



# Brookfield Infrastructure Partners L.P.

## 2013 Third Quarter Conference Call Transcript

**Date:** Wednesday, November 6, 2013

**Time:** 9:00 AM ET

**Speakers:** **Tracey Wise**  
VP, Investor Relations

**Bahir Manios**  
Chief Financial Officer

**Sam Pollock**  
Chief Executive Officer

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## **OPERATOR:**

At this time, I would like to turn the conference over to Tracey Wise, Vice President, Investor Relations. Please go ahead, Ms. Wise.

## **TRACEY WISE:**

Thank you, Operator, and good morning. Thank you all for joining us for Brookfield Infrastructure Partners' Third Quarter 2013 Earnings Conference Call. On the call today is our newly appointed Chief Financial Officer, Bahir Manios, who will review our financial results, and key business and operational highlights, Sam Pollock, our Chief Executive Officer, who will discuss our growth initiatives and the outlook for our business. Following their remarks, we look forward to taking your questions and comments.

At this time, I would like to remind you that, in responding to questions and in talking about growth initiatives and our financial and operating performance, we may make forward-looking statements. These statements are subject to known and unknown risks, and future results may differ materially. For further information on known risk factors, I would encourage to you review our Annual Report on Form 20-F, which is available on our website. With that, I would like to turn the call over to Bahir.

## **BAHIR MANIOS:**

Thanks Tracey and good morning everyone.

In my remarks I will focus on FFO, which is a proxy for cash flow from operations. I will also focus on AFFO yield which is a measure of how effectively we deploy our capital.

Our results this quarter were strong as virtually all of our operations performed better than the prior year. Organic growth across most of our businesses and incremental earnings on capital that we deployed over the past 12 months more than offset the impact of asset sales. Funds from operations ("FFO") for the quarter were \$167 million, or \$0.80 per unit, representing year-over-year increases of 48% and 38%, respectively. We generated an AFFO yield of 12% and our payout ratio remains conservative, currently at 59%, which is below our long-term target range of 60%-70% of FFO.

Our utilities business generated FFO of \$97 million in the period, compared to \$80 million in the third quarter of 2012. The increase was primarily due to the impact from the investments made in our UK regulated distribution business and our Chilean electricity transmission system at the end of last year. Excluding the contribution from these investments, our underlying performance was solid, benefiting from inflation indexation, additions to the rate base of our existing operations, as well as lower financing costs.

We also continue to advance a number of priorities in our utilities business. During the quarter, we closed on a \$150 million financing at our Chilean Transmission business which related to an expansion project we commissioned earlier this year. The financing was completed at an attractive rate of 225 basis points over LIBOR and maturing in 2028. In October, we commissioned the second segment of our Texas transmission system which we expect to have fully commissioned into the rate base by the end of the year. In addition, it has been a year since we successfully completed the acquisition and recapitalization of Inexus where our primary focus has been on integrating the business with our existing UK distribution business

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and realizing cost synergies. We have achieved nearly 70% of these savings and are continuing to implement our business plan to achieve the balance. We are also seeking to leverage and cross sell Inexus' service offerings by introducing product lines such as fibre to home to our existing customers. We made strides on this front during the quarter as we completed several fibre network sales, which we hope will position us well for future growth.

Our transport platform generated FFO of \$82 million in the third quarter of 2013, compared to \$40 million in the prior year period. The significant increase in FFO was driven by the commissioning of our Australian railroad's expansion program, the final portion of which was commissioned in March 2013 as well as higher contribution from our toll road business, where we have made significant investments over the past 12 months.

In September, we completed a R\$600 million debenture issuance at one of the state roads in our Brazilian toll road business, to repay existing debt that was more expensive. The five-year debenture was priced at 109 basis points over the Brazilian Interbank deposit rate and achieved a solid investment grade rating from Moody's.

During the quarter, we invested a further \$500 million into our Brazilian toll road platform, increasing our ownership to approximately 31%. The business has performed well since our initial acquisition in December 2012, and in the past year invested over R\$500 million of growth capital to widen its roads, which is expected to facilitate higher traffic going forward. We were pleased to be able to add to our interest in this high quality business which has attractive long-term growth potential.

Our energy platform earned FFO of \$14 million in the current quarter which was consistent with the third quarter of 2012. Contributions from our recently acquired district energy system in Toronto were offset by lower results at our natural gas transmission system which continues to be affected by weak market fundamentals in the North American natural gas market.

Our district energy business is currently advancing several growth initiatives. During the quarter, we completed the connection of a commercial office property in downtown Toronto to our system and made substantial progress with development plans relating to two additional buildings that we expect to have connected by the end of next year. In August, we acquired district energy systems in Houston and New Orleans which we are currently progressing the necessary consents for and anticipate closing for this transaction in the fourth quarter. In addition to providing attractive risk-adjusted returns, we believe that the added technical expertise that we gain from this acquisition will aid us in growing this platform. We remain optimistic about our ability to expand our district energy platform organically and through acquisitions in the years ahead by utilizing a proactive approach to acquiring systems from corporate, municipal and institutional owners where these operations are not core to their main activities.

I will now turn the call over to Sam to walk through our growth initiatives and outlook for our business.

**SAM POLLOCK:**

Thanks Bahir.

I'd like to begin my remarks by addressing an issue that I have been asked about a lot recently and that is the potential impact that rising rates may have on Brookfield Infrastructure's financial

and unit price performance going forward. We don't profess to know when or if interest rates will rise further, however, we can state that we have for the last several years, during this historically low interest rate environment, operated our business on the assumption that rates would return to more traditional levels. In addition, we do not believe that higher interest rates are bad for infrastructure assets, in fact, we believe the opposite, as higher rates will in all likelihood, be accompanied by higher inflation and economic growth which are generally beneficial for our business.

So let me start with how we operate our business. Since our inception, we have deployed a consistent investment strategy whereby we target acquisition opportunities where we can invest on a value basis and earn attractive total returns of 12-15%. We consciously ensured that we did not reduce our return requirements when interest rates declined dramatically nor did we assume that interest rates would stay at these low levels in perpetuity in our valuation models. This may have put us at a cost of capital disadvantage for a period of time compared to the approach taken by some other investors, but we felt it was the prudent investment approach. From a risk management perspective, we predominantly finance each of our operations with long-term, fixed rate debt on a non-recourse basis to Brookfield Infrastructure and utilize investment grade structures to provide us resiliency through economic cycles. Furthermore, we have been extremely active over the past several years, extending maturities and locking in low interest rates. Our current business has a well staggered maturity profile with an average maturity of almost 10 years and approximately 90% of our long-term debt is at fixed rates.

Now looking at the infrastructure class more generally, we believe that there is a general misconception that rising interest rates are negative for infrastructure assets because they are occasionally perceived as "long bonds" from a valuation perspective. While infrastructure assets have strong barriers to entry that provide the same security of cash flows associated with high grade long-term bonds, they also have operating, regulatory and contractual components that tend to result in rising cash flows and values over time. We target "same store" FFO growth of 6-9% per annum and are optimistic of achieving this target because of the levers that exist in our operations. To give you a sense of the levers, I'll run through the opportunities for organic growth in our own portfolio.

First, we capture inflationary price increases – The majority of the assets we own today tend to operate under regulated and contractual revenue agreements which contain either explicit inflation-linked revenue increases or revenue growth formulas that are derived from real inflation levels. Approximately 70% of our EBITDA is exposed to inflationary price increases, and given the high margin businesses we own, and the fact that our debt is fixed for the next 10 years, we expect our FFO to increase on average 3–4% each year. This growth is dependent on inflation levels in the countries in which we operate.

Second, our surplus capacity captures global economic growth – We operate many businesses that benefit from global economic growth. Businesses such as toll roads and ports that have historically had very high correlation to GDP growth, have surplus capacity that can handle additional volume generated from economic growth. These two businesses alone represent 35% of our total EBITDA and should lead to an approximate 1–2% increase in FFO for us on an annual basis. These growth levels do not take into account several of our other businesses that we also believe will be positively impacted by economic growth, namely our railroad business in Australia, our Chilean transmission business and our UK regulated distribution business.

And lastly, we reinvest internally generated cash flows into upgrades and expansions of our networks, which we categorize as our capital backlog. Typically each year, we retain 20% of

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our FFO to invest in the capital backlog in our existing businesses after we have serviced our distribution and maintenance capital expenditure obligations. We earn on average a 12% FFO yield on these investments, which we expect should add further annual FFO growth of approximately 2–3%. We have a track record of successfully replenishing our capital backlog in our utilities business year after year, and expect to do so in the future.

In summary, long-term bond values may decrease with rising interest rates but we believe that values for infrastructure assets such as the ones we own, are dependent on their unique cash flow attributes that reflect their ability to capture inflationary, economic and expansion growth potential. Should interest rates rise, we believe it is likely to be in conjunction with higher economic growth and inflation which should positively impact our FFO growth and correspondingly the value of our business as a whole. The best protection we have against rising interest rates is the embedded growth potential in our business.

Now let me turn to providing an outlook for our business. We have been successful in the past by applying a contrarian approach when making new investments, often the result of focusing on sectors or regions that are capital constrained. In countries such as Brazil, economic growth has slowed and the currency has fallen against the U.S. dollar. Foreign investment has declined and capital available in the country has suddenly become scarce. At the same time, the demand for infrastructure is considerable given the lack of investment in recent years. As a result, a significant catch-up is required in order to build out the country's infrastructure to meet current needs. In this environment, we see opportunities to acquire high quality assets with strong fundamentals at attractive valuations. Overall, we remain confident in the country's long-term prospects given its plentiful resource base, attractive demographics, established rule of law and expanding middle class.

We also continue to focus our attention on several industrial sectors that are out of favour with the capital markets to unlock infrastructure assets that are part of a larger logistical chain. We believe we can invest at attractive returns in these situations by assisting corporate owners of infrastructure assets to surface value and liquidity within their businesses and bring our unique operating capabilities to bear to drive further value creation. I mentioned on our last call that we were active on a number of transactions. I am pleased to report that we recently increased our investment in our Brazilian toll roads, bought a district energy business and entered into exclusive negotiations for an investment into a large rail and port business in South America. In addition, we are in exclusive discussions relating to several other investment opportunities. As a result, we continue to feel very enthusiastic about our growth prospects going forward.

In addition to seeing excellent opportunities to expand our global portfolio, we also have significant financial resources available to pursue these initiatives. For each ~\$500 million of equity capital that we deploy in new investments each year, we believe we can generate an additional ~2% of FFO per unit growth on an annual basis. Deploying our existing liquidity and new capital we raise in the future can be very meaningful for our business. That's in addition to the organic growth that we can achieve as described earlier. As a result, we are targeting long-term average distribution growth in the range of 5–9% for the Partnership which we believe in combination with our 4-5% current yield, is a compelling total return for our unitholders.

With that, I would like to turn the call back to the operator to open the line for questions.

### **OPERATOR:**

Our first question is from Young Ku with Wells Fargo. Please go ahead

**YOUNG KU:**

Great, thank you. Brendan Maiorana is on the line with me as well. Sam, you made a pretty convincing argument regarding your assets being protected against kind of rising interest rates from a cash flow generation perspective, but just wondering if you can comment on kind of the impact on asset value perspective. I mean, historically speaking, how do infrastructure multiples react in a rising interest rate environment?

**SAM POLLOCK:**

I didn't quite get the full question there, but if I can paraphrase and correct me if I'm wrong, I think your question was in rising interest rate environment, multiples tend to come down. Was that basically your question, or do they?

**YOUNG KU:**

Yes, whether that's kind of true or not.

**SAM POLLOCK:**

Yes, you know what? I obviously didn't go into all the various components of deriving a multiple, but I think the main takeaway you should have from my comments was that more often than not, people just do one way changes when they look at values for businesses. If they see rising interest rates, they just assume that there is just a corresponding reduction in investment return requirements and reduce multiples, but what they don't take into account is that on the revenue side, there's significant changes that are going on and in many cases, you know, a lot of the reasons why we would pay higher multiples has more to do with the growth prospects for a business than the actual cost of capital that we're driving to.

So, it's just not a very simplistic valuation equation and our main point for investors is don't just assume values decline because interest rates are going up. In fact, in many of our assets, we think they'll rise. There will be businesses, and ones that we have sold are the ones where we felt that they were, in particular, very sensitive to long-term interest rates.

**YOUNG KU:**

Okay, got it. Thank you for the clarification. Maybe this is for Bahir or Sam. So, you previously talked about kind of FFO per share going up by 10%-plus per year, hence why you kind of increased the distribution growth to 5% to 9%. I'm just wondering if whether that still stays intact and why wouldn't you raise kind of that 5% to 9% higher since historically, you've been able to increase by 10%-plus as well?

**SAM POLLOCK:**

Hi. I guess I'll answer that question. Look, I think when we set the targets and when the board ultimately decides what the distribution levels will be, we look at a number of factors and it isn't necessarily the past and it's not looking out one year. We tend to take a much longer term perspective when setting these targets and our view is that we can generate a 10% long-term annual FFO growth in the business and, you know, based on our structure with maintaining payout levels at the level that we have them at today, results in distribution growth in the mid-7s, which is in the middle of the range. So, we just decided to give ourselves a band slightly below and above to take into account unforeseen wins and losses and thus, that was the rationale for that level.

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We obviously hope to overachieve that and that's what we're paid to do, but we thought that was a reasonable target to set for ourselves and convey to our unitholders.

### **YOUNG KU:**

Okay, great. That's helpful. And so, in the letter to shareholders, you talked about transitioning from capital recycling mode to kind of a capital deployment mode and I know previously you had some non-core assets that you were looking to sell. Could you just let us know what kind of magnitude in terms of dollar amount that non-core assets remain within your portfolio and when would you expect to be out of these?

### **BAHIR MANIOS:**

So when we look at recycling assets, it really is a reflection of where they are in their life cycle and what our capital requirements are. So, I'd say currently we have a significant amount of liquidity and so we are focused more on capital deployment and raising further liquidity. In addition to that, the obvious candidates for us to look at regarding non-core asset sales would be those investments that are either very tiny and don't have significant growth, and I guess probably our distribution business in the Channel Islands would be one that would fall into that category and then we have a number of investments where we don't have the level of operating control that we would typically like to have.

So I'd say in the near term, we don't have plans to dispose of any of them. From a valuation perspective, I don't think they're all operating at their full potential and there's still recovery underway, and—but I think over the next three to five years, it wouldn't be unreasonable that we would consider selling up to other businesses.

### **YOUNG KU:**

Great, thank you.

### **OPERATOR:**

The next question is from Cherilyn Radbourne of TD Securities. Please go ahead.

### **CHERYLYN RADBOURNE:**

Thanks very much and good morning. You did mention in your prepared remarks that you didn't reduce your return requirements when interest rates declined and that that may have put you at a disadvantage relative to others. Can you just give us a bit of perspective on whether you're seeing any change in the way others are underwriting transactions, either in terms of economic growth assumptions or their interest rate assumptions?

### **SAM POLLOCK:**

You know, I think the change is relatively recent, so the move up in long bonds really just took place a number of quarters ago, so it's probably premature for us to have enough data points or examples where we've seen that change.

I would say, just in my discussions with peers, my sense is that as we've been saying for quite some time, the pricing level for utility-type assets has become quite aggressive, and so I think there are a lot of investors who recognize that now. So, I think you may see some people take a more balanced approach in that regard and I think we've been advocating acquiring more

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GDP-sensitive assets for some time now as a counterbalance to that and I think others are thinking along the same lines.

So, I wouldn't want to say we were the ones leading the charge, but I do think that there is maybe a little bit of shift towards some of the things that we've been talking about the last couple quarters or years.

**CHERYLYN RADBOURNE:**

Okay, that's interesting color. Could you just comment on what your FFO would have looked like this quarter without the benefit of your foreign exchange hedging program?

**BAHIR MANIOS:**

Hi Cherylyn, this is Bahir. So, we did have a positive impact from our FFO hedging program in the quarter. It wasn't very material. I think where we see some tailwinds or positive results coming from that program will be in the positions that we've put on for the next 24 months, in fact, especially for Australian dollar FFO. So we see going forward, a bigger positive impact although in the current quarter, it was positive but yet not all that material to BIP.

**CHERYLYN RADBOURNE:**

Okay. And then last one for me, the supplemental refers to certain large-scale projects at NGPL. Can you just elaborate a little bit there?

**BAHIR MANIOS:**

Sure, Cherylyn. It's Bahir again. We've been very focused this year doing a lot of stress crack and corrosion work in older parts of our pipeline and so we don't think these are non-recurring. You know, 2013, if you look at our maintenance CapEx that we've spent – in the energy segment which predominantly comes from that business – far exceeds where we think sustainable levels will be. So, it just relates to certain of those projects which we expect will reoccur again in Q4 and maybe into the early part of 2014 before we reach more sustainable levels there.

**CHERYLYN RADBOURNE:**

Okay, thanks. That's all for me.

**OPERATOR:**

The next question is from Paul Tan with Credit Suisse. Please go ahead.

**PAUL TAN:**

Hi, good morning. Regarding your Arteris investment; could you clarify how much percentage of Arteris is owned through the Abertis-Brookfield joint venture, and is there a portion that is owned directly by BIP or a Brookfield entity?

**BAHIR MANIOS:**

Hi Paul, it's Bahir. So, the combined joint venture owns about 70% of Arteris and then Brookfield and other institutional partners own an additional 14%. So, combined between the Brookfield-led consortium and our partner, Abertis, we own approximately 84% of the operating company, Arteris.

**PAUL TAN:**

And secondly, does that put you over the threshold of the—obviously the 75% with regards to the choices that you have to make with that going forward, whether or not it's to decrease below 75% or to do an outright takeover of the whole entity. What's your thoughts or plans going forward with being at 84%?

**SAM POLLOCK:**

Yes, hi Paul. Yes, I guess our current view is, in fact, that we don't go over that level because a portion of the shares held within the Brookfield consortium are in relation to institutional investors that invest alongside of us and consequently that's the position we've taken with the regulator but, you know, we're waiting to hear back from them and see if they have a different view. So, it's unclear at the moment and I think in the next little while we'll be informed of the situation by the Bovespa.

**PAUL TAN:**

Oh great, thank you. And lastly, with regards to one of the items that you have on your outlook, with the exclusive negotiations for a large general cargo infrastructure, could you confirm if that is the Vale VLI assets?

**SAM POLLOCK:**

Yes, we can confirm. They made a public announcement, hence the reason why we felt comfortable in referring to it, but that's really all we can say about the transaction at this time.

**PAUL TAN:**

Okay, great. Thank you very much.

**BAHIR MANIOS:**

You're welcome.

**OPERATOR:**

The next question is from Bert Powell with BMO Capital Markets. Please go ahead.

**BERT POWELL:**

Yes, thanks. Bahir, just back to the toll roads for a minute. This was a good quarter for FFO; a good sequential increase. Can you help us understand how much of that was just organic improvements in the Chilean toll roads; the Arteris versus what the bump was from the increased investment that came into September?

**BAHIR MANIOS:**

Sure, Bert. Thanks. So, we recorded approximately \$6 million of FFO relating to the partial contribution from the step-up in our interest in that company that happened in, I believe, the second week of September, so that aided our results. If you took that out, we were at \$20 million, which I believe was relatively flat to Q2. So going forward in Q4, you'll see obviously the bigger contribution coming out of that business once we get the full benefit of the step-up in

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Arteris coming through our results and then looking into 2014, we will then achieve higher levels as our Chilean toll road continues to step up its earnings profile.

### **BERT POWELL:**

So, how should we think about that sequential \$6 million? Is that a third? Is it one month that's in there, or should we bump that to an additional \$18 million a quarter? I'm just trying to think what the \$6 million represents. Is it a third or is it more? I'm just not sure.

### **BAHIR MANIOS:**

Yes, Bert, that's not a bad assumption, although I would caution that any time you do these partial quarter contributions, there's maybe some noise that may come through your results. But in all material respects, if you did exactly what you said, I think you would get to a good run rate, at least for Q4.

### **BERT POWELL:**

Okay, perfect. And then just with respect to capital opportunity on widening the roads and increased traffic; is that material at this point?

### **SAM POLLOCK:**

Hi Bert. You know, I'd say the benefits of that are probably more back-end loaded to years 2016, '17, '18. I think the capital projects are in mid-swing and it will probably take at least two years to break the back of most of them. But we do think that they're great opportunities for us.

### **BERT POWELL:**

Okay, thanks. Sam, can you also maybe give us just your thoughts in terms of how much equity BIP would be comfortable with in this Vale asset, assuming you're successful?

### **SAM POLLOCK:**

I guess what I can say is that we'll obviously invest in the business alongside other institutional investors. As you know or may have seen the scale of the transaction is about \$2 billion, which is anywhere between \$800 million and \$900 million, and we typically take anywhere between 40% to 50% of a transaction. So, that will probably give you a ballpark size. It will be reasonable but obviously not gargantuan for us.

### **BERT POWELL:**

Okay, and then just back to your comments earlier, Sam, when you talked about assets that are out of favor with capital markets. Were you referring to the cooling asset or did you have other assets you had in mind that you were thinking about?

### **SAM POLLOCK:**

No, generally when we're talking about assets that are out of favor, we're these days normally referring to the shipping sector and the mining sector. You know, those would be areas where we see lots of businesses are capital constrained and who are large owners of infrastructure assets and so, you know, we've been building our relationships with companies in those sectors for some time.

### **BERT POWELL:**

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Okay, and that pipeline still looks fairly robust at valuations that you think are kind of where you'd delineate them?

**SAM POLLOCK:**

It does, yes.

**BERT POWELL:**

Okay, thanks Sam. Thanks Bahir.

**SAM POLLOCK:**

Okay, thanks Bert.

**BAHIR MANIOS:**

Thanks Bert.

**OPERATOR:**

This concludes the time allocated for questions on today's call. I will now hand the call back over to Mr. Pollock for closing comments.

**SAM POLLOCK:**

Okay, thank you, Operator. With that, I'd just like to thank everyone for participating on today's call and we look forward to speaking with you again next quarter to review our progress. Have a nice week.

**OPERATOR:**

This concludes today's conference call. You may now disconnect your lines. Thank you for participating and have a pleasant day.