



# RARE Series Emerging Markets Fund

**Infrastructure specialist RARE delves into the emerging markets to give retail investors better access to the growth of the world's next economic giants, writes MICHELLE BALTAZAR.**

To the highly experienced team at RARE Infrastructure, the road to wealth can be found in, well, roads. They know this because they've been investing in roads and other infrastructure like airports, utility, ports and highways since the early 1990s – back when the sector was strictly the domain of institutional and high-end investors.

This year, RARE opens its doors to retail investors who, up until now, would be hard-pressed to find an emerging market fund with RARE's formula: invest in listed infrastructure shares that best capture the high GDP growth of their home country. But only do so if those companies pass muster had they been based in developed countries.

Put another way, the RARE team – headed by co-founders Richard Elmslie and Nick Langley – uses its combined 77 years analysing global infrastructure assets to weed out those that are more vulnerable to country-specific shocks.

Using this formula, RARE deftly addresses the socio-political, legislative and operational risks investors often associate with foreign investments.

### Hedged into high growth

Elmslie and Langley believe one way to capture the transformation of emerging economies is to tap into the long overdue and much-awaited construction of toll-roads, highways, airports and utilities as businesses in these regions motor along.

If it's hard to imagine 14-wheeler trucks driving past remote ricefields in Asia, let the numbers paint the picture.

In China, the government and the private sector is set to spend US\$250 billion on railway infrastructure by 2020. Power capacity spend by 2020 is marked at US\$1 trillion. Not to be outdone, India's infrastructure expense bill could be US\$600 billion by 2012.

But where high GDP growth is, inflation is not too far behind. Not so with in-

frastructure because the sector is inflation-hedged.

"People who are worried about an inflationary environment should like infrastructure per se and if they're looking for growth in the market and growth in GDP, this product should be very attractive," said Elmslie.

### Emerging to developed

While many retail investors are yet to set foot in emerging countries to see the transformation of these regions for themselves, perhaps it is the fact many of the major roads are yet to be built that they should invest today.

"You want to be in the market before these countries emerge and develop," said Elmslie. But by accessing these markets through RARE, investors can rest assured that the fund follows a strict discipline to capture the upside and to protect capital from the downside.

"This product has a relatively low financial risk. We look at the gearing of the underlying companies that go into the portfolio and in this fund, the weighted average gearing of the underlying companies is only 12 per cent," said Langley. By contrast, other infrastructure funds could have between 30 to as much as 70 per cent weighted gearing.

Besides the "safe" gearing levels, investors benefit from the fund's relatively high yield of five per cent when global equities only deliver half that.

And just as developed countries are obsessed with corporate governance and ESG as key investment yardsticks, the fund monitors the same measures.

"In working out the cost of equity, we explicitly look at and factor into that cost all the corporate governance type issues and political issues. If we think they are poor then that would obviously increase the cost of equity so we capture that risk in our valuation process," said Elmslie.



RICHARD ELSLIE



NICK LANGLEY

To be on the safe side, RARE only invests in infrastructure shares that are listed, have mature cashflows and are defensive.

"Listed" because it means RARE can easily get in and out of investments.

Less urgent but just as important, being "liquid" means it's easy for investors to buy or redeem their units. "An investor might want to take out money for tax planning reasons but invest back in so at least, the option is there," he explained.

Besides addressing liquidity concerns, Elmslie said investors need to stop thinking that the sector sprung overnight.

"Some of these vehicles have actually been listed for a long time. For example, there are Chinese toll roads that have been listed in Hong Kong for 10 years so they've got a track record where they've been reporting to a developed exchange," he said, continuing, "Same with Brazil. It's not like they've all just come to the market."

Proof of the pudding is that 81 per cent of the fund's portfolio is in companies with mature cashflows, guaranteeing stable and predictable returns regardless of the economic cycle.

### Leave it to the experts

There are local fund managers who are experts in emerging markets and others who are experts in infrastructure – but

rarely both. And that's where RARE's pedigree shines through.

Elmslie boasts 18 years global infrastructure experience and was previously head of power and joint head of infrastructure at UBS Investment Bank. Langley has notched up 10 years in the same sector and spent four years at AMP Capital's infrastructure funds management team. Senior investment analyst Sarah Shaw has nine years emerging markets experience including seven years at Dresdner Kleinwort Wasserstein.

No wonder ratings firms give the boutique fund a thumbs up. S&P rates RARE's existing Infrastructure Value fund a four-star while Zenith rates the same fund "recommended".

The key takeaway is that RARE's team has followed the sector long enough to avoid the pitfalls and spot the gems early on. Testament to their reputation is that they have accumulated more than \$800 million in funds under management from institutional investors since December 2006.

"Richard and I have been in this space for a long time. That means we've actually seen the development of those regulatory regime over time and what we're finding is that in the emerging markets, the regulatory regimes are developing along the same lines as the developed markets." ■

Figure 1. Indexed total return of various asset classes (A\$m)

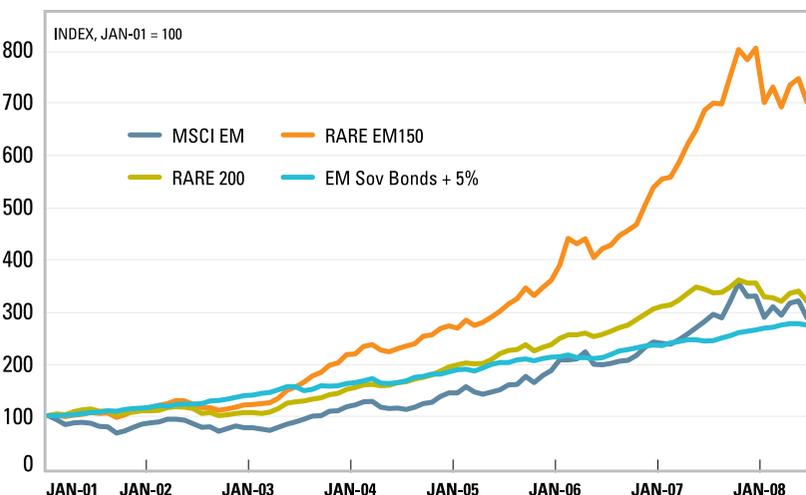


Figure 2. Growth in market capitalisation of RARE EM150 (A\$m)

