Brookfield Infrastructure Partners L.P.

2014 Second Quarter Conference Call Transcript (Q&A only)

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Speakers:

Sam Pollock
Chief Executive Officer

Bahir Manios
Chief Financial Officer

Tracey Wise

Thank you, operator and good morning. Thank you all for joining us for Brookfield Infrastructure Partners' second quarter 2014 earnings conference call. On the call today is Bahir Manios, our Chief Financial Officer, and Sam Pollock, our Chief Executive Officer.

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 our 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 you to 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 Manios. Bahir?

Bahir Manios

Thanks Tracey and good morning.

In my remarks I will focus on Funds from Operations or FFO, which is a proxy for cash that we generate in our business.

Our results for the quarter were strong with most of our operating businesses performing well. We reported Funds from Operations ('FFO') of $180 million or $0.86 per unit which translates to a 62% payout ratio that sits comfortably at the lower end of our long-term target range. For the first half of the year, our results were up 12% on a comparable or "same store" annualized FFO per unit basis, surpassing our targeted goal of 6% to 9% of organic growth that gets generated without additional fresh capital from BIP. For the quarter, our results were flat compared to the prior year as the second quarter of 2013 benefited from the contribution of assets that were subsequently sold as part of our capital recycling initiative.

Our utilities business generated FFO of $92 million in the period, compared with $83 million on a comparable basis and $96 million in total for the second quarter of 2013. Total results in this segment were lower, reflecting the impact of the sale of our Australasian distribution operations in the fourth quarter of 2013. However, the comparable results were strong as our businesses benefited from higher connection activity in our UK regulated distribution business, inflation indexation, a larger regulated asset base and lower costs resulting from margin improvement programs at a number of our operations.

Our transport business generated FFO of $94 million in the second quarter of 2014, compared to $83 million in the prior year period. The increase in FFO was driven largely by the greater contribution from our Brazilian toll roads, where we doubled our ownership in September 2013, and stronger results in our ports business, where we benefited from both the newly acquired North American West coast port operation and better performance at our European port operations. This increase in FFO was partially offset by $6 million of non-recurring interest income from a favourable stamp duty ruling at our Australian railroad that was reflected in prior year results.

Our energy business generated FFO of $16 million in the second quarter of 2014, compared to $18 million in the prior year period. Results were negatively impacted by lower transportation volumes in our North American gas transmission business and a warmer winter that affected volumes in our UK energy distribution business.

On the financing front, subsequent to period end, our Chilean electricity transmission business completed a $375 million financing, comprised of notes that were rated Baa1 by Moody's and BBB by Standard and Poor's. The issuance, which was almost 7x oversubscribed, has an 11-year term and a coupon of 4.25%. The proceeds from this financing will be used to repay debt that is maturing in the second half of 2014 and 2015.

From an operations perspective, most of our businesses performed well during the quarter and we're encouraged on a number of fronts:

- Most noteworthy was our Australian regulated terminal where we experienced record capacity utilization of over 95% in June. Given that we have take-or-pay contracts in place with premier mining companies, our financial results for this business are not impacted by volumes handled at the terminal. However, this level of throughput is encouraging as it demonstrates that, in this low price environment, our customers are continuing to ship significant volumes through the terminal.

- Our railroad saw another good quarter with volumes up 5% from prior year as a result of higher iron ore and grain shipments which were ahead of our expectations.

- And finally our ports business also experienced a solid quarter with results improving compared to the prior year. The business in the UK has seen an overall 15% increase in underlying volumes on a year-to-date basis compared to the prior year, primarily due to improving economic conditions and several customers expanding their operations. In response to increased demand from our customers, we are investing $35 million to complete an upgrade of the quay to accommodate increased volumes. In addition, we are in the midst of integrating our North American west coast container terminals into our ports platform. We expect to see a meaningful contribution from this business with the completion of its modernization program at the end of 2015.

And finally on the organic growth font, as you know, this is a core part of our overall growth strategy and we have continued to add to our capital backlog in our utilities, transport and energy businesses during the quarter. These are all projects that are funded by internally generated cash flows and earn us very attractive risk adjusted returns.

As an example, this quarter, in our utilities business we grew our committed projects backlog during the second quarter to approximately $435 million which we expect to invest and commission into our regulated asset base in the next 24 months.

We did that by adding almost $100 million of projects primarily at our UK regulated distribution business and our Australian regulated terminal. Our UK regulated distribution business experienced record sales activity during the period, with sales of our multi-product offerings up over 40% compared to the prior year. The increase in activity levels is primarily attributable to a broader recovery in the UK housing market which still remains below pre-financial crisis levels.

Also at our Australian regulated terminal, we received approval to invest an additional $50 million on the final phase of a storm water management system.

With that, I will turn the call over to Sam

Sam Pollock

Thanks Bahir.

The focus of my remarks today will be on updating our investment activities and reviewing our investment posture.

Last quarter we indicated that approximately $450 million of capital was committed to be deployed into four new investments. We have made considerable progress towards closing these transactions and expect them to start to contribute to our results during the second half of the year.

In mid- August, we expect to close on our investments in VLI and Macquarie District Energy, as we have received all consents required for closing these transaction. VLI is a Brazilian rail and port business which will provide us with approximately $300 million of organic growth projects as the business has a substantial capital program to expand operations. Macquarie District Energy is a district energy system that provides environmentally-efficient heating and cooling to large buildings in Chicago and Las Vegas.

We are still waiting for regulatory consents to close our investment in the Elizabeth container terminal located in the port of New York/New Jersey and the acquisition of Seattle Steam. We expect to obtain the required consents during the second half of 2014.

Just after quarter end, we signed an agreement to acquire Lodi Gas Storage in California with institutional partners, for $105 million. Our equity investment will be 40% or approximately $40 million. While this is a modest investment, we believe we are acquiring the business for exceptional value. This business complements our existing natural gas storage business and we expect to achieve some synergies from combining it with our current platform. We expect this transaction to close by the end of the first quarter of 2015, following completion of customary closing conditions.

I would now like to discuss our investment posture as lately we have had a recurring question from a number of our investors regarding how much longer will the investment cycle for infrastructure assets last before we see a correction in values?

While our views don't necessarily lead to a simple answer, we can certainly see an argument for both sides of the debate. For those of us with GDP sensitive operations in North America and Europe, it certainly feels like the recovery in economic growth is just beginning. Our European ports business has only recently shown improvement with increases in container traffic and signs of new customer investment activity, particularly in our UK operations. Furthermore, in both the UK and the U.S., we are still not seeing housing starts at levels that approach the steady-state levels we would expect. Consequently, we should still experience stronger economic growth for a number of years to come, which will support valuations and encourage further investment.

But you can also take the view that we are late in the investment cycle. The stock market in the U.S. and Canada is well into its fifth year of strength, there has been a recent spate of IPOs by companies looking to exit core assets, and the use of leverage and valuation multiples in a number of notable mergers and acquisitions are approaching levels that we haven't seen since 2005-7. These are all indicators of a cycle nearing its conclusion.

Now, no one can say for certain how much longer this cycle will last or what sort of correction we could experience once interest rates start their climb from these historic lows. Our view is that valuation levels for some asset types have been inflated by a combination of extremely low interest rates and a scarcity of infrastructure opportunities to satisfy the investment appetite of new market entrants. On the other hand, we also believe that the global economy will likely surprise on the upside, which should mitigate these factors from a valuation perspective.

Our businesses are not liquid investments and therefore we take a much longer term approach to investing than many investors. As a result, our investment and financial strategy is formulated to succeed throughout the business cycle, including conditions which currently exist. However, we believe that several of our investment guidelines are particularly relevant in this valuation environment and therefore I wanted to reiterate 5 of these guidelines to you.

First and foremost, we remain focused on investing capital to meet our long-term return target of 12-15%. We do not believe in reducing our return thresholds for the sake of making it easier to acquire assets, nor do we justify purchases based solely on our accretive cost of capital.

Second, we create value for our unitholders by being both good buyers and good sellers. Late last year we recycled over $1 billion of equity capital in our business through asset sales. While we don't expect that we will be selling assets every year, harvesting assets to re-invest back into our business is a core strategy. Investing capital at 12-15% returns and selling assets at an 8-10% return level is very accretive to our company's per unit growth.

Third, we don't pay for unrealistic growth targets. Whenever we look to make an acquisition, the seller will always portray a very rosy future for the business. We apply our expertise to forecast a reasonable expectation for growth that reflects competitive dynamics such as new market entrants and regulatory considerations. This is where many acquisition mistakes are made, in particular when capital is more freely available.

Fourth, we buy high quality assets with established, proven business models and management teams that have a solid track record. We are always focused on identifying businesses with internally generated organic growth potential where we can deploy further capital at highly accretive returns. Furthermore, in an environment where odds favour interest rates increasing, assets that are fully contracted with little organic growth are the most susceptible to valuation declines.

Lastly, we maintain a high level of liquidity. We currently have approximately $2.5 billion of total liquidity. We have also extended the maturity profile of our debt to an average of 10 years and, for the most part, fixed our interest rates. While we incur some costs for maintaining high levels of liquidity and utilizing long-term, fixed rate debt, we believe the benefits of being in a position to take advantage of market corrections far outweigh the costs.

I am going to conclude my remarks with an outlook for our business.

We have built a business over the past number of years that is positioned to deliver solid results in a variety of economic environments. We are currently operating in global economic conditions that are generally good. The U.S. economy is continuing to demonstrate signs of renewed growth and we have also seen further easing of monetary policy by the European Central Bank. There are continued signs of economic stabilization within China, where government officials recently expressed confidence that the country would achieve the 7.5% annual GDP growth target established late last year. The only region where we operate that has seen economic growth decelerate is South America, however, we believe the fundamentals continue to support favourable growth over the longer term. On the whole, our business should perform well in this economic environment.

We remain disciplined with our capital allocation and underwriting. Liquidity is strong, and our business development teams are continuing to engage on a number of attractive investment opportunities. In addition, as I mentioned earlier, we have almost $1 billion of organic investment opportunities in our operations that are committed which are always the lowest risk and highest return for us.

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

OPERATOR:

Thank you. We will now begin the question and answer session. If you would like to ask a question, please press star, and one, on your touch-tone phone. You will hear a tone to indicate you're in queue. For participants using a speaker phone, it may be necessary to pick up your handset before pressing any keys. If you wish to remove yourself from the question queue, you may press star, and two. There will be a brief moment while we poll for questions.

The first question today is from Brendan Maiorana with Wells Fargo. Please go ahead.

BRENDAN MAIORANA:

Thanks. Good morning. Sam, so at DBCT you guys had record utilization. What do you think that means for the prospects for additional growth CapEx at your Australian Rail operations, and could you also maybe speak to does the high utilization do anything to rekindle the opportunity at Dudgeon Point as well?

SAM POLLOCK:

Let me just write these down for a second. So, hi Brendan. Maybe the first comment I'll make on the higher volumes we're seeing at DBCT. You know, I think the reason we're seeing that is because all the mining companies right now are highly focused on bringing down their per unit costs, and so they're focused on maximizing volumes and achieving those economies of scale. So, that's why we think we're seeing this phenomena take place in this particular environment and so we would expect that to continue for the foreseeable future. I believe that we're seeing to a certain extent, maybe not as widely but also taking place out in the western part of Australia in relation to our rail business as well. So, I think over the next couple of years we should continue to see higher volumes and higher utilization for both businesses and obviously, subject to where the commodity prices trade. I think as far as major expansions, my view is that most of those are probably on the shelf for the time being until we see some price signals that would suggest that they would make sense.

So, in relation to Dudgeon Point, at this stage we are still pretty much pens down as it relates to that particular large scale expansion project. What we are doing though and what we've been thinking about for the last couple of quarters is some smaller, more incremental type expansions that we can do at DBCT itself. So, you know, the first phase might be a 4 or 5 million tonne expansion and then we've got some ideas around maybe how we can do a 15 or 20 million tonne expansion, but they're much more smaller and incremental than Dudgeon Point which would be in relation to much greater growth, which we just don't see at this point in time.

BRENDAN MAIORANA:

Okay, that's helpful. So it sounds like kind of similar to what you guys put in place this quarter. I think it was $50 million of additional at DBCT. Then just my second question, last question, for Bahir. So, just thinking the capital backlog now, the growth CapEx projects, they're about – I think it's about $900 million – kind of give or take. I forget if that's sort of a number through the end of 2015 or if that's a 24-month window and how should we think about the ability to finance that on a leverage-neutral basis through your cash flow, and what that may mean for the dividend? Because if I think about just a high level BIP perspective, your AFFO less the dividend is sort of in the low $200 millions which would suggest to me that maybe funding this internally from just operating cash flow on a leverage-neutral basis – call it 50/50 debt to equity or maybe even 60/40 – seems like you may fall a little bit shy. So, just wondering with the increase in the CapEx backlog, does that mean you've got to look for some additional sources to help fund that on a leverage-neutral basis?

BAHIR MANIOS:

Sure, thanks. Hey Brendan, thanks for that. So, as you said, there's about $930 million of total CapEx in our backlog, including about $35 million in energy projects and if you add that to our utilities and transport numbers that we disclosed in our Supplemental, you get about $930 million. These numbers will be invested over the next two to three years. As you've correctly pointed out, they will be funded say, on average, by 50%. Typically, your utilities projects will be funded with 60% to 65% debt and the transport and energy projects will be funded by, say 40% to 50% debt to equity so, on average, you're right, about 50%. So over three years, and if I look out to our forecasted results and just keeping with sort of our methodology of retaining 20% of the FFO that we generate in our business, retaining that back into our business and reinvesting in these projects, we don't think we will be in need of any fresh, new capital. That's also in addition to about $760 million of retained cash that's in the business that today we have. So, we do have currently, a lot of cash in the business and in addition to that in the next three years we'll be generating some pretty good cash flows that will be sufficient to fund this approximately $930 million CapEx backlog.

SAM POLLOCK:

Yes. Maybe just to add to that, a significant amount of this backlog relates to our Brazilian toll roads where we have lines of credit with BNDS specifically set aside for these expansion projects, as well as a significant amount of cash that we have prefunded that sits down there as well to fund the CapEx. So, you know, that probably skews the numbers a bit but most of that CapEx has already been prefunded through those two mechanisms.

BRENDAN MAIORANA:

Okay. All right, very helpful. Thanks guys.

BAHIR MANIOS:

Thanks, Brendan.

OPERATOR:

The next question's from Andrew Kuske of Credit Suisse. Please go ahead.

ANDREW KUSKE:

Thank you. Good morning. I just want to sort of step back a little bit and think about your capital allocation on a global basis and how you're thinking about just some of the currency moves we've seen recently. So, we've seen the euro pull back a little bit; some of the Lat Am currencies are still somewhat depressed relative to where they were a few years ago. So, how do you think about that in terms of allocating your dollars on a say, the next few years, relative to say, quote-unquote more normalized levels of some of those currencies?

SAM POLLOCK:

Hi Andrew. Aas it relates to currencies themselves, we take a much longer term view when thinking about where they sit at this particular point in time. I think whenever we make an investment, long-term growth rates, inflation and currencies are all factors that go into our underwriting analysis but I'd say, you know, the currency side of it is one that if we think that we're sitting outside of a particular band then we'll usually cover that off through some sort of hedging activity, particularly as it relates to the euro or the UK pound where we can almost always hedge that out at very low cost if we think that they're trading outside of what we would describe as a normal band. South America is obviously a little different but, you know, today I'd say we think that the currencies down there are probably fairly attractively priced and putting aside all other factors, it would be a relatively good entry point to go into that market.

But, I think just sort of maybe adding to your question a little bit, putting aside valuation for the time being – we see good conditions for investing across the world. Our two most active regions at the moment are probably Europe and then maybe to a lesser extent Australia and then we've got a number of I'd say more early stage opportunities that we're evaluating here in North America and in South America. But all-in-all, we've got a good pipeline around the world.

ANDREW KUSKE:

Okay, just as a follow up on that and then if we focus on the European situation, really what are the primary drivers of some of the opportunities you're seeing? Is it corporate deleveraging or is it effectively bank deleveraging trying to get off of some loans on their books?

SAM POLLOCK:

It's both, you know, to be honest. The theme is definitely deleveraging though. With where the bank market is today in Europe, there's some opportunities that unfortunately have gotten away from us because companies have been able to blend and extend to a certain extent but generally, people are either taking advantage of this point in time to sell assets to help pay down debt or banks are giving them a bit of a push. So, that is creating opportunities for us.

ANDREW KUSKE:

Okay. That's very helpful. Then if I may, I'd just ask one more specific question as it relates to some of your co-investor interests in some of the assets and say Transelec, in particular. I think if we looked at that asset, it's probably the one that's been on the Brookfield books the longest and so the ownership positions there, are they coming up to the end of life of the original life of the Fund before they go into the option periods? Then, what does that really mean from a BIP standpoint on an opportunity to increase the capital position allocated to those assets?

SAM POLLOCK:

So, in relation to Transelec, that was an investment we've made with three institutional partners going back probably to 2005. At the time, it wasn't really a fund per se, it was more of a joint venture type arrangement. It doesn't really have a specific termination period and so, the exit decisions are really dependent on each individual partner's investment horizon. So, we know our partners like that asset as much as we do and so I'm not expecting that anyone's looking to exit any time soon.

ANDREW KUSKE:

Okay. That's very helpful, thank you.

OPERATOR:

The next question is from Robert Kwan with RBC Capital Markets. Please go ahead.

ROBERT KWAN:

Good morning. Just when it comes to GDP-driven investments, it seems that those fit your long-term thesis quite well and generally that leads you to the transport business and maybe a little bit more away from the utilities business. I'm just wondering how you think about balancing the percentage of the investment from each of those different asset classes, if you do at all, and if you do have some targets, what type of goal posts are you looking at in terms of balancing the two?

SAM POLLOCK:

Hi Robert. You know, we don't have any specific objectives around or targets around balancing one asset class to another. I'd say our investment philosophy has always been much more opportunistic and we have just found that over the last 12 to 24 months that the better value opportunities for us have been in the more GDP-sensitive businesses because people have been paying an extremely high valuation for contracted cash flows, which I think we see both in the public markets and in the private markets. But, you know, cycles change. I think once interest rates move you could see that change and people's concerns around that could result in more opportunities for us to invest in utility-type transactions. Obviously, we're able to add to our utilities business through our capital backlog and so, they continually organically grow and make up a meaningful portion of our organic growth and even though we may not do as many utility-type transactions, we are continuing to seek them out and we will from time-to-time, make investments and often they can be large.

So, that's probably a long-winded answer for what you asked but I think the short answer is there is no target and I think you need to look at our investment program over a much longer term time frame than just the last 12 to 24 months.

ROBERT KWAN:

Okay. Just to be clear; if it's not necessarily between utilities and say transport or energy as well, is there a level of exposure to just GDP-driven assets that would get you uncomfortable?

SAM POLLOCK:

I don't think so, and I apologize for the noise in the background here. We've got the air conditioner on in the room here. But I think the thing you need to keep in mind, Robert, is that even for our GDP-sensitive businesses, they're all highly contracted and and/or regulated entities and so, you know, you shouldn't necessarily conclude that the cash flows have a lot of volatility to them. The examples such as our district energy business which we might describe as GDP-sensitive because a lot of our new customers come on because of new buildings that are built and so it has a sensitivity to the economy but besides that, all of our existing customer base is locked in for 20 to 30 years and the cash flows are, to a large extent, indexed to inflation.

So, I think it's just you need to be careful in concluding that GDP-sensitive is volatile; that doesn't necessarily mean that.

ROBERT KWAN:

Okay. Just I guess the last question here, when it comes to your UK regulated distribution business, you cited the multi-product offering. Is that just the fibre side than Inexus brought to you, or is there something else and is this selling additional services to existing customers or is this more driven by an expansion to footprint just offering more services as you roll that out?

SAM POLLOCK:

So, today we have five products; two we had prior to the acquisition of Inexus. So, we always had gas and electricity and those still remain the main multi-product offerings that we sell to customers. Since the acquisition of Inexus we added three new products. One is fibre-to-the-home, one is water and the last one is district energy. District energy typically sells on its own because it targets a different type of residential property but we could and do in fact offer the other four to our customers and I'd say water is a much more nichey, smaller product for us but the one that is continuing to grow, albeit it will take some time before I'd say it's hugely meaningful for our results, but the fibre-to-the-home is probably the one we're most excited about. But today, you know, gas and electricity are very established and I'd say, in most cases, we sell both of those to our customers when we do a sale.

ROBERT KWAN:

What's the fibre penetration rate to the existing customers, i.e., how much running room do you have for kind of above average growth as you sell through to the existing customers?

SAM POLLOCK:

Well, today the penetration is quite modest and in fact, you know, because of the relatively infancy of the regulation around it, from a profitability perspective, it really only is economic for customers with larger entitlement schemes. So, we're hoping that with further work that we'll do with the regulator where we can improve our access points that we, in fact, can make this more economic to much smaller schemes and then our penetration will rise substantially. But, it's still relatively new; I think this is something that hopefully we'll be able to provide you greater transparency on over the next couple of years.

ROBERT KWAN:

That's, great. Thanks, Sam.

SAM POLLOCK:

Okay. Thank you.

OPERATOR:

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

BERT POWELL:

Thanks. Good morning, Sam and Bahir. Just a question on the toll roads. $341 million is your capital backlog and I'm going to assume most of that is for Brazil. Just wondering, can you walk us through how that capital goes in and the lag between the increasing and widening of lanes then turns into FFO. I would assume increasing a road you could automatically—you can start tolling right away; widening is a judgment call around utilization of the toll roads. I'm just wondering if you could help us think about the return on that capital flows.

SAM POLLOCK:

Okay. There's really two elements to it, Bert. The first element relates to higher tariffs that we get from what they describe as rebalancing which is where when we expend the capital, the regulator will allow us to adjust our models where we can increase tariffs and that obviously, gets collected over the life of the concession. So, it's somewhat of a mathematical analysis that we do with the regulator, but it would be over, let's say, the remaining 20 years of the concession. So that's obviously, a very large component to it.

The second component which, you know, can happen relatively quickly is that when we do an expansion and de-bottleneck a road, there's often sort of a step change increase in volumes that takes place and this can happen quite quickly following one of these widenings. They're very specific examples but we have a number of roads such as Regis Bittencourt, which one of the roads that connects São Paulo with Curitiba and, you know, there there's a couple of choke points where traffic is extremely dense and as a result, it just discourages people from making the trip. But once you've completed an expansion, you know what we've seen on other roads is that the experience of travelling from A to B becomes that much better that it just results in people now making that trip whereas today, the only people who would take the road were the people who just must use it. So, you know, that's obviously hard to predict as far as what the quantum of that will be, but those are really the two examples of how it takes place.

BERT POWELL:

Okay, that's great. That gives it a little bit of colour on that front. Just wondering, in terms of your ports commentary, I assume more of that relates to PD ports but how are Euroports doing outside of the PD ports?

SAM POLLOCK:

I'll start on this one and Bahir can jump in as well. You're correct in your first statement that the stronger of the operations has been our UK operation where we have really seen a change in the economic situation in the UK over the last six to 12 months. I think it really started in the fourth quarter of last year and has really carried through to this year and it looks quite promising for the next little while.

The experience in Euroports and in the European continent is I'd say mixed. There is, as far as trade goes, you know, we're starting to see some improvement, albeit lower than what we have seen in the UK, but it's a much more diverse business and so there's always specific situations such as weather conditions in Spain that can impact the amount of generation that comes through hydro versus coal generation; whether or not the coal plants are operating. If the coal plants are operating then there's reduced coal imports and – which is what we've seen – and that's impacted our numbers.

So, it's harder to draw a comparison on the economic conditions of Europe with our operations specifically but, I think our business in Europe, as whole, has been very steady and we're expecting that with the better economy and then hopefully none of this noise with weather or whatever will result in better results over the next couple of years.

BAHIR MANIOS:

Yes, and Bert, I'll just add to that. So volumes have stabilized, as Sam said, so at the EBITDA level were essentially flat to slightly up year-over-year and we get more benefit at the FFO line item. Just, you'll recall, that financing that we did last year where we deleveraged the business and also reduced our cost of carry there. So, as volumes ramp up in the next little while, we'll also get that added benefit as well because our FFO there is going to pick up additionally just because of the financing that we did.

BERT POWELL:

Okay. Bahir, just while I've got you, last question on Other Income. In the Corporate side, you had kind of a better than expected quarter there. Can you—is there anything that you can call out to say that this is normal level or what are the one-timers that are contributing to that in the quarter if there's any?

BAHIR MANIOS:

Sure. So Bert, we've got about a—it ranges between $275 million to $325 million; that's the total size of the investment program. From a current yield perspective, we target 4% to 5% returns and from a total return perspective we're targeting 8% to 10% returns.

During the quarter, you're right. Income was $10 million; I would say that's a little bit outside as we did realize on some gains on certain positions that we sold during the quarter, so on a normalized basis I think modelling a 4% to 5% current yield on that investment program will be good, realizing that in certain quarters we could surprise on the upside if we did realize on any positions.

BERT POWELL:

Okay, that's perfect. Thank you.

OPERATOR:

The next question is from Frederic Bastien with Raymond James. Please go ahead.

FREDERIC BASTIEN:

Good morning guys. You mentioned that sales activity was up 40% for your UK regulated business but I suspect this is probably coming off a low base. Can you provide more colour on the strength you're actually observing and whether we can expect this improved sales activity to have somewhat of a material impact on your results in the second half?

SAM POLLOCK:

Hi Frederic. You know, I'd say that the real driver for the sales activity has been the improvement in the economy of the UK and, in particular, in home building. We had, I think, some slight benefit this quarter because of some pricing changes that we were going to institute in the fall and so my understanding was some of the developers advanced some of the sales to lock in that price. But generally our expectation is that the housing starts in the UK will remain strong for the foreseeable future. They're still, as we mentioned in our remarks, at levels below what we would describe as steady state. I don't expect that our market share will drop or increase from the levels we're at now. So, I think we're at a level of penetration that's pretty sustainable.

FREDERIC BASTIEN:

Okay, thanks. The second question I have regards NGPL. There has been little mention of it today. Has your view on the business changed fundamentally?

SAM POLLOCK:

The short answer is no. I think what has changed from quarter-to-quarter, you know, last quarter we talked about how with the extremely cold and long winter that we had that storage levels had dropped to the lowest level we'd seen in – I think in history – and so we were predicting that it was unlikely that we would see injection levels, you know, take storage levels back up to where they were at the end of last year. So, we probably could have, you know, greater volatility and higher prices, which would all be great for our business.

As you know, the summer has seen very temperate weather conditions in the Northeast and injection levels, as a result, have exceeded what we probably would have expected a few months ago and so while storage levels probably won't get back up to where they were, I don't think they're going to be at the drastically low levels that we and others were predicting. So I think we're probably in for another year of relatively modest volatility. Obviously, we hope that I'm wrong and that there'll be better volatility, but unless we get some real scorching weather soon, my expectation is that we'll probably see gas prices and volatility at levels that maybe are a little better but comparable to what we've seen the last couple of years.

FREDERIC BASTIEN:

Okay. Thanks, Sam. That's helpful, thank you.

OPERATOR:

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

CHERILYN RADBOURNE:

Thanks very much. Good morning. First question is just on VLI and the $300 million of growth projects there. I assume that that's your share and was just curious over what timeframe you'd expect to deploy that capital.

SAM POLLOCK:

Hi Cherilyn. So, the answer to your first question, yes, that's our share. I think for the whole business it's a very substantial program of about R$6 or R$7 billion and the timeframe for completing all the projects is anywhere between five and seven years. So, you know, the $300 million that we spoke about really relates to that five- to seven-year time horizon. Our expectation is that a good chunk of that will be at the front end but we haven't yet had an official Board meeting and so the exact timing of those programs we still need to work out with Management and our partners. But that hopefully gives you a bit of a sense of how the numbers fit in.

CHERILYN RADBOURNE:

Okay. Just to come back to the currency discussion earlier in the call, you do continue to be well hedged on your non-Latin American currency exposures and I'm just curious why you aren't hedging the Latin American exposure, whether that's a cost issue to your earlier point, or a view on the currencies, or both?

SAM POLLOCK:

It's primarily a cost issue. We've seen some pretty substantial corrections to date and most of the currencies are within a band that we think is relatively what we describe as normal and so our Treasury group, while obviously cautious about the environment, nonetheless recommend that we maintain the current stance.

CHERILYN RADBOURNE:

Okay. Then last one from me; you do note in your commentary that the use of leverage and valuation multiples on some recent deals has approached prior peak levels and I think we're all aware of some of those examples. Just curious how vulnerable you think some of these deals are to a change in economic conditions or interest rates or both? Are we setting ourselves up for another period of distress at some point?

SAM POLLOCK:

Well, I don't have a crystal ball so I can't say how the things will unfold and there's no doubt that some of the transactions have been fuelled by higher debt levels but I'd say if there is a silver lining it's the fact that most of the higher valuations have been funded from equity and as a result of new entrants using lower return expectations than they would in the past. So, I think there is a risk that for some of those investors who will need to realize on their investments in the short term that they could experience losses but I think some of them also are long-term investors and they may, in fact, hold onto their assets for a much longer time horizon and so, you know, we won't really see the impact of those results. I think it will be almost—it'll be the equivalent of them having bought long-term bonds and just having to wear the mark-to-market losses. But, at this stage I can't predict any sort of negative systemic issues that might come out of this higher valuation period.

CHERILYN RADBOURNE:

Thank you. That's all from me.

SAM POLLOCK:

Okay. Thank you very much.

OPERATOR:

There are no more questions at this time. I will now turn the call back over to Mr. Pollock for closing comments.

SAM POLLOCK:

Thank you, Operator and thank you for everyone on the call for participating today. We look forward to speaking with you again next quarter and reviewing our progress. Have a nice summer.

OPERATOR:

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