos**
  - **Today: still owned by nonprofit Aus. pensions… but invests globally w/ "capitalist" approach**
  - **40 billion € under management incl. ≈ 15 billion € infra equity funds** (typically concessions)

  ⟶ *must be viewed as a private-sector asset manager*, not a "platform" (anymore)

- **UK/Pensions Infrastructure Platform (PIP)**
  - **Established in 2012 after 2 years+ of high-level consultations and ardent support of Prime Minister David Cameron (delivered more than 20 speeches on the topic!), NAPF and PPF**

    → "top-down", centralized pol. Initiative + wanted to "start big" → built bureaucratic balloon
  - **Fairly expensive cost-structure = quite ironic for a large non-profit platform…**
  - **Initially v. ambitious, planned to raise "*more than £ 2 billions+ by end 2013*"**
  - **As of today (2014), only raised ≈ approx. £ 400 millions …**
  - **Q1 2014: 3 of 10 "founding" investors pull out abruptly = BT, BAE (private sector) and LPFA → sending paradoxically neg. signal… at time when the class is taking off in the UK!**

- **Other/smaller infra platforms being formed in EU Holland (NII), Italy (Arpinge), in US (FII Pilot), globally World Bank (GIF) = BETTER DESIGNED & MORE COHESIVE, learning fr. UK's mistakes**

V. Why the Asset Class Makes (a lot of) Sense for Pension Funds

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INDUSTRIAL ECONOMICS :

- PF favor "sec." infra assets ≠ not green-field/new projects w/ sizeable construction unknowns
- "Regulated" A.C. (price + vol. reg) → "last refuge" of fin. predictability in volatile deregulated

COUNTRY RISK :

- AAA long-dated govt. bonds rare (no much debt iss. > 10 yr.), int. rates durably low and "counter-ex." Greece, Portugal … → like "REAL asset" OWNERSHIP/30 years+ concessions

ACTUARIAL AND FINANCIAL ECONOMICS :

- De-correlation fr. traditional assets (FI, Eq.) → stat. div. & improve. of overall ptf. risk/return
- By definition, pension funds need to
  - Protect long-term val. of invest. fr. inflation debasement of currency & market fluctuations
  - Provide recurrent, stable cash flows to pay for retiree benefits in the long term
- Infrastructure is an IDEAL ASSET CLASS provides tangible advantages incl. long duration - thus facilitating CASH FLOW MATCHING w/ long-term liabilities

→ Drivers MOST RAPIDLY GROWING ASSET CLASS ≈ $ 85bn today, $ 35 bn invest. by pensions

→ Finally attracting the attention of smart supra. policy-makers

e.g. Apr. 2014 M8 Road Project in Scotland = Infra Debt on greenfield project with EIB, GEC Pension, Allianz GI behalf of UK PF clts.