MFG Select Infrastructure

Strategy Update: 31 December 2013

Portfolio Manager	Total Infrastructure Assets[1]
Dennis Eagar/Gerald Stack	USD $3,350.5 million / GBP £2,022.9 million
Inception date	Composite Size[2]
1 July 2007	USD $485.6 million / GBP £293.2 million

AUD Hedged Gross Performance[2]

	Composite %	Index %[3]	Excess Return %
1 Month	1.8	1.4	0.4
3 Months	5.6	3.7	1.9
6 Months	9.2	7.7	1.5
1 Year	19.1	18.5	0.6
2 Years (p.a.)	18.0	13.7	4.3
3 Years (p.a.)	16.1	10.6	5.5
4 Years (p.a.)	15.3	9.3	6.0
5 Years (p.a.)	17.3	9.5	7.8
Since Inception (p.a.)	6.6	3.0	3.6
Since Inception	51.8	21.3	30.5

Top 10 Holdings[4]

	Sector	% of Strategy
Transurban Group	Toll Roads	9.0%
Fraport	Airports	7.3%
Atlantia	Toll Roads	6.7%
National Grid	Transmission and Distribution	6.5%
SES	Communications	6.0%
Zurich Airport	Airports	5.3%
Auckland Airport	Airports	5.3%
Enbridge	Energy Infrastructure	4.0%
Sydney Airport	Airports	3.3%
Spark Infrastructure	Transmission and Distribution	3.2%

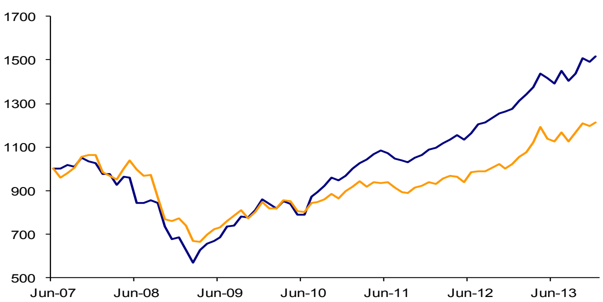
AUD Hedged Gross Performance - Calendar Year[2]

	Composite %	Index %[3]	Excess Return %
2007 (part year)	2.7	6.5	-3.8
2008	-33.4	-27.5	-5.9
2009	25.5	10.0	15.5
2010	13.0	5.7	7.3
2011	12.4	4.7	7.7
2012	16.8	9.1	7.7
2013	19.1	18.5	0.6

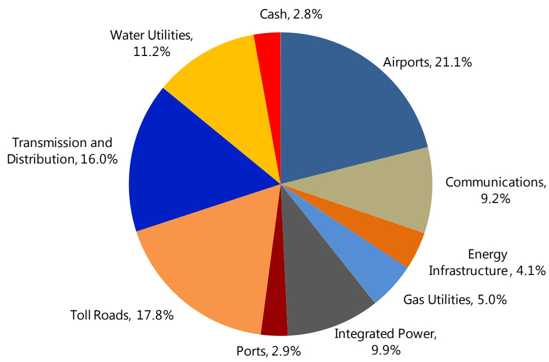
AUD Hedged Risk Measures Since Inception[2]

Upside Capture	0.9
Downside Capture	0.7
Beta	0.8
Information Ratio (p.a.)	0.4
Tracking Error(p.a.)	9.4%
Worst Drawdown - Composite	-45.6%
Worst Drawdown - Index[3]	-37.4%

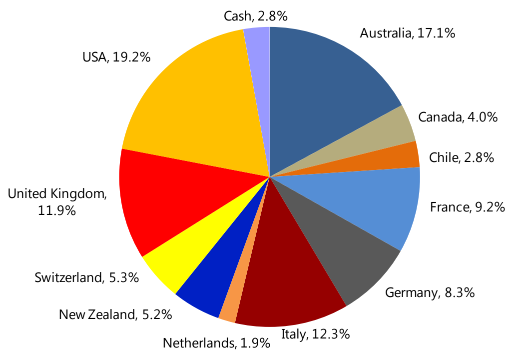
Performance Chart Growth of AUD $1,000



Industry Exposure[4]



Geographical Exposure[4]



[1] Comprised of the total Firm Infrastructure assets, comprising the Select Infrastructure strategy and Core Infrastructure strategy.
[2] Returns and risk measures are for the Select Infrastructure Hedged in AUD Composite. *Refer overleaf for further information.
[3] Index: UBS Developed Infrastructure & Utilities Net Total Return Index (Hedged to AUD) Source: UBS
[4] Representative Portfolio. ^Refer overleaf for further information.

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Strategy Commentary

As at 31 December 2013, the portfolio consisted of 30 stocks. The top ten investments represented 56.5% of the strategy at 31 December 2013.

The major sector changes to portfolio composition during the period were a reduction in exposure to US utilities offset by an increase in the weighting of European transport infrastructure stocks. Over the course of the year we have found utilities in the better performing economies of the world (effectively the most defensive infrastructure investment opportunities) to have become progressively more expensive relative to other opportunities in the infrastructure investment universe. Accordingly, we have reduced the exposure to regulated utilities in the USA, and increased our exposure to airports and toll roads in Europe.

The last 12 months have witnessed the share-price recoveries of the utilities and infrastructure sectors that are often included in broader market definitions of infrastructure investment universe, but are outside the universe of stocks that we consider investment grade. These sectors, European integrated utilities with significant exposure to unregulated power generation and Japanese electric utilities, have been poor investments in previous years reflecting their inability through this period to generate reliable earnings.

The Risk of Increasing Interest Rates

In our view, the major risk currently faced by infrastructure and other asset classes is the impact on global money flows and bond yields as a result of the end of the quantitative easing programme (QE) run by the US Federal Reserve (Fed).

The past six months has witnessed a broad increase in underlying interest rates as investment markets have turned their focus to the prospect the Fed will end QE in the next couple of years. We expect interest rates to continue to rise over the medium term. Increasing interest rates represent a challenge for all investment classes and, whilst better placed than many asset classes, infrastructure is not immune from these risks. While prevailing interest rates have been well below historical averages since the global financial crisis, we do not believe that long-term infrastructure investors made their investment decisions during the period based on prevailing interest rates, but on a higher, more historically normal level of interest rates. As a consequence while increasing interest rates represent a risk for investors in infrastructure assets, we believe that the risk over the medium to long term is not that interest rates rise from present levels, but rather that they rise materially above “normal” levels.

The risks posed by an increase in interest rates are somewhat different for utilities as compared to infrastructure assets.

- **Utilities:** Utilities operate under a compact with their communities under which they provide reliable, efficient services while investing for the future. In return, the utility is able to earn a fair return on the capital invested in its operations. Utilities are not able to exploit their natural monopoly power but are protected from the fluctuations of the economic cycle and from changes in variables outside their control, such as interest rates. Ultimately, the key determinant of the level of returns generated by regulated utilities is the return approved by the utilities’ regulator and, therefore, an increase in interest rates should lead to an increase in the approved rate of return, ensuring that the utility continues to be able to earn a fair return. However, a utility can suffer because of mismatches and lags between the increase in interest rates and the subsequent increase in the approved regulatory return. Regulatory rates of return have been sticky as interest rates have declined and we expect that there will also be stickiness as interest rates rise.

- **Infrastructure:** Infrastructure assets typically have an ability to pass through the effects of inflation through the price of the service provided; e.g. tolls on a toll road are normally linked to inflation. However, where an increase in interest rates is not accompanied by an increase in inflation, the cost of the debt can be expected to rise (with a lag if the debt interest costs are hedged), reducing the returns available to investors.

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Performance is compared to the UBS Developed Infrastructure & Utilities Index Net Total Return (Hedged to AUD) which 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.

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The Magellan Select Infrastructure composite is a global strategy investing in strictly defined or "pure" infrastructure companies (typically 80-120). The composite is hedged to Australian dollars with forward contracts.

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 list of composites and descriptions, as well as policies for valuing investments, calculating performance, and preparing compliant presentations are available upon request by emailing data@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.

Industry and Geographical Exposures are calculated on a look through basis based on underlying revenue exposure of individual companies held within the portfolio

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