Preqin Insight: Alternative Assets in Australia

October 2016

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Contents

Data Pack for Preqin Insight: Alternative Assets in Australia

The data behind all of the charts featured in the report is available for **free** in an easily accessible data pack. The data pack also includes ready-made charts that can be used for presentations, marketing materials and company reports.

To download the data pack from Preqin's **Research Center Premium**, please visit:

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CEO's Foreword

Alternative Assets in Australia

Welcome to this special report highlighting the scale and stature of the alternative assets industry in Australia. Preqin is proud to have collaborated with our many expert contributors – listed below – to assess the development of the private capital and hedge fund industries in Australia, demonstrating the growing importance and success of the industry. We all hope that the report will be a useful summary and reference point for investors, fund managers and advisors globally as they consider the opportunities presented by Australia.

The sheer scale and sophistication of alternative assets in Australia may come as something of a revelation to many readers. With total industry AUM having reached A$115bn, and with a total of 391 alternatives fund management firms and 253 significant institutional investors based in Australia, the country is truly one of the leaders of the industry globally.

Australian private capital[1] has AUM of A$81bn, placing it in seventh position globally, behind the US, UK, China, Hong Kong, France and Canada, but ahead of the likes of Singapore, Japan, Germany, Korea and India. In hedge funds, meanwhile, Australia actually comes ninth in the global rankings of AUM, behind the US, UK and Hong Kong, but ahead of China, Singapore and Germany.

Linked to the scale and sophistication of the alternative assets industry in Australia, its financial performance has been impressive. Private equity returns in Australia over the long term have been superior to those elsewhere; and meanwhile, 2015 was a great year for the local hedge fund industry, delivering returns well in excess of the global benchmarks.

The bottom line is that Australia really matters for investors and fund managers globally. With the significant body of major superannuation funds and other large investors, it is an important and growing source of capital for alternative assets fund managers around the world; and with the excellent returns on offer in the Australian market, it should have an important place in every global investor's portfolio.

We would like to thank our expert contributors for their invaluable help in preparing this report, and we hope that it meets our readers' expectations as a guide to the important Australian alternative assets industry.

Mark O'Hare

With thanks to our contributors:

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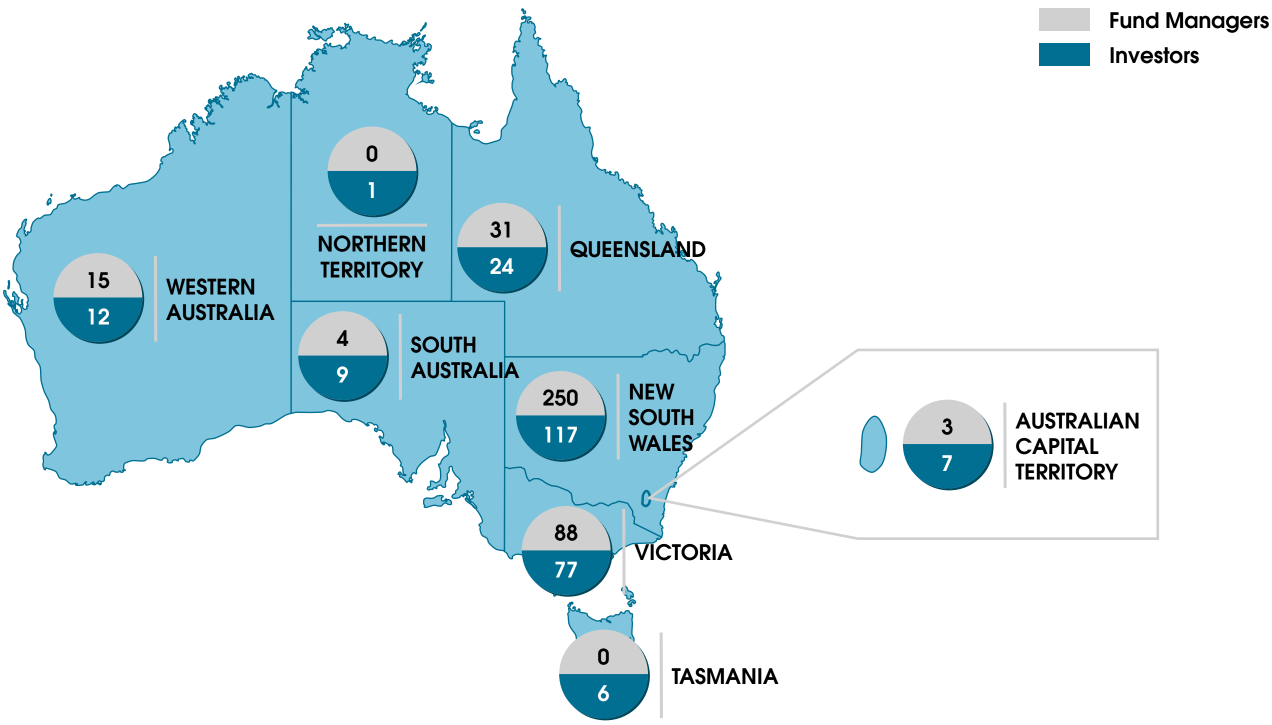
[1] 'Private Capital' includes all private closed-end funds, including Private Equity, Private Debt, Infrastructure, Real Estate and Natural Resources.

Key Facts: Australian Alternatives

Australia-Based Alternative Investment Managers and Institutional Investors by Location



Key Stats

A$115bn
Combined assets under management of the Australian alternatives industry.

A$69bn
Total capital raised by Australia-based private capital funds in the last decade.

107
Number of Australia-based hedge fund managers.

9.53%
Performance of Australia-based hedge funds in 2015, outperforming the S&P 500 Index significantly (-0.73%).

56%
Superannuation schemes are the most prevalent institutional investor type in alternatives within Australia.

A$25bn
Value of the largest Australian infrastructure deal, the financing of the five natural gas terminals comprising the North West Shelf LNG Facilities in 2008.

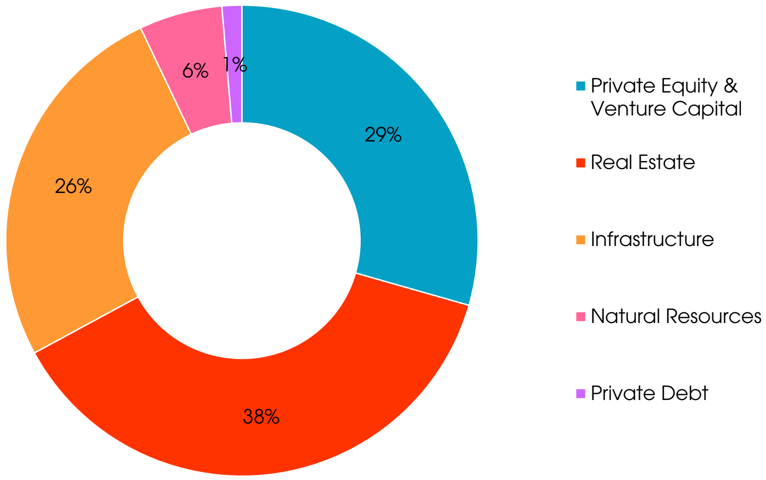
The Alternative Assets Landscape in Australia

Assets under Management

The Australian alternatives industry is the second largest marketplace in Asia-Pacific, with combined assets under management (AUM) of the private capital* and hedge fund industries standing at A$115bn. Within Asia-Pacific, Australia is third behind China (A$272bn) and Hong Kong (A$190bn), although the vast majority (98%) of China's AUM is attributed to its large private capital industry, whereas Australia's environment is more diverse with assets split 70:30 between its private capital and hedge fund industries.

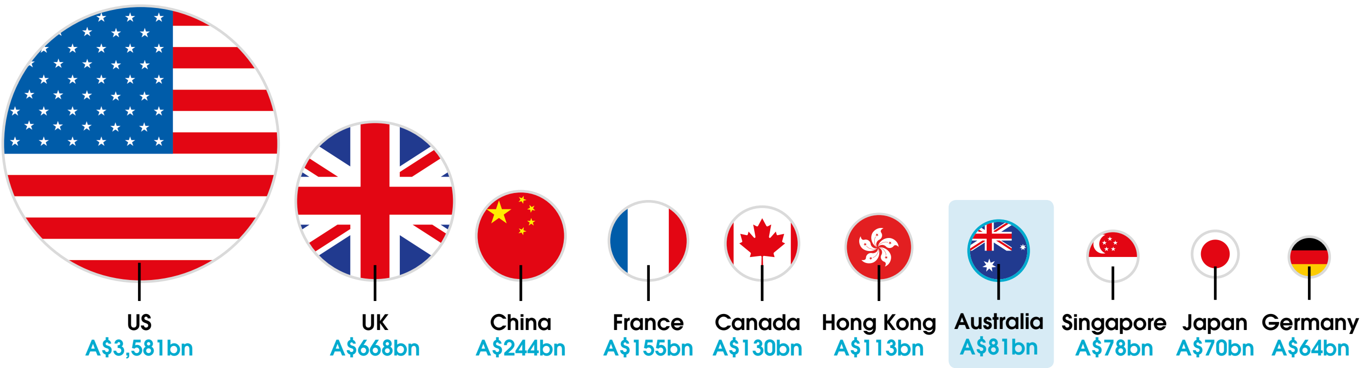
While Australia's private capital industry is still emerging – lagging behind other major markets such as China, France and Canada (Fig. 1.2) – the country's hedge fund industry is more developed and is the second largest in Asia-Pacific; its A$34bn in AUM surpasses that of

Fig. 1.1: Australia-Based Private Capital* Assets under Management by Asset Class (As at December 2015)



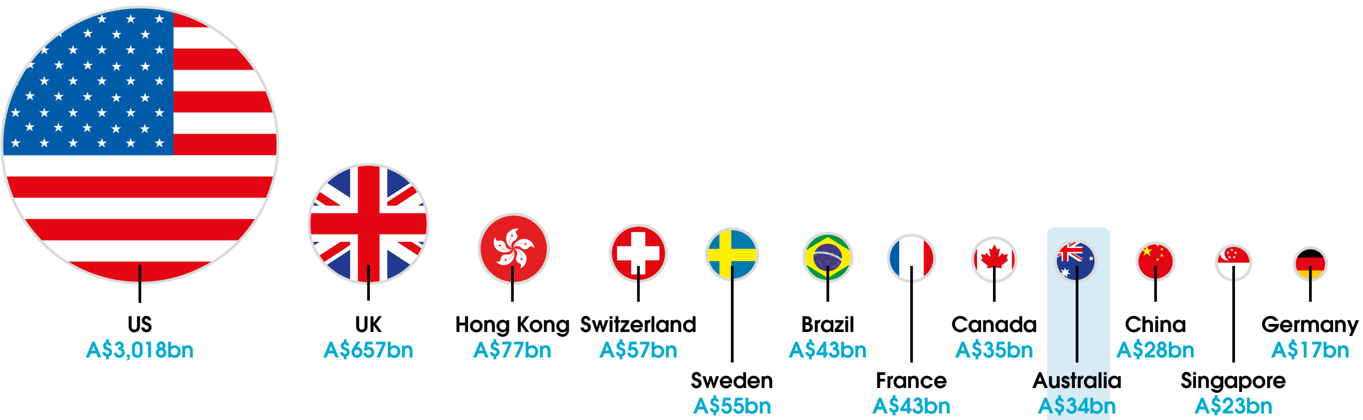
Source: Preqin

Fig. 1.2: Private Capital* Assets under Management by Fund Manager Location (As at December 2015)



Source: Preqin

Fig. 1.3: Hedge Fund Assets under Management by Fund Manager Location (As at June 2016)



Source: Preqin

**Private Capital includes all private closed-end funds, including Private Equity, Private Debt, Infrastructure, Real Estate and Natural Resources.*

major global players such as China (A$28bn), Singapore (A$23bn) and Germany (A$17bn, Fig. 1.3)

AUM of the private capital market in Australia stands at A$81bn, of which the largest proportion (38%) is ascribed to real estate (Fig. 1.1). However, the country's private equity and infrastructure industries also make up notable proportions of private capital assets, with A$24bn and A$21bn held in these asset classes respectively. Natural resources and private debt as distinct asset classes are still relatively nascent markets in Australia, and represent just 6% and 1% of private capital AUM.

Growth in Fund Managers

The number of active Australia-based private capital firms over time (broken down by the number of new firms launched each year versus active existing firms) is displayed in Fig. 1.4. These figures were calculated using the vintage year of the first fund to represent the year in which a firm was established; firms that have not raised a fund within the past 10 years were considered inactive.

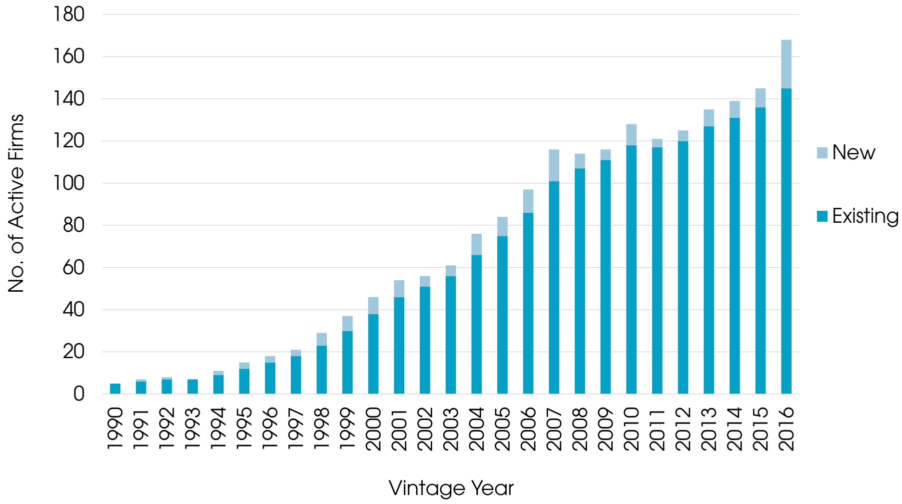
Overall, there has been clear growth in the private capital industry, indicative of the positive developments across alternative assets as a whole since 1990, with 168 Australia-based private capital firms identified as active in 2016. The rate of growth has varied, peaking with 15 newly formed private capital firms in 2007, after which the yearly rate slowed down as a result of the difficult fundraising environment post-crisis. Since 2011, there has been annual growth in the number of firms established and more recently, 23 new firms were identified between January and August 2016, the highest number of new firms entering the market on record.

Furthermore, these totals are boosted by the numbers of new hedge fund managers and vehicles incepted each year (Fig. 1.5). There have been an average of six hedge fund managers incepted and 21 hedge funds launched annually since 2006, with the peak for new managers witnessed in 2009 (16) and funds launched in 2012 (27).

Participation in Alternatives

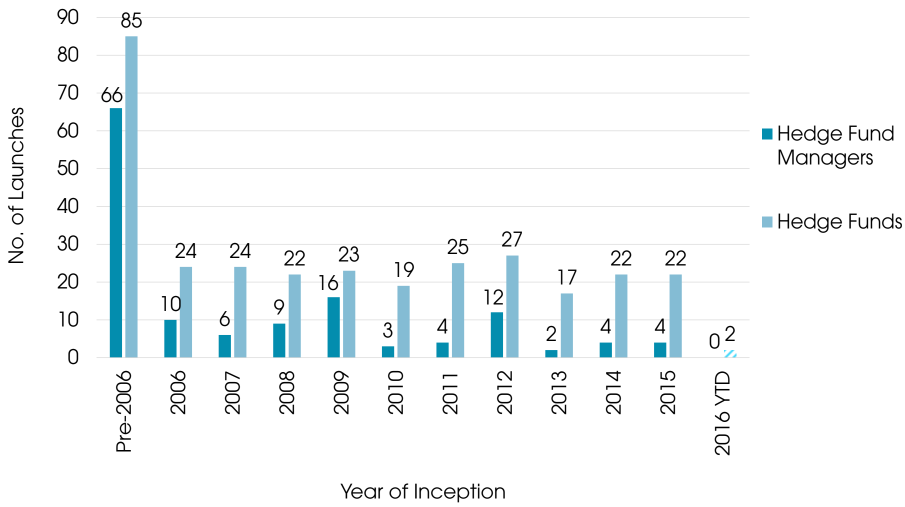
The majority (61%) of institutional investors based in Australia invest in at least one alternative asset class, including a significant proportion (30%) that invest in at least three alternatives as part of their investment portfolios (Fig. 1.6).

Fig. 1.4: Number of Active Australia-Based Private Capital Firms over Time (By Vintage of First Fund Raised)



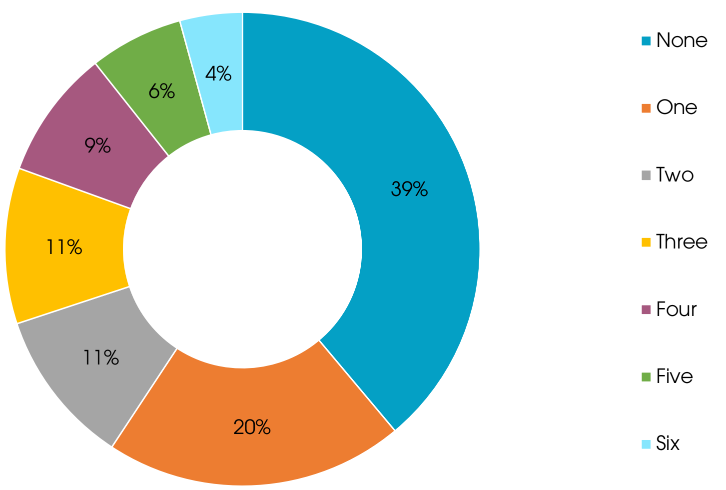
Source: Preqin

Fig. 1.5: Number of Australia-Based Hedge Fund Managers Incepted and Hedge Fund Launches by Year of Inception (As at August 2016)



Source: Preqin Hedge Fund Online

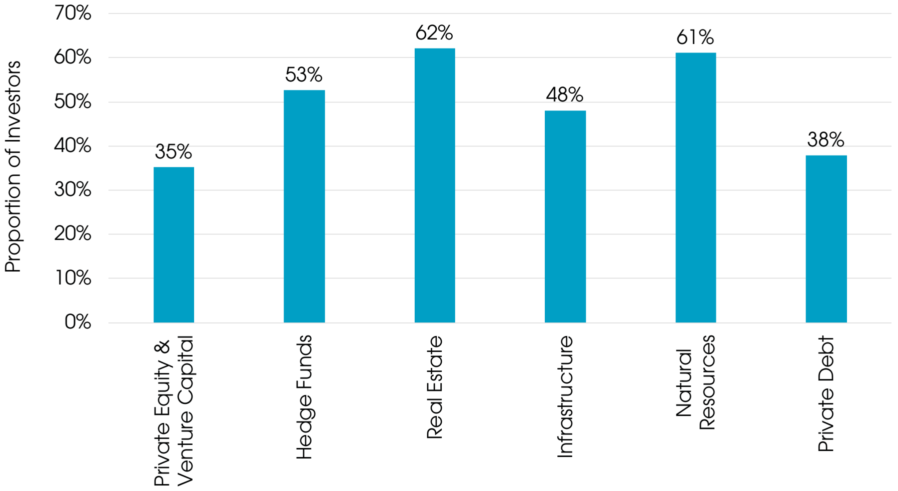
Fig. 1.6: Australia-Based Institutional Investors by Number of Alternative Asset Classes Invested In



Source: Preqin

In terms of individual asset classes, real estate, natural resources and hedge funds have the largest proportions of participating investors: 62%, 61% and 53% of Australia-based investors are investing in these asset classes respectively (Fig. 1.7). Despite the large and active infrastructure deal environment in Australia (see page 37, Infrastructure: Deals), only 48% of investors in the country target infrastructure investment, although this is still greater than the proportions targeting private equity & venture capital (35%) and private debt (38%) investment.

Fig. 1.7: Proportion of Australia-Based Institutional Investors Allocating to Each Alternative Asset Class



Source: Preqin

Data Source:

With global coverage and detailed information on all aspects of alternative assets, Preqin's industry-leading online services keep you up-to-date on all the latest developments in the alternative assets industry.

View in-depth profiles for over 2,900 private capital funds currently in market and over 15,400 hedge funds open to new investment, including information on investment strategy, geographic focus, key fund data, service providers used and sample investors.

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Private Equity in Australia

- Shannon Wolfers, Director, Pacific Equity Partners

Three Australia-based private equity managers feature among the World's 20 Most Consistent Buyout Fund Managers (Preqin, 2016). Put a different way, 15% of the top performing fund managers are based in a location which accounts for less than 1.5% of the total number of private equity fund managers. Shannon Wolfers of Pacific Equity Partners explores the reasons for this success – or as Australians might put it – why the country "punches above its weight".

1. Stable and Growing Economy

Statistics of Australia's macroeconomic picture are important here. Australia is entering its 26th consecutive year of economic growth: real GDP growth of 3.3% per annum since 1991 compares favourably to other developed economies. This growth is underpinned by positive population dynamics – the Australian lifestyle is a magnet for long-term migrants. This, when combined with rising natural birth rates, is delivering population growth of 1.5% per annum, more than double the rate of most developed economies.

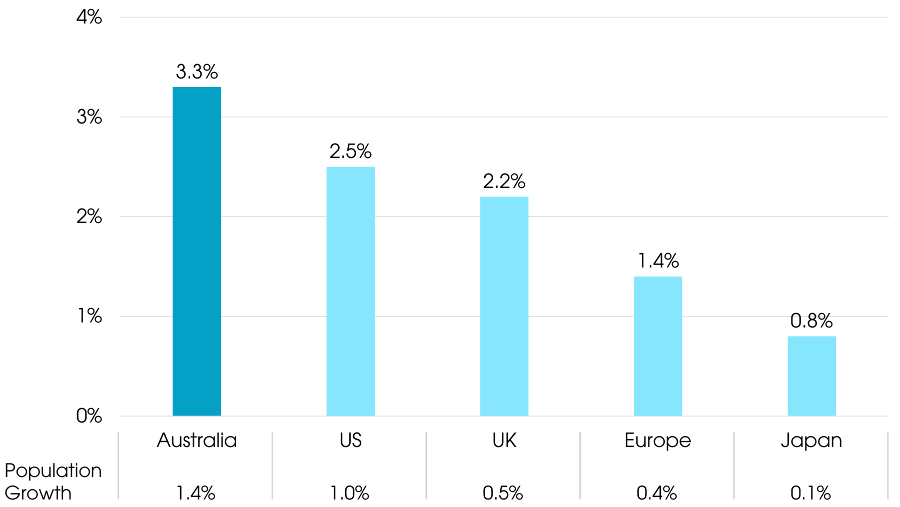
Australia's relatively young population, combined with a government mandated retirement savings scheme, means the country is not as exposed to the demographic time bomb of unfunded retirement liabilities. Similarly, government debt levels remain among the lowest in the OECD (19% of GDP).

The stereotype of Australia as "a big quarry" – i.e. iron ore and coal mining – is misunderstood. Few appreciate that mining accounts for just 10% of GDP and less than 2% of employment. It is instead a domestically driven economy with GDP growth comprising ~80% internal demand and only ~20% exports. The economy is dominated by service industries – representing more than 70% of GDP – reflecting the fact that Australia is one of the most urbanized countries in the world.

It used to be said that Australia suffered from a "tyranny of distance" thanks to a location so divorced from the Western markets of the northern hemisphere. Today, Australia's service-driven economy is ideally positioned to service Asia's growing middle class.

China accounts for only 6% of GDP today, and the majority of this comprises exports of the world's lowest cost iron ore and coal. On the other hand, the growth opportunity exists to sell products and services to the middle class in China, where the sheer scale of the segment

Fig. 1: Real GDP Growth, 1991 - 2015



Source: International Monetary Fund

creates for Australian businesses a "mass market" opportunity.

By way of example, inbound tourism from China has grown almost 3x over the last six years to about one million visitors a year. Similarly, education is now Australia's third biggest export earner – its growth is soaring, with more international tertiary students studying in Australia than the UK or Canada. China is now also the second largest export market for Australian wine with exports rising 64% over the past year. These trends are supported by recent free trade agreements signed with China, Japan and South Korea.

Much to the surprise of those who saw Australia as simply a leveraged commodity play on China's rampant growth, a strong domestic, service-oriented economy lies at the heart of a growth rate which is among the highest in the Western world.

2. Significant Deal Opportunity Set

Against this strong macroeconomic environment lies a well-established and sound legal system, providing the bedrock for a wealth of M&A opportunities.

Australia is not a small market for M&A by global standards. It is the sixth largest M&A market in the world, even accounting for the exclusion of resource deals not typically the domain of private equity: US$160bn of M&A activity in FY 2014-2015 exceeded that of Japan, Canada, Brazil, India, Hong Kong or Italy.

Critically, M&A is relatively underpenetrated by private equity in Australia, representing a unique opportunity. To illustrate, some 16% of M&A activity in FY 2015 was private equity-driven – approximately half the level of other developed markets such as the US, UK, Japan and the Eurozone.

The private equity environment is underpinned by a stable financial services system. Australia's financial economy is dominated by four large domestic banks: all four banks are prudent lenders, rated by the credit agencies among the top 20 banks in the world. The market capitalization of Australia's largest bank (Commonwealth Bank) stands at more than A$130bn, putting it in the top 10 largest banks globally.

This bank-dominated credit market does not suffer from the same volatility as bond markets. In offshore, institutionally driven markets, investor sentiment can drive wild swings in both availability and cost of leverage. Instead, in Australia, sustainable levels of leverage are consistently available through the cycle. Senior leverage levels of 4-5x EBITDA are available to proven private equity players, at a total cost of ~6% per annum. Mezzanine debt is available in addition to that.

The size of the market and the consistent availability of debt at sustainable levels to select players makes for an attractive environment for acquiring assets.

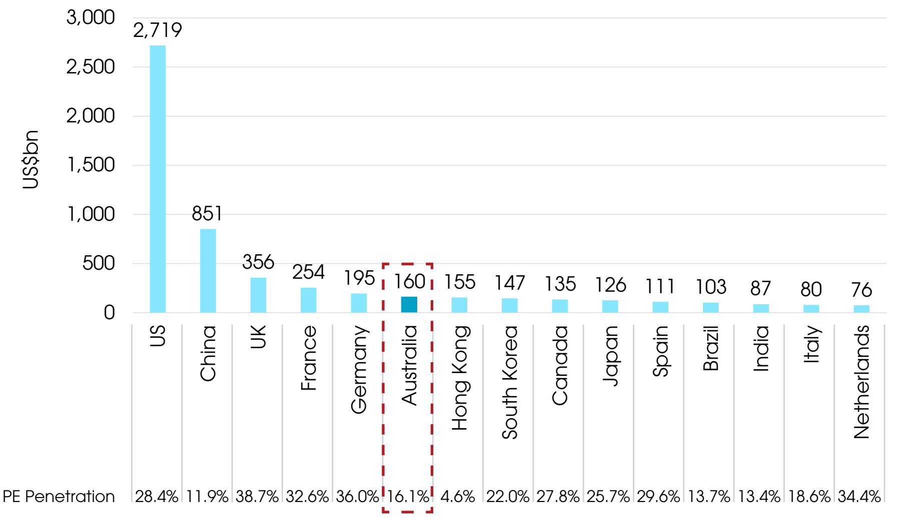
3. Rational Competitive Set

Attractive market structures are a common feature of Australia's economy. Most major industries are characterized by stable oligopolies: there are two large supermarket chains, four banks, three telecommunication companies. Private equity is no different.

In the mid-market (that is, enterprise value of A$200mn to A$1bn plus) where PEP invests, there are three local private equity players, all of which have been operating in the market alongside one another for a long time. Each pursues a different investment strategy, making it rare for firms to compete for assets. Across the pool of all 48 mid-market deals undertaken over the last 10 years, only two saw competition between the different private equity players.

This segmented market ensures buyout multiples remain in check. While the price of EV multiples in the rest of the world average 11x EBITDA, the average entry price for buyouts in Australia over the last five years is 8.2x EBITDA.

Fig. 2: Non-Resource M&A Activity, FY 2014-2015



Source: Dealogic, PEP Deal Database

4. Attractive Industry Returns

The upshot of this is that average returns for private equity funds in Australia are well above these of the rest of the world. Returns are also more consistent over time – the same few players keep delivering strong results year in, year out.

An analysis of Preqin data across all buyout and late stage funds globally since 1998, which compares the average returns and dispersion of returns by fund and by geography, shows this clearly. On average, the Australian private equity industry has delivered 20% net IRRs over the long term, a 6% premium to global benchmarks; this has been achieved at substantially lower dispersion risk than in other geographies. Australian private equity provides the scale, quality and consistency of returns necessary to underpin any diversified Asian portfolio strategy.

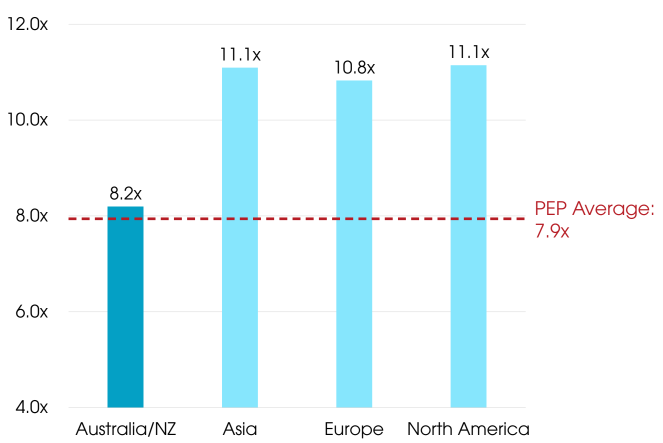
Pacific Equity Partners

PEP Funds take control positions in a select group of Australian and New Zealand companies with enterprise values in the range A$200mn-A$1bn. Operating company management are provided with capital and resources as necessary to deliver full potential.

Established in 1998, the firm has made 26 operating company investments, over 90 bolts-ons and joint venture acquisitions at the company level and manages around A$3.5bn of equity funds. Recent investments have spanned industrial, energy, food, consumer products, entertainment/media and the financial services industries.

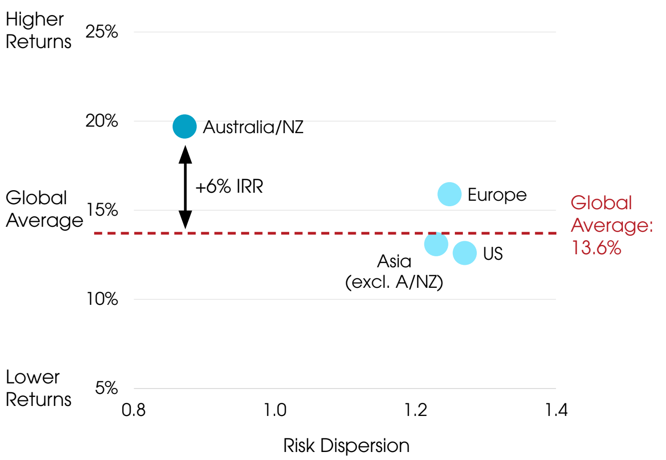
www.pep.com.au

Fig. 3: LBO EBITDA Multiples (Five-Year Average)



Source: UBS, Dealogic, Mergermarket, Company Reports and Announcements, Press, PEP Deal Database

Fig. 4: Risk/Return, 1998-2016



Source: Preqin as at February 2016; All "Buyout" and "Expansion/Late Stage" Fund Vintages from 1998

Note: Return is average net IRR, Risk is variability to the average net IRR

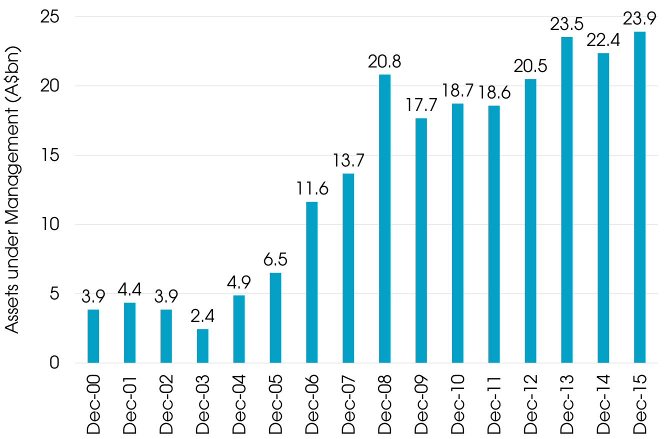
Assets under Management, Dry Powder and Performance

The private equity market in Australia has shown strong growth over the last decade, with the AUM – defined as uncalled capital commitments (dry powder) plus the unrealized value of portfolio assets – of Australia-based firms now 3.7 times higher than in 2005, standing at A$23.9bn as of December 2015 (Fig. 2.1). The vast majority of this total is held in unrealized value (71%, A$17bn).

Unsurprisingly, the Australian buyout industry is far larger than any other private equity strategy, accounting for three-quarters (A$18.1bn) of private equity AUM, and representing the same proportion of dry powder and unrealized value (Fig. 2.2). This total far surpasses the AUM attributed to venture capital (A$3.4bn), growth (A$0.8bn) and other private equity* fund types (A$1.5bn).

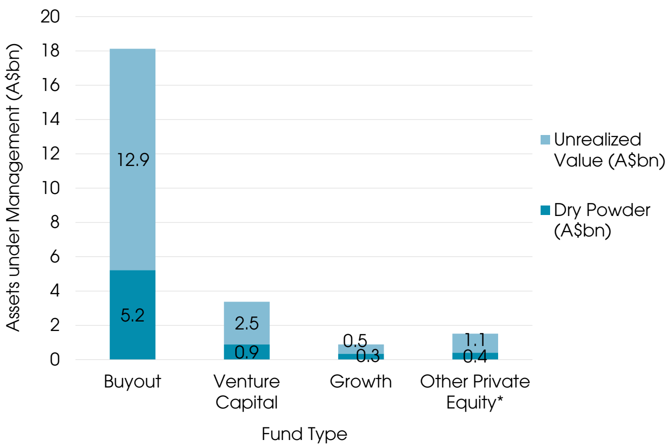
The top performing Australia-based venture capital fund is the 1998 vintage AMWIN Innovation Fund, which achieved a net multiple of 5.47x with a net IRR of over 1,000%. The best performing buyout vehicle is Anacacia Partnership I; the A$53mn fund achieved a net multiple of 3.21x with a net IRR of 41.0%.

Fig. 2.1: Australia-Based Private Equity & Venture Capital Assets under Management, 2000 - 2015



Source: Preqin Private Equity Online

Fig. 2.2: Australia-Based Private Equity & Venture Capital Assets under Management by Fund Type (As at December 2015)



Source: Preqin Private Equity Online

Fig. 2.3: Top Performing Australia-Based Private Equity & Venture Capital Funds by Net Multiple (All Vintages)

Fund	Firm	Vintage	Fund Size (mn)	Type	Geographic Focus	Net Multiple (X)	Net IRR (%)	Date Reported
AMWIN Innovation Fund	CHAMP Ventures	1998	42 AUD	Early Stage	Australasia	5.47	1,015.7	Dec-14
African Lion	Lion Manager	1999	34 USD	Early Stage	Africa	3.58	24.8	Jun-16
Anacacia Partnership I	Anacacia Capital	2007	53 AUD	Buyout	Australasia	3.21	41.0	Jun-16
Archer Capital Fund II	Archer Capital	2001	192 AUD	Buyout	Australasia	2.78	48.6	Jun-16
Brandon Bioscience Fund No. 1	Brandon Capital Partners	2008	50 AUD	Early Stage	Australasia	2.72	24.1	Mar-16
Pacific Equity Partners Supplementary Fund II	Pacific Equity Partners	2004	162 AUD	Buyout	Australasia	2.70	61.9	Mar-16
Quadrant Capital Fund II	Quadrant Private Equity	1998	75 AUD	Buyout	Australasia	2.57	31.9	Jun-16
Quadrant Capital Fund III	Quadrant Private Equity	2001	125 AUD	Buyout	Australasia	2.50	64.4	Jun-16
Australian Mezzanine Investment No. 2 Trust	CHAMP Private Equity	1993	50 AUD	Venture Capital (All Stages)	Australasia	2.47	19.9	Jun-16
Pacific Equity Partners Fund II	Pacific Equity Partners	2004	316 AUD	Buyout	Australasia	2.42	36.1	Mar-16

Source: Preqin Private Equity Online

**Other includes Balanced, Co-Investment, Direct Secondaries and Turnaround funds.*

LP Opportunities in the Australian Private Equity Mid-Market

- Interview with Jeremy Samuel, Managing Director, Anacacia Capital

Your Anacacia Partnership I fund is the highest ranked Australian buyout fund with ~40% net IRRs since 2007 and >4x gross return. How strong is demand for private equity from Australian smaller mid-market businesses?

Australia is a small business economy.

Demand for private equity among small-medium enterprises (SMEs) is very strong in Australia. There are tens of thousands of SMEs that are sizeable, established and profitable.

Many of these companies are facing succession issues as the "baby boomer" owners are reaching retirement age.

By contrast, there are only about 300 companies in Australia with a market capitalization of over A$300mn.

How competitive is it for deals in the Australian smaller mid-market?

The competition is relatively limited. However, the "competition" is usually the business owner determining whether or not they want to sell their business at that point.

One major change in the Australian landscape is that fewer firms are managing more and more capital. There are very few private equity funds with say A$100-400mn under management that focus here.

This creates a supply-demand imbalance in the Australian smaller mid-market. This inefficiency makes the segment attractive for investors.

What other key drivers do you attribute for Anacacia's strong returns?

There is no single factor and we are working hard each day to be better but here are some thoughts.

We have a sizeable, highly experienced 10-member investment team, supported by a seven-member Business Advisory Council (BAC). The BAC members are leading business people with deep operational experience. Some view them like operating partners. They get very involved with portfolio companies and assist with due diligence and board support.

Each member of the investment team and the BAC has committed significant personal capital to co-invest alongside our LPs. So we focus a lot on achieving the best possible risk-adjusted returns.

Our strategy is basically to invest with profitable, established SMEs. We structure our deals with preference equity and take control positions. That way we can take charge if things are not progressing according to plan, although the focus is on partnering with the best possible management teams.

Our investment process is a contributing factor. On origination, we have a record of only committing resources to due diligence when we have exclusivity on a potential deal and there is a good people fit with management. The supply-demand imbalance makes this easier and ensures that we have completed more rigorous due diligence prior to any investment.

Once invested, we typically have 2-3 of our team as active non-executive directors assisting with strategy and operations.

We also focus heavily on achieving successful exits. The exit strategy of each portfolio company is a key focus in our initial due diligence and something that we regularly revisit during the term of our investment. Once it comes time to exit, we play a very hands-on role in that process.

What are Anacacia's usual fund terms and how do you balance some investors' concerns about fees with returns?

Anacacia's fund terms are industry standard with a strong focus on aligning interests. We manage small funds and we have a relatively large team. The performance fee, rather than the management fee, is the key motivator for our investment professionals.

We are very aware of fee constraints on LPs. To minimize the fee drag on each of our private equity funds, we have always rebated 100% of any director or other fees from portfolio companies back to the fund. This means that while the manager accrues the usual 2/20 formula, in reality, the fees charged directly to the fund (and to investors) are often negligible and well below 1%.

We are also investing in profitable companies that have the capacity to pay dividends early, and often do. This helps reduce the usual J-curve of private equity.

Do you have any other options for investors that want access to the small to mid-market but are liquidity and fee constrained?

We are also seeing opportunities in the listed market and have created the Wattle Fund for investors that want to have exposure to listed SMEs in addition to our private equity funds.

The Wattle Fund invests in ~20 listed emerging SMEs including 8-12 high-conviction positions. The focus is mainly on companies with a market cap of A$20-200mn (and up to a maximum of A$500mn).

Australia is an attractive niche market for listed SMEs due to market inefficiencies. For example, there are ageing founders and passive financiers that hold material stakes and/or SMEs that want to place capital with a partner for growth, succession, sell-downs or acquisitions.

However, supply of institutional capital for such SMEs is limited. Broker coverage of this segment is also thin, which allows our team to spend more time with boards and senior management of the target SMEs and analyze the information better than others. The fund targets double-digit net absolute returns and has returned more than 25% since early 2015.

The Wattle Fund has also brought enormous synergies for our private equity origination and portfolio management. There is great sharing of knowledge across the team to benefit both funds.

Can you take us through the key characteristics of a recent successful investment?

Sure, our investment in Rafferty's Garden won many awards including the local industry AVCAL Chairman's Award. Our investors particularly liked this investment because it was so successful at growing and returning about 10 times the investment during the Global Financial Crisis.

We conducted top-down industry research into the Australian branded food market. We were looking for innovative brands that would have pull with the retailers and international appeal.

We cold-called the major shareholder and founder of Rafferty's Garden, a branded baby food company that at the time was achieving around A$20m revenue.

Cutting a long story short, we worked on due diligence exclusively for several months. We then invested in a control position using preference equity alongside management. We hired a new CEO, CFO and other senior executives to work alongside the existing team. Two of us joined the board as very active non-executive directors.

Three years later we had grown the business to about 40% domestic market share and commenced an export business. We sold the company to a listed UK business that had the global distribution to take the business to the next level.

Are you seeing other opportunities similar to Rafferty's Garden?

Of course not everything works as well, but yes, we have been fortunate to have several similarly successful investments. For example, in 2009 we invested in Appen, a language technology services business. The founding husband and wife team were reaching retirement age when we approached them.

Again, we took a controlling preference equity position, strengthened the management team and by 2015 we listed the company on the Australian Securities Exchange.

The business has grown such that its monthly revenue and earnings are now about the same as its annual performance back in 2009. Its clients include nine of the world's 10 largest technology companies.

Today's share price is more than 30x our initial entry price. With a staged sell-down, we have made 12x our initial investment including still holding some shares.

When does Anacacia plan on raising its next private equity fund?

We expect to raise Fund III in early 2017 based on the current drawndown rate. Using historical deal flow as a measure, we expect to continue to see plenty of interesting investment opportunities. This will enable us to pursue the same strategy as predecessor funds and remain focused on investing in leading SMEs. We expect existing LPs to take up most of the demand with some capacity for a small handful of new investors.

Anacacia Capital

Anacacia Capital is an award-winning Australian private equity firm that invests in established and emerging small-medium enterprises (SMEs) in the mid-market. An acacia tree adapts to its arid Australian environment, resilient in good and tough times, producing gold wattle flowers each year.

Anacacia funds include private equity limited partnership (VCLP) funds for private companies and the Wattle Fund for small listed companies. The firm manages more than A$250mn of committed capital.

www.anacacia.com.au

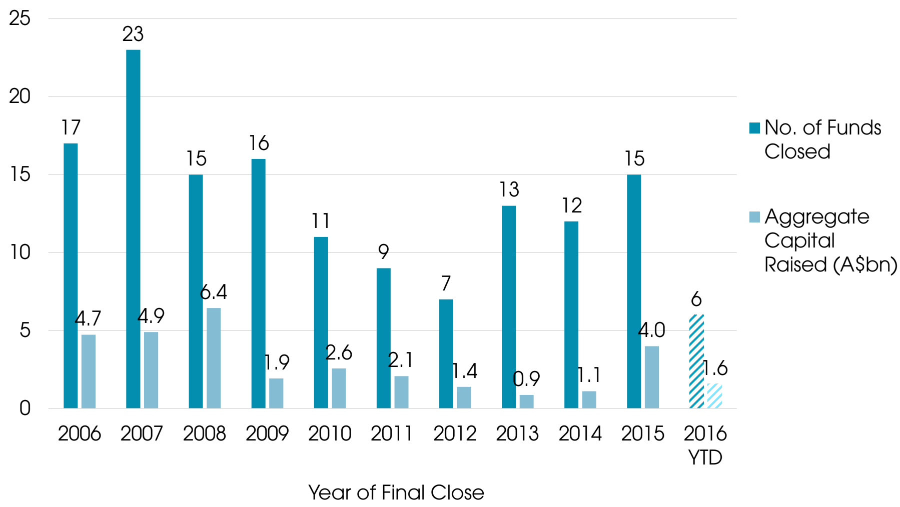
anaCacia Capital

Fundraising

Fundraising by Australia-headquartered GPs has fluctuated over time, with annual capital raised in recent years failing to surpass the A$6.4bn secured from 15 vehicles reaching a final close in 2008 (Fig. 2.4). However, 63% of this total was raised by just one fund, Pacific Equity Partners Fund IV, which secured just over A$4bn for investment in buyout opportunities in Australia and New Zealand.

While the number of funds reaching a final close grew in 2009 to 16, there were three consecutive years of decline following this, despite the average capital raised annually fluctuating around A$2bn. Recent years have seen an increase in the number of funds closing, although aggregate capital raised reached lows of A$0.9bn and A$1.1bn in 2013 and 2014 respectively.

Fig. 2.4: Annual Australia-Based Private Equity & Venture Capital Fundraising, 2006 - 2016 YTD (As at August 2016)



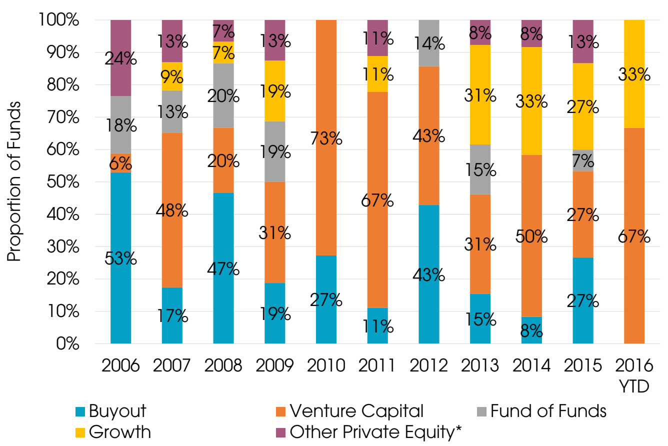
Source: Preqin Private Equity Online

Illustrating the influence of large fund managers on the Australia-based fundraising market, the post-crisis peak of A$4bn raised in 2015 saw Pacific Equity Partners Fund V secure more than half the total; however, figures so far in 2016 have been encouraging for the asset class in Australia as a whole, with six vehicles closed securing A$1.6bn.

Unsurprisingly, despite buyout vehicles securing the majority of Australia-based capital, venture capital funds have been more prevalent in the marketplace, representing 38% of funds closed since 2006 (Fig. 2.5). Although buyout funds constituted the largest proportions of funds closed in 2006, 2012 and 2015, when excluding these years, buyout funds represent an average of 18% of the Australia-based private equity fundraising market. Recent years have seen growth funds come to the fore, with 31% of funds closed since 2013 following a growth strategy.

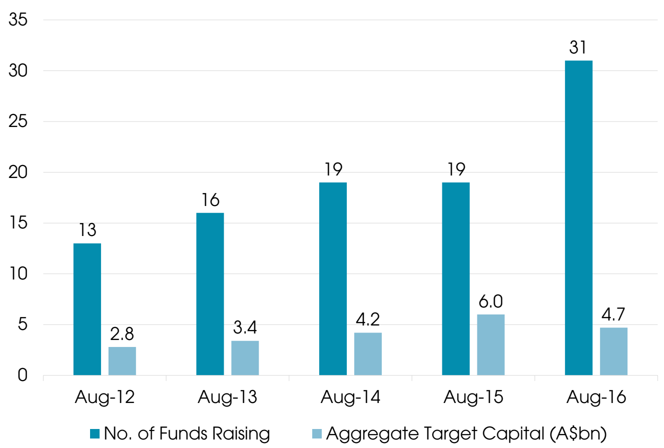
Furthermore, Australia-based GPs are keen to capture the momentum generated from recent fundraising successes: there are now 31 Australia-based private equity funds in market profiled on Preqin's **Private Equity Online**, targeting A$4.7bn in institutional capital commitments, as seen in Fig. 2.6. While this is a slight reduction on the A$6.0bn targeted by these vehicles in August 2015, the number of funds seeking capital is at its highest point on record, far surpassing the previous peak of 19 in both 2014 and 2015 and is indicative of the growth of the asset class in Australia.

Fig. 2.5: Australia-Based Private Equity & Venture Capital Fundraising by Fund Type, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Private Equity Online

Fig. 2.6: Australia-Based Private Equity & Venture Capital Funds in Market over Time, August 2012 - August 2016



Source: Preqin Private Equity Online

**Other includes Balanced, Co-Investment, Direct Secondaries and Turnaround funds.*

Australia's Appeal

- Yasser El-Ansary, Chief Executive, AVCAL

The global economic landscape remains uncertain since the Global Financial Crisis (GFC), with advanced economies still struggling to regain the momentum of the early to mid-2000s. Political shocks such as the UK's decision to exit the European Union will take years to play out, while in the US, a presidential election in November 2016 promises a change in leadership and possible direction.

Meanwhile, Australia has shown considerable economic resilience by managing to survive the GFC with limited damage, and although the national growth outlook remains relatively subdued, it is the envy of other developed nations. As at August 2016, the Reserve Bank of Australia put economic growth at 3.1%, and the unemployment rate at 5.8%. Indeed for the last 25 years, Australia has avoided a recession.

Despite this strong economic performance, the recent end of the resources boom and the need to find and support the next driver of Australia's economic growth has been front of mind for government and policy makers. The government's National Science and Innovation Agenda (NISA), announced in December 2015, focused on addressing this challenge. The aim of the NISA was to put in place the right settings to encourage greater investment and growth in start-ups and other innovative sectors of the economy, increase productivity and build future industries.

The NISA was an important step in the right direction for Australia's venture capital (VC) sector, which funds hundreds of high-growth early stage companies that are developing new technologies and commercializing innovative products and services. A more entrepreneurial culture is emerging supported by new tax incentives and government programs aimed at backing promising ideas.

But the real driving force behind Australia's economic prosperity has, for decades, been the thousands of small and medium-sized businesses (SMEs). These SMEs operate in every region and community, and provide millions of jobs. SME business owners can often struggle to find the right sources of funding and the right partners to help them grow their businesses. This is where later stage VC and private equity (PE) has played an important role by providing capital, networks, business expertise and experience in order to expand.

PE funds typically invest in established businesses that need expansion capital, more management attention, strategic direction, or the potential to turn around a struggling business and make it profitable again. Unlike many other asset classes, PE involves an active 'hands-on' approach from PE fund managers. From the due diligence and investment phase, to the active management of the portfolio companies that have been invested in, and right through to the exit process, the PE firm is involved. This investment model, along with incentive structures designed to align the interests of investors and fund managers (e.g. performance hurdles, carried interest, fund managers committing their own capital to their funds), are some of the factors that explain why PE has performed so strongly compared to other asset classes both over short- and long-term periods.

According to Preqin data, Australia-based PE funds launched since 2000 have delivered an average net of fees internal rate of return of 19.2%. Meanwhile, the S&P ASX 300 Index has returned 7.7% over 15 years, and the Small Ordinaries Index has returned only 5.8% over the same period. This data shows the outperformance that investors allocating to Australian PE funds can achieve relative to other asset classes. Indeed such returns are the envy of global fund managers worldwide where the search for yield has become increasingly difficult in an environment of slow or negative growth and low interest rates.

Companies that have been backed by PE also tend to perform well even when the PE funds have divested their holdings. Research released by AVCAL and Rothschild in February 2016 showed that PE-backed IPOs with minimum offer sizes of A$100mn that took place from 2013 to 2015 on the ASX delivered an average return of 41%, outperforming non PE-backed IPOs by around 15%.

Despite this impressive track record, it is worth noting that the Australian PE market is still relatively young compared to other developed markets such as the UK or the US, with significant untapped potential. The under-penetration of PE in Australia is illustrated by the number of PE transactions as a percentage of total M&A transactions: in Australia, PE deals accounted for an average of 6.6% of all M&A deals over FY 2011 to FY 2015, compared with an average of 21.4% in the UK and 24.4% in the US over the equivalent period.

Fundraising levels reflect the opportunities on offer, with FY 2015 seeing an almost tripling of investor commitments on FY 2014 levels – from A$933mn to A$2.7bn. This has been driven largely by Asian investors keen to capitalize on Australian opportunities. Around 70% of investor commitments to Australian PE and VC funds now come from offshore, with a particularly strong presence from sovereign wealth funds, pension funds, funds of funds and family offices.

In the time since the first PE and VC funds were launched in Australia some 40 years ago, the market has matured to become a diverse ecosystem that supports businesses throughout each phase of growth, across almost all sectors of the economy. This has translated into a significant economic contribution delivered by our industry. Companies backed by PE in Australia support an estimated half a million jobs and contribute A$59bn p.a. in total value added to GDP, or approximately 4% of the economy. These companies operate across a wide range of industry sectors, including healthcare, retail, financial services and information technology.

At the early stage end of the market, there are many domestic VC funds providing seed capital to entrepreneurs to build innovative start-ups and commercialize the latest technological advances. According to AVCAL data, early stage VC investments accounted for 82% of all companies backed by VC in Australia in FY 2015.

Australia's attractiveness as an investment destination has also brought a number of international VC funds, such as those that have backed Atlassian, Campaign Monitor and BigCommerce, to the local market. They typically invest larger amounts than Australia-based VC funds, so this is one area (late stage funding) where Australia can do more to increase the level of capital available to companies that are coming out of the start-up phase and scaling up into sizeable businesses. This might be about to change, however, with fundraising levels expected to reach a record high of around A$1bn in FY 2016 (a tripling of FY 2015 levels), opening up the potential for larger, later stage deals.

For established businesses that are seeking to expand into new regions, increase their productive capacity or develop a new product line, growth/expansion PE funds will invest in those businesses. In Australia in FY 2015, these investments made up 40% of all PE funds invested in Australia. At the large end of the market, local fund managers and global PE firms conduct buyouts of companies, including acquiring listed companies through public-to-private transactions. These deals represented 43% of transactions in FY 2015.

In FY 2015, most PE investment in Australia was in two broad sectors: business/industrial products and services and consumer/retail products and services. They accounted for 60% of dollars invested, and 57% of companies that received PE funding in that year. Businesses in these sectors tend to have large customer bases and generate strong cash flows, which are important for PE fund managers to be able to reinvest in and grow their portfolio companies.

Healthcare has also provided good opportunities for PE investment, in part due to the ageing demographic trends that are shaping the Australian population. Not only have tried and tested healthcare businesses like hospital operators and makers of healthcare products been transformed by PE capital in Australia, but new pharmaceutical drugs and medical devices are being backed by Australian PE and VC funds. These have the potential to change the lives of patients and their families around the world, at the same time as generating significant returns for investors.

An estimated US$5.8bn of dry powder is currently available to Australian PE funds, according to Preqin data. While this sounds large, at current rates of investment this would be deployed within two to three years by Australian GPs. So Australian fund managers continue to look for sophisticated institutional investors, both domestic and offshore, to help build a broad capital base.

Domestically, policy work is being done to develop a world-class limited partnership collective investment vehicle to bring Australia in line with international PE and VC practice. This reform has the potential to harmonize Australian structures and further attract high-quality offshore investors.

More broadly, the Federal Government is moving onto the next stage of innovation policy focused on transforming existing 'scale-up' businesses. Schemes such as a new National Innovation co-investment fund are being explored with industry, and further work is being done to forge closer links between the research and private sectors with the Biomedical Translation Fund potentially game-changing for that sector.

More broadly, there is bipartisan political commitment to support Australia's transition into a dynamic, knowledge-intensive economy with deep commercial links to Asia. Recent free trade agreements with China, Japan and South Korea, along with ongoing negotiations with high-growth countries such as India and Indonesia, underscore the potential for Australia to capitalize on its geographic location.

Australia is therefore well positioned to succeed in the "Asian Century" with PE- and VC-backed businesses capable of servicing the needs and wants of a rapidly growing Asian middle class eager to buy high-quality goods and services. It is these high-growth opportunities that will lie at the heart of PE and VC business strategies both now and well into Australia's future.

AVCAL

The Australian Private Equity & Venture Capital Association Limited's (AVCAL) members comprise most of the active private equity (PE) and venture capital (VC) firms in Australia, who together manage around A$28bn on behalf of Australian and off-shore superannuation and pension funds, sovereign wealth funds and family offices.

PE and VC firms provide capital for early stage companies, later stage expansion capital, and capital for buyouts of established companies. Over the last 10 years, PE and VC invested around A$32bn in almost 900 Australian companies. In FY 2015, PE and VC funds invested A$3.3bn into 140 Australian companies, across almost all sectors of the economy.

www.avcal.com.au

Deals and Exits

Buyout Deals

Since 2006, private equity-backed buyout deals in Australia have represented, on average, 15% of all Asia-Pacific deal flow. In this period there have been 650 buyouts for an aggregate A$82.1bn, although activity has generally fluctuated annually, with peaks in the number of deals seen in 2007 (71), 2012 (79) and 2015 (69), as shown in Fig. 2.7.

Furthermore, while deal flow has recovered post-crisis, deal value has failed to surpass the A$20bn witnessed in 2006; in 2015, however, A$17.6bn worth of deals was announced or completed.

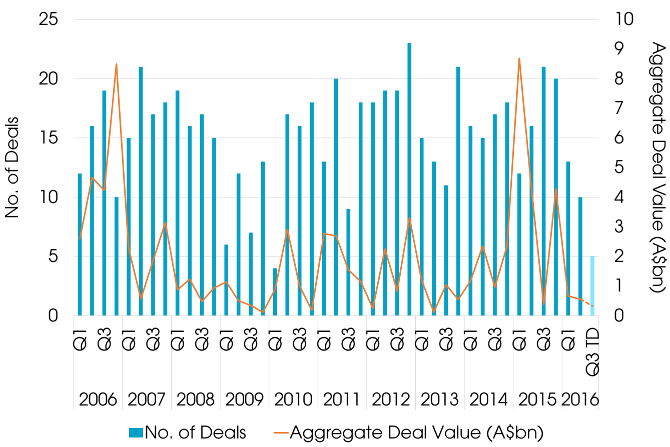
Over the same period, there have been 259 private equity-backed exits, valued at an aggregate A$57.2bn (Fig. 2.8). While trade sales represent the largest proportion of Australian exits, there has been an improvement in IPO activity since 2013, with 2014 seeing equal numbers of trade sales and IPOs from private equity-backed companies.

Venture Capital Financings

There have been 530 venture capital financings in Australia since 2006 for an aggregate A$2.9bn (Fig. 2.9). However, the environment has changed over recent years; greater numbers of financings have occurred from 2011 onwards, with annual deal flow surpassing 100 transactions for the first-time in 2015 (104). Correspondingly, aggregate deal value has risen annually since 2009, with the 2015 figure standing at A$842mn, an all-time high.

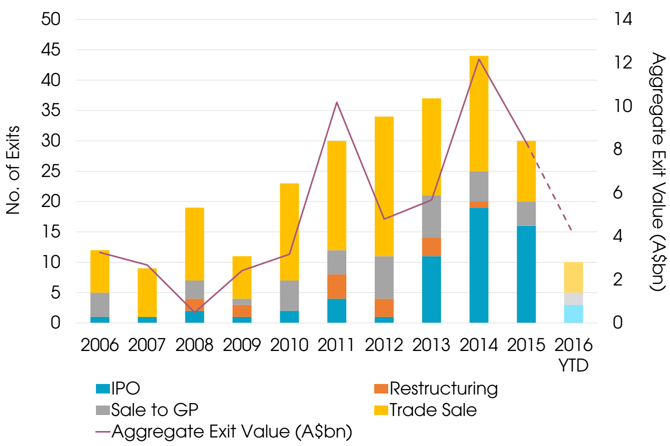
Venture capital deals in the healthcare sector represented a larger proportion of deals from 2007-2011 than for more recent years, with the sector average falling from 29% in 2007-2011 to 12% for deals post-2011. Contrastingly, internet financings have come to represent the largest share (26%) of venture capital financings since 2011.

Fig. 2.7: Number and Aggregate Value of Australian Private Equity-Backed Buyout Deals, Q1 2006 - Q3 2016 TD (As at August 2016)



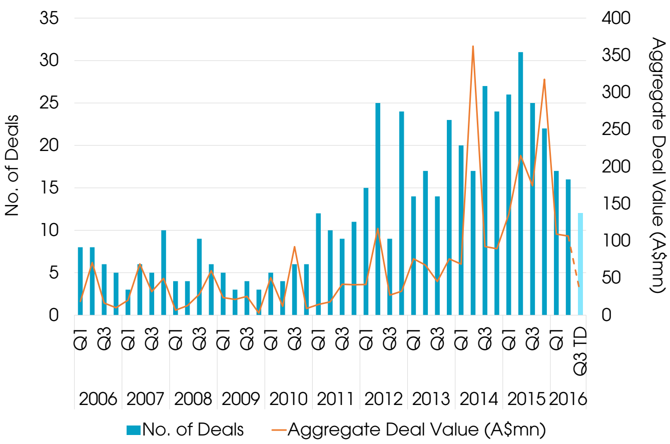
Source: Preqin Private Equity Online

Fig. 2.8: Number and Aggregate Value of Australian Private Equity-Backed Buyout Exits by Type, 2006 - 2016 YTD (As at August 2016)



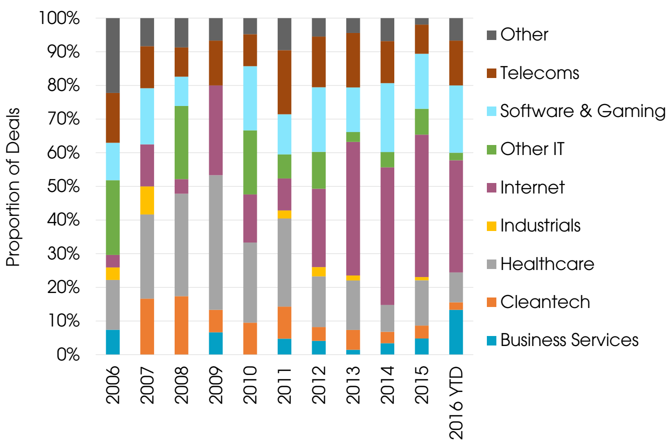
Source: Preqin Private Equity Online

Fig. 2.9: Number and Aggregate Value of Australian Venture Capital Deals*, Q1 2006 - Q3 2016 TD (As at August 2016)



Source: Preqin Private Equity Online

Fig. 2.10: Australian Venture Capital Deals* by Industry, 2007 - 2016 YTD (As at August 2016)



Source: Preqin Private Equity Online

**Figures exclude add-ons, grants, mergers, secondary stock purchases and venture debt.*

Investors

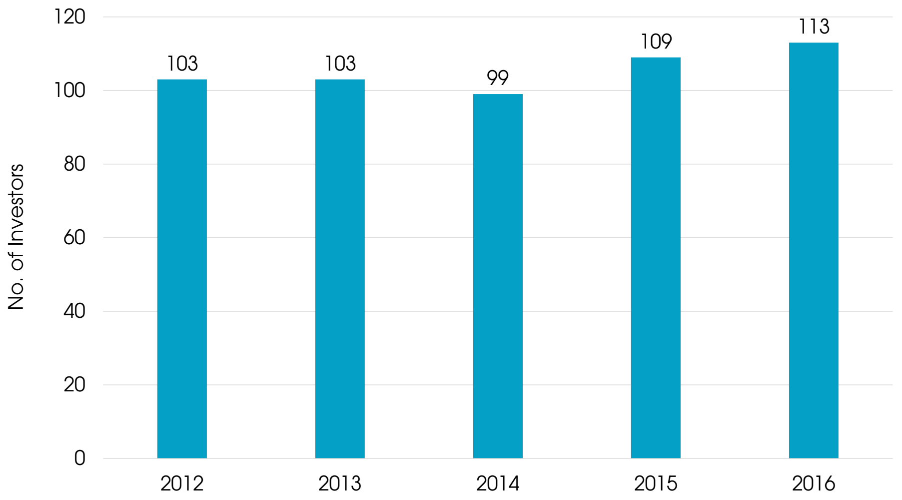
The number of active institutional private equity & venture capital investors has remained relatively stable, although there has been greater numbers of entrants to the asset class over 2015 and 2016 (Fig. 2.11). As of August 2016, there were 113 active institutional investors in the asset class based in Australia.

The average current allocation of an Australia-based LP in 2016 stands at 4.4% of total assets, below the 7.7% of total assets held by all investors globally. Furthermore, the 5.1% target allocation is four percentage points below that of all other investors. Over time, Australia-based allocations have fallen slightly, a potential result of new entrants to the asset class holding smaller proportions of their total assets in private equity (Fig. 2.12).

The make-up of Australia-based investors is vastly different to the composition of investors in Europe and North America. Superannuation schemes dominate the institutional investor base in Australia, accounting for over half (56%), while globally, the largest proportion (15%) of private equity investors are foundations. Furthermore, superannuation schemes' closest relative in the rest of the world, public pension funds, account for 14% of the global private equity investor population.

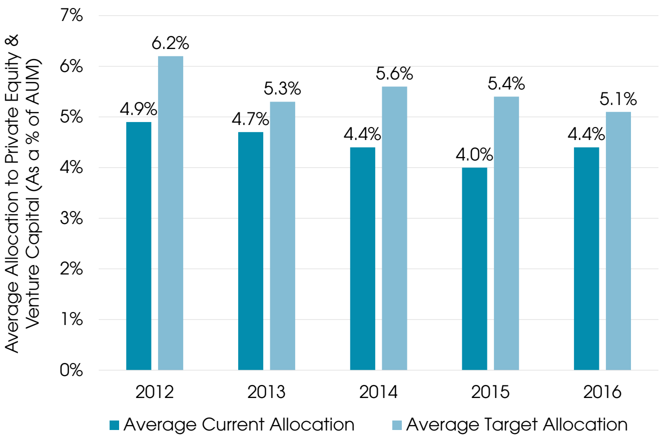
In terms of geographic preferences, 89% of Australia-based LPs look to invest domestically, with 62% looking to pursue investment opportunities globally. Strategically, 71% of investors have appetite for buyout funds, above the 62% and 53% that maintain a preference for venture capital and private equity funds of funds respectively.

Fig. 2.11: Number of Active Australia-Based Private Equity & Venture Capital Investors over Time, 2012 - 2016



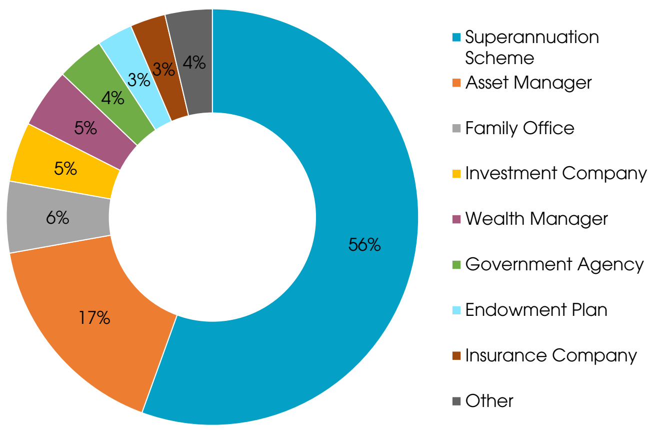
Source: Preqin Private Equity Online

Fig. 2.12: Australia-Based Investors' Current and Target Allocations to Private Equity & Venture Capital over Time, 2012 - 2016



Source: Preqin Private Equity Online

Fig. 2.13: Australia-Based Private Equity & Venture Capital Investors by Type



Source: Preqin Private Equity Online

Fig. 2.14: Top Five Australia-Based Private Equity & Venture Capital Investors by Current Allocation

Investor	Location	Type	Current Allocation to Private Equity & Venture Capital (A$bn)
Future Fund	Melbourne, Victoria	Sovereign Wealth Fund	9.5
MLC	Sydney, New South Wales	Asset Manager	3.9
QIC	Brisbane, Queensland	Asset Manager	3.9
QSuper	Brisbane, Queensland	Superannuation Scheme	3.5
AustralianSuper	Melbourne, Victoria	Superannuation Scheme	2.4

Source: Preqin Private Equity Online

Tribeca Global Natural Resources Fund: Preqin Top Performing Long/Short Equity Fund Globally

- Ben Cleary, Co-Portfolio Manager and Craig Evans, Co-Portfolio Manager, Tribeca Investment Partners

Can you tell us about Tribeca Global Natural Resources Fund?

The Tribeca Global Natural Resources Fund is a long/short global natural resources fund focused on large liquid opportunities across asset classes including equities, credit and commodities. We define the investible universe as hard rock commodities, energy, soft commodities and the infrastructure and service companies that wrap around these commodity groups. If we had a slogan it would be “low net, low gross, concentrated and active”.

The natural resources sector is inherently volatile and we believe therein lies a persistent opportunity to deliver positive absolute returns regardless of macro conditions using a low net, low gross, concentrated and active strategy. We talk about -20% to +60% on a beta-adjusted basis as our net investment range. We also believe you can generate returns without the use of leverage and have an absolute limit of 2x gross. We firmly believe the best hedge is cash and have no problems holding large amounts of it in times of uncertainty.

The fund is concentrated and we talk about 20-60 positions as being the usual range of portfolio positons. Having said that, the top five or six positions or themes will usually take up 50% of the gross of the portfolio, these could be longs or shorts. On average, 50% of the portfolio will be invested in the Americas with 25% in Europe and 25% in Asia-Pacific.

Central to our investment thesis is that the inherent volatility in the natural resources sector means that you will not be sufficiently rewarded for buy and hold strategies. You need to be active. Look at the oil price in the first quarter this year, it was the same price on 1 January as it was 31 March; however, there was a 65% trading range in between. We generally target catalysts for change at the stock or commodity level in the next three to nine months and this represents our average investment time horizon.

How did the fund come into existence?

We spent the majority of our careers at Macquarie Bank in Asia, London, New York and Sydney. With a combination of analytical and portfolio management backgrounds focused on the natural resources sector, we had long-term plans to launch a specialist long/short strategy.

The absence of low net, low gross, concentrated and active specialist resources strategies on offer to Asian investors formed the basis of our decision to leave the investment banks behind and start the strategy. At the time of founding the strategy in 2014, plenty of people called us crazy with commodities in a structural downtrend at the time, but the moves in the natural resources sector in 2016 have showcased the cyclical nature of the sector and why it pays to be long/short.

We are both material investors in the fund and have committed to reinvesting any performance fees earned by the fund, and paid to us, back into the fund for the foreseeable future.

The fund is currently the top performing equities hedge fund globally, as well as the top performing hedge fund of all strategies in Australia at 107% 2016 YTD. Can you tell us a bit more about what has been driving the returns in 2016?

The majority of our returns in 2016 have come from the precious metals, energy, soft commodities and specialty sectors, with the largest geographic contributors being North America and Australia.

Some of our best months so far in 2016 have actually been during general drawdown months like January and June when we were up 17% and 18% respectively. Our returns have zero correlation to other major asset indices like the S&P 500, but also the MSCI Commodity Producers Index. We continue to highlight to our investors that our returns have also been delivered using no leverage, on average, and low net exposures.

Looking forward, what is your outlook for the strategy over the rest of 2016 and beyond?

There are several interesting market structure issues that we see present in the natural resources sector at the moment. The sector has always been a boom bust sector, which of course leads to poor asset allocation over time. Generally speaking, most major commodity producers remain heavily indebted having overinvested at the top of the market, and are now unable to take advantage of what appears to be a bottoming of the sector. It is similar in the fund management space where most long-only managers have spent the past three years selling out of the sector and are now frantically trying to buy back in. This has led to lower liquidity, high volatility and wider spreads in the sector. For a long/short manager, this is an ideal backdrop to take advantage of capital raisings, mispriced assets and cheap volatility.

How do you manage risk in such a volatile sector?

We report our attribution monthly to our investors based on eight subgroups that include precious metals, base metals, bulks, energy, soft commodities, large and diversified businesses, duel listed companies, speciality metals and soft commodities. In terms of portfolio construction, we have net long or net short exposures across these eight subgroups at any one time with different gross exposures, giving a portfolio level net and gross.

We view our best hedge as cash and will take down overall portfolio gross in times of uncertainty. Take Brexit for example, we normally have 25% of gross exposure invested in Europe. During late May and early June, we took off all exposure in Europe and took down portfolio net. In the lead up to binary market events where we have no information edge, like Brexit, we will generally build cash and lower net. Subsequently, we were left in a good position to put money to work and buy natural resources stocks that had been sold off that clearly would not be impacted by goings on in the UK.

Tribeca was formed in 1998; how have you seen the hedge fund sector in Australia evolve since this time?

Tribeca started in 1998 as a small caps manager. Over time, the firm has become known for investing in areas beyond the mainstream and seeking to add value to client's portfolios on the fringe rather than the core. This approach to investing saw the business develop an active management style and hedge fund culture. The development of the business has somewhat echoed the development of the industry.

It has taken some time for Australian investors to truly embrace hedge funds; however, it seems that there is a change in the wind. There has been great development by groups such as AIMA and the country's leading institutional investors that have worked tirelessly to educate the industry about the inherent risks that investors have in their portfolios; and that they need to protect themselves from the dire situation when both equities and bonds are down, which we have all seen. Investors need something in their portfolio that provides them with absolute returns after fees, something uncorrelated and something that protects them when they truly need it. People are starting to understand this now and that there are some very good managers out there that can provide these things. In that perspective the industry has come a long way. That said, alternatives are still less than 5-10% of many institutional portfolios, which is worrying. There is still a long way to go, but the more participants there are in the market the better it is for everyone.

Have you seen any changes in the investor base in Australia over this time?

Due to the inherent complexity in hedge fund strategies, the investor base in Australia has been skewed towards sophisticated institutional investors, which is still the case. It is still the most innovative and forward-thinking institutions that use hedge funds in a meaningful way though.

Family offices and ultra-high-net-worth investors are another group that have really embraced investing in hedge funds over this period.

Why should global investors consider hedge fund managers based in Australia?

Australia has a unique position being a cultural and geographical blend of North America, Great Britain and Asia. The cultural element enables hedge fund managers based out of Australia, to understand the psyche of the North American and British investors. The geographical location of Australia, however, means that we operate in the same time zone as Asia and are away from much of the noise created in the market. This enables fund managers located here to have a unique perspective, which has proven to be a successful advantage.

Specifically relating to global natural resources, funds managed out of Australia have a distinct advantage due to our natural resources. It is also important to note that the flow of information is instantaneous these days, and with a committed team with global access to opportunities, the location of the office is far less significant than it used to be.

When investing in hedge funds based out of Australia, are there any particular nuances investors offshore should be aware of?

There are tax and distribution differences within Australian domiciled funds which work well for Australia resident investors. Offshore investors should look for managers with vehicles that accommodate their needs. As an example, the Tribeca Global Natural Resources Fund has both an Australia onshore and Cayman investment vehicle for the same strategy.

Is there anything else you would like to add?

It is volatility that creates opportunity, and when that volatility strikes, you want to be able to go long and short to capture it. That is what we do.

Tribeca Investment Partners

Established in 1998, Tribeca Investment Partners is an Australia-based, boutique fund manager with A$2.4bn AUM and a reputation for delivering on performance targets. Its clients are those who actively seek investment solutions beyond the mainstream. Distinct in the market, Tribeca blends traditional fundamental qualitative research with quantitative analysis. It combines quality investment decisions with the insight of successful experience the create meaningful outcomes for our clients.

Tribeca
Investment Partners

Ben Cleary – Co-Portfolio Manager, B.Econ, Grad Dip. Banking & Finance
Ben joined Tribeca in 2015 as Portfolio Manager for the Tribeca Global Natural Resources Fund, an active long short strategy investing in listed resources companies globally. He has over 15 years' experience in natural resources and served at a number of director level positions for Macquarie and RBS in Asia, the UK and Australia.

Craig Evans – Co-Portfolio Manager, B. Bus (Finance & Accounting)
Craig Evans joined Tribeca in 2016 as co-Portfolio Manager for the Tribeca Global Natural Resources Fund. He has over 20 years of financial markets experience. For the last 15 years Craig has been focussed on running long short investing, trading and financing businesses across the US, Europe, Asia and Australia for Macquarie Bank and Bank of America Merrill Lynch.

www.tribecaip.com.au

For more information about Tribeca Investment Partners, please contact:

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Disclaimer:
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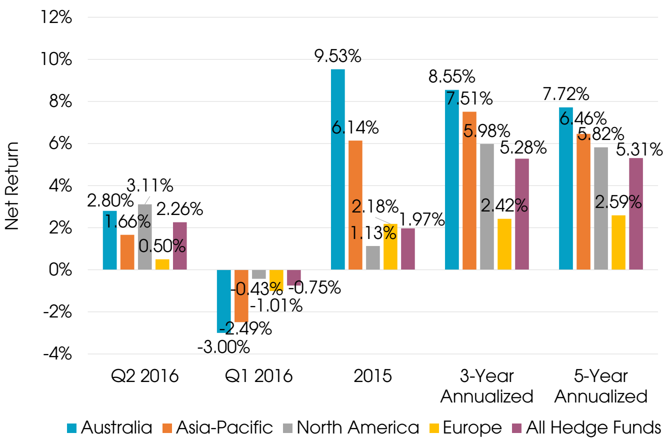
Performance

Hedge funds managed by Australia-based firms have significantly outperformed the Preqin All-Strategies Hedge Fund benchmark in 2015 and on a three- and five-year basis (Fig. 3.1). Over these timeframes, funds raised by Australia-headquartered hedge fund managers also outperformed vehicles managed by firms based in Asia-Pacific, North America and Europe.

After a successful 2015 in which Australia-based funds added gains of more than 9.50%, outstripping the S&P 500 Index by more than 10 percentage points, the choppy markets at the start of 2016 proved challenging for Australia-based hedge fund managers: hedge funds in the country lost 3.00% and trailed the S&P 500 by nearly four percentage points over Q1 2016 (Fig. 3.2). However, funds managed by Australia-headquartered managers saw a return to form in Q2 2016, adding 2.80% over the quarter, taking their YTD return to 3.30%.

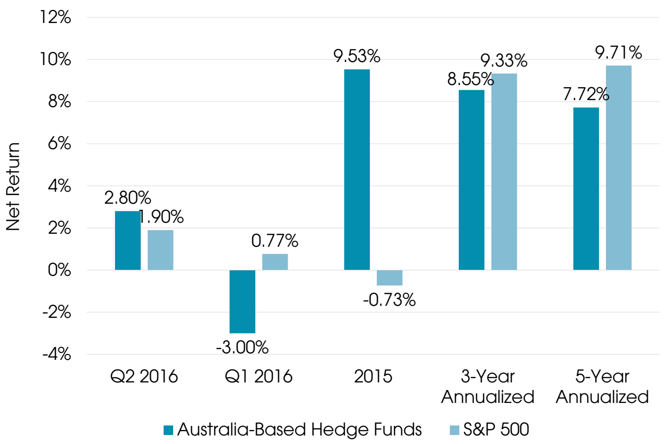
The top performing hedge fund based in Australia in 2016 so far, Tribeca Global Natural Resources Fund (see page 17 for our interview with Tribeca Investment Partners to find out what is driving the performance of this fund), pursues an equity strategy. Half of the top 10 performing funds in Australia also pursue an equity strategy, and all have outperformed the S&P 500 Index over this period.

Fig. 3.1: Performance of Hedge Funds by Fund Manager Location*



Source: Preqin Hedge Fund Online

Fig. 3.2: Performance of Australia-Based Hedge Funds vs. S&P 500 Index*



Source: Preqin Hedge Fund Online

Fig. 3.3: Net Returns of Top Performing Australia-Based Hedge Funds in 2016 YTD*

Fund	Manager	Core Strategy	2016 YTD Net Return (%)
Tribeca Global Natural Resources Fund - Class A	Tribeca Investment Partners	Equity Strategies	107.32
KIS Asia Long Short Fund	KIS Capital Partners	Equity Strategies	10.96
Wattle Fund	Anacacia Capital	Equity Strategies	10.82
Cor Capital Fund	Cor Capital	Multi-Strategy	10.29
KIS Asia Long Short Cayman Fund (USD Feeder)	KIS Capital Partners	Equity Strategies	9.18
Quay Global Real Estate Fund	Bennelong Funds Management	Niche Strategies	8.77
Hunter Burton Capital Alpha Fund	Hunter Burton Capital	Macro Strategies	8.66
Avenir Capital Value Fund	Avenir Capital	Equity Strategies	8.09
Attunga Power & Enviro Fund	Attunga Capital	Niche Strategies	6.37
Tribeca Global Total Return Fund	Tribeca Investment Partners	Macro Strategies	4.91
LHC Capital Australia High Conviction Fund	LHC Capital	Equity Strategies	4.52

Source: Preqin Hedge Fund Online

**Please note, all performance information includes preliminary data for July 2016 based upon returns reported to Preqin in early August 2016. Although stated trends and comparisons are not expected to alter significantly, final benchmark values are subject to change.*

Hedge Fund Managers

Australia is one of the leading centres for hedge funds within the wider Asia-Pacific region by assets under management (AUM); in total, funds within the region represent A$34bn in AUM. Within Australia, Sydney is the centre of the hedge fund industry, and is home to all of the five largest fund managers based in the country (Fig. 3.6); 68 of the 107 fund managers based in Australia are headquartered in Sydney and the wider New South Wales region (Fig. 3.5).

The largest hedge fund manager in Australia, Platinum Asset Manager, which runs nearly A$25bn in hedge fund assets, was formed in 1994 and is one of the longest standing firms in the region. As shown in Fig. 3.4, the number of fund managers launched in a single year reached a peak in 2009, but dropped in 2010 following the aftermath of the Global Financial Crisis (GFC). Subsequently, it reached a second peak in 2012 as the industry recovered. However, since 2012, only a small number of new firms have been established within Australia as the existing groups within the region mature. In contrast to the numbers of new firms being formed in Australia from 2006 to 2016, there have been relatively similar numbers of funds launched each year – typically between 20 and 25.

Data Source:

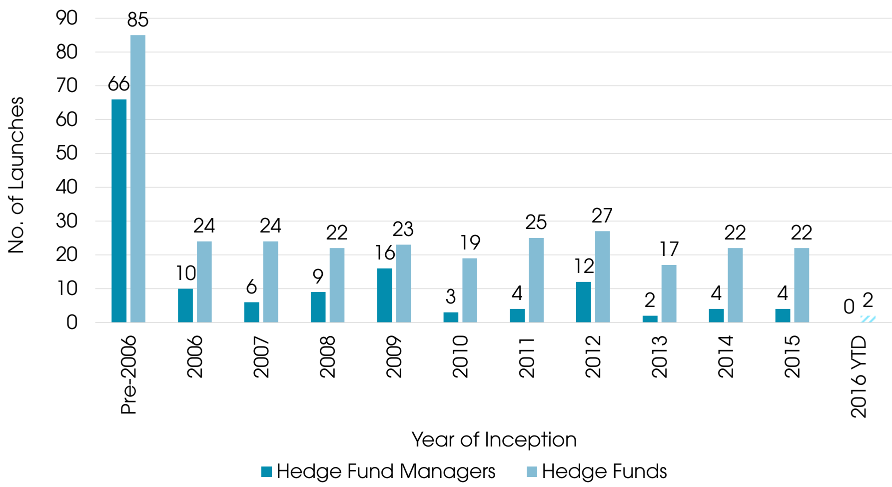
Preqin's **Hedge Fund Online** service contains detailed information on over 380 hedge funds in Australia.

Comprehensive profiles include assets under management, monthly returns, strategy and geographic preferences and much more.

For more information, please visit:

www.preqin.com/hfo

Fig. 3.4: Number of Australia-Based Hedge Fund Managers Incepted and Hedge Fund Launches by Year of Inception (As at August 2016)



Source: Preqin Hedge Fund Online

Fig. 3.5: Australia-Based Hedge Fund Managers by Location

Source: Preqin Hedge Fund Online

Fig. 3.6: Top Five Australia-Based Hedge Fund Managers by Assets under Management

Manager	Year Established	Location	Assets under Management
Platinum Asset Management	1994	Sydney, New South Wales	A$24.7bn as at 31 March 2016
Ellerston Capital	2004	Sydney, New South Wales	A$4.7bn as at 31 July 2016
Macquarie Investment Management	2003	Sydney, New South Wales	A$3.9bn as at 30 September 2015
Caledonia Investments	1992	Sydney, New South Wales	A$2.7bn as at 30 June 2016
Tribeca Investment Partners	1998	Sydney, New South Wales	A$2.4bn as at 31 July 2016

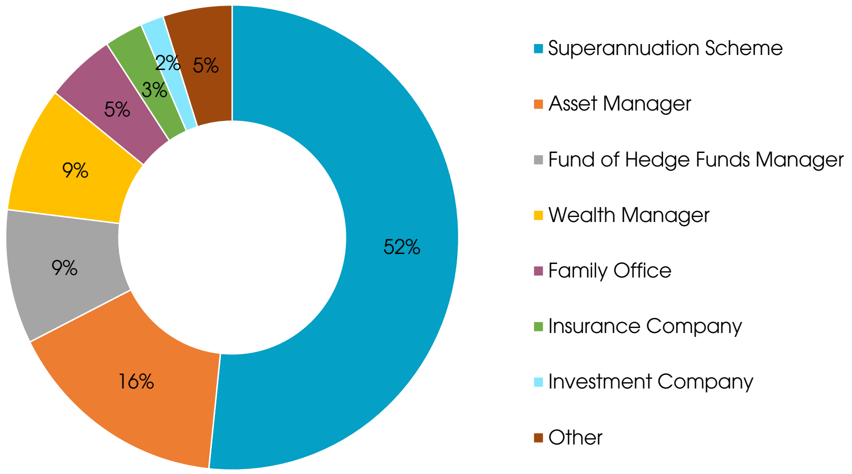
Source: Preqin Hedge Fund Online

Investors

Superannuation schemes are the leading hedge fund investor type within Australia, representing more than half (52%) of the institutional investors tracked by Preqin in the country (Fig. 3.7). Although superannuation schemes can allocate significant amounts of capital to hedge funds, such as SunSuper which has A$2.6bn invested in the asset class, the largest Australia-based investor in hedge funds is the sovereign wealth fund Future Fund. Future Fund, established in 2006, has more than A$118bn in assets under management (AUM) and dedicates a significant proportion of this to alternative assets, investing nearly $15bn in hedge funds.

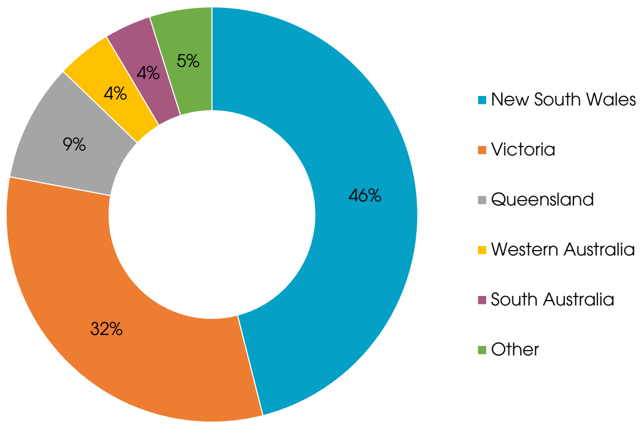
Future Fund is based in Melbourne – 32% of the active Australia-based hedge fund investors tracked by Preqin are located in the wider Victoria state; however, the largest proportion (46%) are based in New South Wales. These include MLC, the A$80bn asset management arm of National Australia Bank, which is based in Sydney. MLC invests 3% of its total AUM (approximately A$2.4bn) in hedge funds.

Fig. 3.7: Australia-Based Hedge Fund Investors by Type



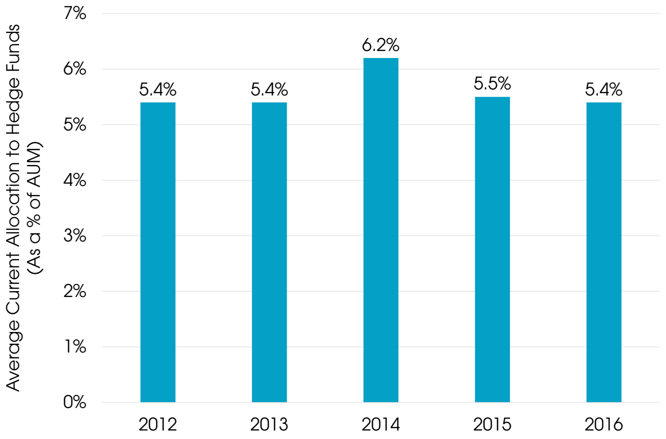
Source: Preqin Hedge Fund Online

Fig. 3.8: Australia-Based Hedge Fund Investors by Location



Source: Preqin Hedge Fund Online

Fig. 3.9: Australia-Based Investors' Average Current Allocation to Hedge Funds over Time, 2012 - 2016



Source: Preqin Hedge Fund Online

Fig. 3.10: Top Five Australia-Based Hedge Fund Investors by Current Allocation

Investor	Location	Type	Current Allocation to Hedge Funds (A$bn)
Future Fund	Melbourne, Victoria	Sovereign Wealth Fund	15.0
SunSuper	Sydney, New South Wales	Superannuation Scheme	2.6
Victorian Funds Management Corporation	Melbourne, Victoria	Asset Manager	2.6
MLC	Sydney, New South Wales	Asset Manager	2.4
QIC	Brisbane, Queensland	Asset Manager	0.9

Source: Preqin Hedge Fund Online

Australian Real Estate: A Beacon of Stable Growth and Returns

- Andrew Mihno, Executive Director, Property Council of Australia

What is driving demand for Australian real estate?

Internationally, investors and fund managers have been driving demand for property and listed/unlisted REITs in search of better yields and a shelter from anaemic global fundamentals.

The Australian economy has outpaced the OECD average and helped propel the property market to achieve stunning returns in comparison to other developed markets.

The uncertainty surrounding Brexit, the US elections and deteriorating bond yields are now pushing more investors towards Australia's real estate market with its consistently stable and high risk-adjusted returns.

The Australian property industry is the largest sector in the economy, representing 11.5% of economic activity and employing more workers than mining and manufacturing sectors combined.

Sixty percent of ordinary Australians have a financial stake in the industry both directly and through institutional funds, ensuring the population and government is highly engaged in the prosperity of the industry.

Critically, patient, long-term global capital has played a vital part in the growth of the industry and is recognized by the government as a crucial element to finance major investments and infrastructure.

The government has deliberately targeted reforms that free up investment in commercial real estate to ensure Australia is a more powerful magnate for the world's capital.

The government also has about 100 infrastructure projects underway with another 80 in the pipeline.

With the economy, global markets and government all drawing investment capital to Australian shores, it is little wonder we are seeing ever-increasing demand from investors across the globe.

How has the Australian real estate market evolved over time, where do you feel it is headed for the future and what are the key drivers for this?

The Australian real estate market has evolved enormously over the last 20 years.

Australia has one of the most highly securitized and transparent markets in the world, with a listed and unlisted REIT sector dating back to 1971.

Twenty-five years of uninterrupted growth has helped drive the real estate market and returns for investors.

JP Morgan's figures reveal that over the last five years, Australian-listed REITS (A-REITS) were the best performing REIT market globally, generating a cumulative total return of 130% and outperforming the Global REIT Index by 60%.

UBS analysis also shows that Australian-listed REITs significantly outperformed major markets including the US, Europe and the UK.

A combination of domestic and global factors will bolster Australia's favourable market conditions into the future.

The strength of the domestic economy and population growth will drive ongoing demand for new and existing real estate.

The Australian economy has successfully transitioned in recent years from a reliance on mining and resources to growth in the service and property sectors. This is fuelling increasing demand for commercial property investment in Sydney and Melbourne.

This transition mirrors the rise of the Chinese and Asian middle classes and their increasing appetite for Australian healthcare, higher education, professional services and tourism.

The Australian economic picture is markedly better than the OECD average, with the economy recording growth of 3.1% in March 2016, the fastest rate since 2012, coupled with low and stable inflation. In addition, the unemployment rate continues to trend downwards (currently at 5.7%) despite high rates of workforce participation and solid population growth of 1.4% per annum.

Internationally, anaemic economic growth across the developed world, volatile emerging markets and yield compression across other asset classes will help drive global demand for Australian real estate.

The decision by the UK to leave the European Union is driving increased interest in Australian real estate. Brexit has amped up investor concerns on the economic future for the UK.

While the stock market is recovering ground (as equity analysts adjust to the new market trend), the Bank of England is tipping an economic slump for the UK and 250,000 job losses.

Increased investor risk aversion and a growing preference for assets with reliable and regular cash flows (such as sovereign bonds and property) is driving more investors towards other sophisticated markets including Australia.

The truth is, no one knows what will happen (yet), but the uncertainty is driving a sharp rise in investor inquiries for Australian real estate investment out of Europe.

Australia's future challenge is to keep pace with demand for new products to avoid further tightening of the market in an already competitive domestic environment.

Are there any regulatory or policy issues that have changed recently or are likely to change that will have a big impact?

A competitive and stable Australian economy is essential to attracting the global capital necessary to finance major investments including infrastructure projects.

The Australian Government has undertaken significant reforms to help Australia attract a greater share of global capital.

Australia has progressively liberalized its REIT rules to remove impractical investment restrictions and help Australia become a funds management hub. Importantly, it has:

1. Streamlined and simplified existing industry practice;
2. Extended withholding tax concessions to a greater range of foreign and domestic investors;
3. Ensured REITs can reliably access rules that are critical to the functioning of their organization; and
4. Simplified the allocation of distributions to ensure the financial health of REITs.

Overall, the focus reduces barriers to allow the REIT industry to remain nimble in an ever-changing market.

On the other hand, while the government wants to encourage global investment, recent changes to stamp duty and land tax for international investors in New South Wales, Queensland and Victoria have increased the cost to overseas residential purchasers.

The Property Council is working with the state governments to press them to instead look to real policies to improve housing affordability, including fixing their planning systems and removing stamp duty.

Critically, however, the Australian Federal Government has legislated changes to streamline and improve Australia's foreign investment rules for commercial investment. The new rules allow investment in commercial property up to A$252mn without Foreign Investment Review Board (FIRB) approval. This near five-fold increase in the threshold frees up investment for office, industrial and commercial accommodation. Importantly, the threshold for foreign investors from "agreement countries" (NZ, Japan, Korea, Chile or the USA) has been raised to A$1.094bn.

The overall message from the government is that Australia is keen to embrace global capital and is making the real estate market a stronger magnet for international funds.

How segmented is the market for real estate by territory? Are certain states experiencing boom periods and are others in decline?

A mixture of local and national factors influences real estate asset classes and geographic markets differently. In the office market space, the two largest office markets, Sydney (5,100,000m^2) and Melbourne (4,400,000m^2) are in high demand for developers and investors.

These are relatively large, mature, diversified office markets, with Sydney recognized as the gateway and home to a number of global corporates including investment banks, and Melbourne as the headquarters of some of Australia's largest corporates. These markets are driven primarily by sectors such as finance, professional services, healthcare and education. These sectors account for two-thirds of the Australian economy but only 20% of Australian exports. There is considerable room to grow these markets.

The retail sector reflects both regional and state economic factors, but the most important driver for retail is the specific trade area demographics. Australia has one of the highest population growth rates within the OECD (1.4% in 2015) and this is a major driver of the retail sector. The limited amount of retail floor space in Australia (about half the rate per capita of the USA) and strong population growth see Australian regional shopping centres offering some of the strongest risk-adjusted returns in the world.

The next 12 months will be an interesting time in the market and Australia is well placed for investors looking for stable returns.

Property Council of Australia

The Property Council champions the interests of more than 2,200 member companies that represent the full spectrum of the industry, including those who invest, own, manage and develop in all sectors of property, creating landmark projects and environments where people live, work, shop and play.

Led by a powerful board and strong executive leadership team, the Property Council's vision is a thriving industry creating prosperity, jobs and strong communities.

The Property Council's International and Capital Markets Division (ICMD) influences governments globally to free up property investment flows and capital markets, connects industry and market leaders and drives international initiatives to partner investors.

For further information on the Australian markets and inbound/outbound investment, please contact:

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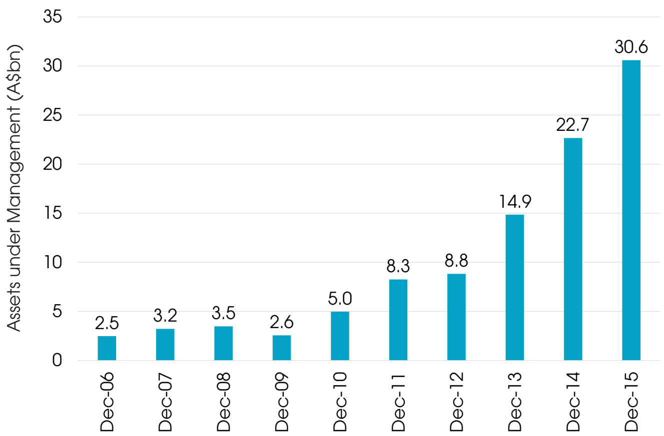
Assets under Management, Dry Powder and Performance

The Australian private real estate industry has seen rapid growth since the financial crisis, with the AUM of Australia-based closed-end private real estate firms rising 1,077% over the past six years to a record A$30.6bn as of December 2015 (Fig. 4.1). The vast majority (79%) of AUM is held as unrealized value of portfolio assets, with just A$6.5bn in uncalled capital commitments.

The majority (55%) of real estate AUM is held in lower risk core and core-plus vehicles, more than the combined AUM held in higher risk and higher returning value added (11%) and opportunistic (30%) funds (Fig. 4.2).

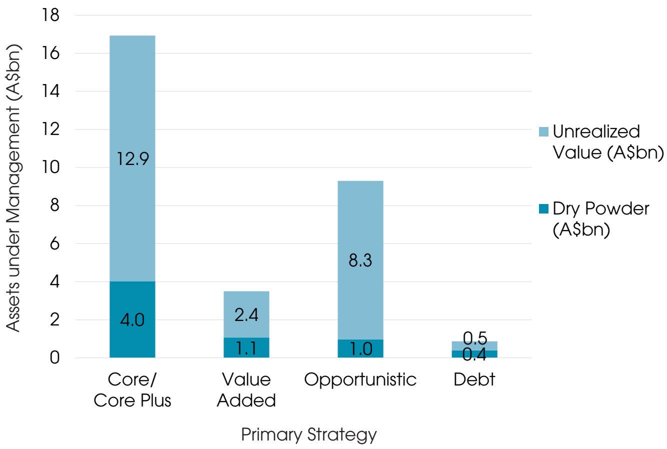
The top performing private real estate funds by net multiple are listed in Fig. 4.3. Sydney-based Altis Property Partners currently holds the top two spots for Altis Real Estate Equity Partnership Vintage 1 and its follow-on Vintage 2; both funds follow an opportunistic strategy targeting a variety of property types across Australia, and have posted net multiples of 1.75x and 1.66x respectively.

Fig. 4.1: Australia-Based Closed-End Private Real Estate Assets under Management, 2006 - 2015



Source: Preqin Real Estate Online

Fig. 4.2: Australia-Based Closed-End Private Real Estate Assets under Management by Primary Strategy (As at December 2015)



Source: Preqin Real Estate Online

Fig. 4.3: Top Performing Australia-Based Closed-End Private Real Estate Funds by Net Multiple

Fund	Firm	Vintage	Fund Size (mn)	Geographic Focus	Net Multiple (X)	Net IRR (%)	Date Reported
Altis Real Estate Equity Partnership Vintage 1	Altis Property Partners	2010	107 AUD	Australasia	1.75	18.0	Jun-16
Altis Real Estate Equity Partnership Vintage 2	Altis Property Partners	2013	250 AUD	Australasia	1.66	n/a	Dec-15
Fortius Active Property Trust No.1	Fortius Funds Management	2006	434 AUD	Australasia	1.65	5.8	Mar-16
Property Development Portfolio No.3	Charter Hall Group	2002	223 AUD	Australasia	1.57	19.2	Jun-16
Propertylink Australian Industrial Partnership	Propertylink	2013	265 AUD	Australasia	1.46	10.9	Mar-16
Property Development Portfolio No.1	Charter Hall Group	1997	386 AUD	Australasia	1.45	13.5	Jun-16
Lend Lease Real Estate Partners I	Lend Lease Investment Management	1999	70 AUD	Australasia	1.42	7.5	Jun-15
Property Development Portfolio No.2	Charter Hall Group	2000	384 AUD	Australasia	1.37	19.0	Jun-16
AMP Capital Select Property Portfolio III	AMP Capital Investors (Australia)	2007	190 AUD	Australasia	1.36	11.1	Mar-15
Gresham Property Fund No. 4	Gresham Property	2011	85 AUD	Australasia	1.26	12.7	Mar-16

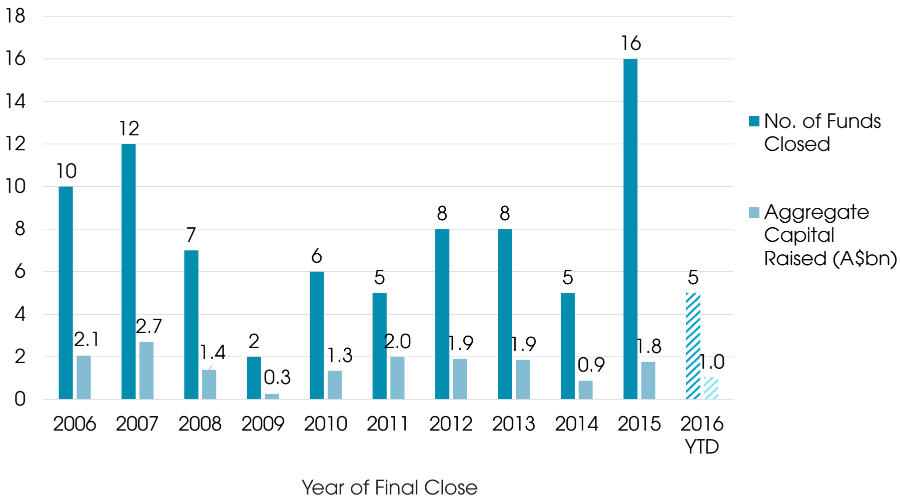
Source: Preqin Real Estate Online

Fundraising

Preqin's **Real Estate Online** contains detailed information on 84 Australia-based closed-end private real estate funds which have collectively raised A$17.2bn in institutional capital since 2006 (Fig. 4.4). Fundraising peaked in 2007 when 12 funds reached a final close securing A$2.7bn. Following three years of subdued fundraising post crisis, momentum picked up again, with five vehicles securing A$2.0bn in 2011. Among these was Goodman Australia Partnership, a A$1.7bn fund that targets core logistics and business park assets primarily on the eastern seaboard of Australia. The amount of capital raised annually has remained relatively consistent since 2011, although 2015 did see a record 16 Australia-based private real estate funds close.

Lower risk core and core-plus funds have represented the largest proportion (47%) of funds closed in the last 10 years, although they account for just 35% of aggregate capital raised. However, since 2013, fund managers appear to be seeking strategies higher up the risk/return spectrum: 51% of the capital raised since 2013 was secured by higher risk funds (Fig. 4.5), with 84% of capital raised so far this year secured by Australia-based value added and opportunistic funds.

Fig. 4.4: Annual Australia-Based Closed-End Private Real Estate Fundraising, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Real Estate Online

Driving the growth of the fundraising market is the rising number of Australia-based firms bringing vehicles to market. There are currently 10 funds in market collectively targeting A$2.5bn, a record amount sought by firms in the country (Fig. 4.6). Half of these vehicles are targeting value added (3) and opportunistic (2) investments, with only three core and core-plus vehicles in market and two debt funds.

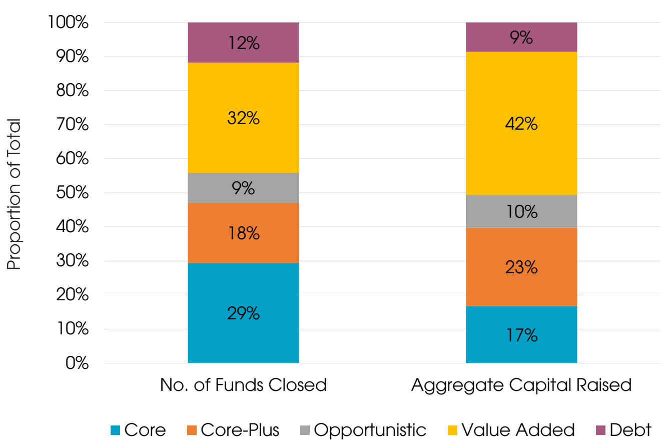
Data Source:

Preqin's **Real Estate Online** contains detailed information on all 84 Australia-based real estate funds closed since 2006. Profiles include close sizes, investment preferences, known investors and more.

For more information, please visit:

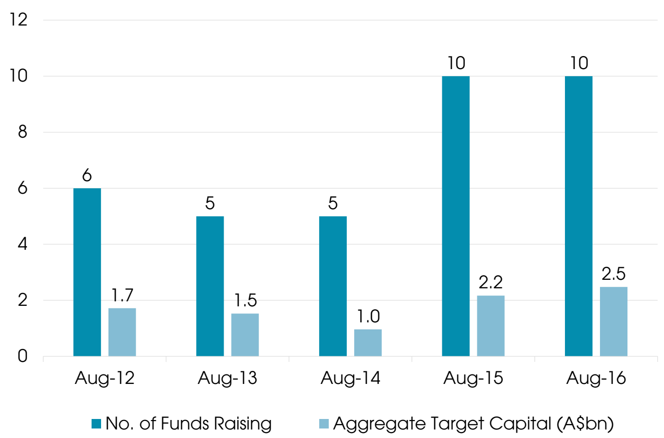
www.preqin.com/reo

Fig. 4.5: Australia-Based Closed-End Private Real Estate Fundraising by Primary Strategy, 2013 - 2016 YTD (As at August 2016)



Source: Preqin Real Estate Online

Fig. 4.6: Australia-Based Closed-End Private Real Estate Funds in Market over Time, August 2012 - August 2016



Source: Preqin Real Estate Online

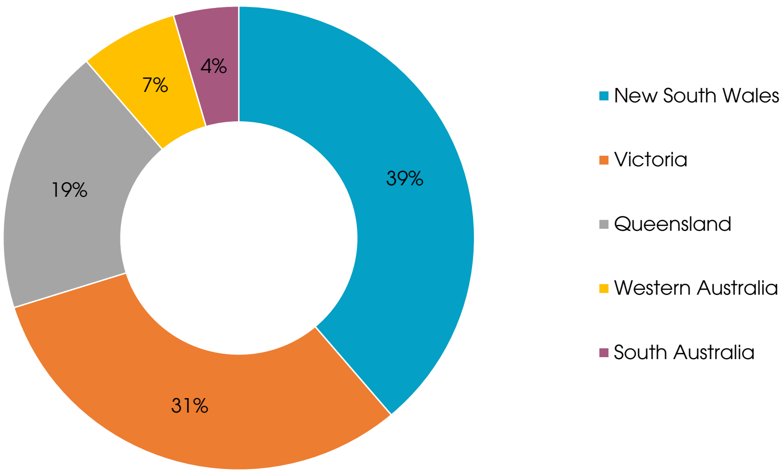
Deals

Unsurprisingly, of the property deals completed involving private equity real estate firms since 2006, the largest proportions were completed in New South Wales (39%) or Victoria (31%, Fig. 4.7), and mainly in the hub cities of Sydney, Melbourne and Brisbane.

Office and retail assets together account for three-quarters of Australian private equity real estate deals, with office assets representing 39% and retail assets 36% (Fig. 4.8). However, retail assets complete for much smaller sizes, with 69% of aggregate deal value accounted for by office assets, while retail assets make up just 11% of the overall value, below that of mixed-use property (14%).

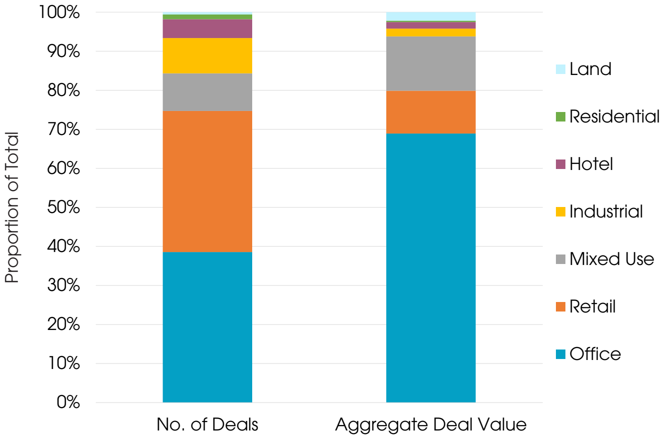
Most private equity real estate deals involve mid-sized assets, with 64% of transactions involving property of 100,000-499,999ft² in size and only 8% of deals since 2006 involving larger assets (more than 500,000ft²).

Fig. 4.7: Australian Private Equity Real Estate Deals by Asset Location, 2006 - 2016 YTD (As at August 2016)



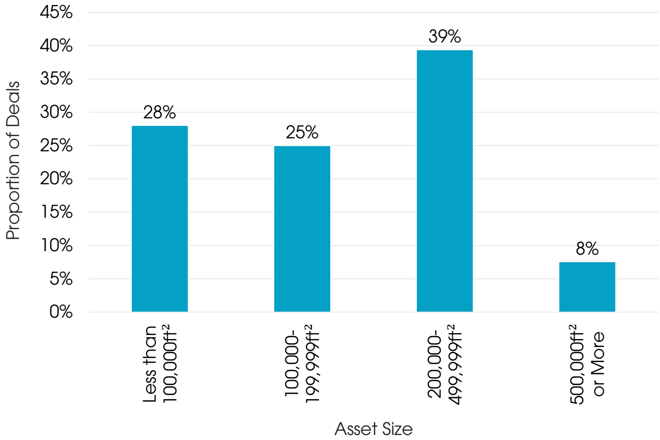
Source: Preqin Real Estate Online

Fig. 4.8: Australian Private Equity Real Estate Deals by Primary Asset Type, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Real Estate Online

Fig. 4.9: Australian Private Equity Real Estate Deals by Asset Size, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Real Estate Online

Fig. 4.10: Notable Australian Private Equity Real Estate Deals Completed in 2016 YTD (As at August 2016)

Asset	Primary Asset Type	Buyer(s)	Seller(s)	Deal Size (mn)	Location	Deal Date
Adelaide's Rundle Place	Retail	Blackstone Group	Unidentified Seller/s	400 USD	Adelaide	Jan-16
One Shelley Street	Office	Charter Hall Group, Morgan Stanley Real Estate Investing	Unidentified Seller/s	525 AUD	Sydney	May-16
420 George Street	Office	Investa Property Group	Fortius Funds Management	442 AUD	Sydney	Apr-16
MidCity Centre	Retail	Unidentified Buyer/s	Fortius Funds Management	310 AUD	Sydney	May-16
Southgate Complex	Mixed Use	ARA Asset Management, Korea Investment Corporation, Unidentified Buyer/s	Dexus Property Group	289 AUD	Melbourne	Aug-16

Source: Preqin Real Estate Online

See how investors measure up...

Investor Analyst:
The True Perspective

Investors

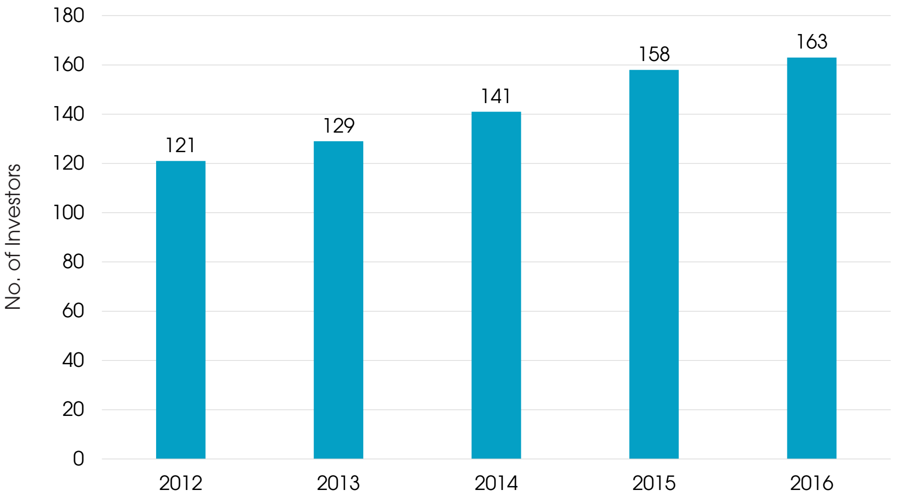
Preqin's **Real Estate Online** features detailed profiles for 163 institutional investors based in Australia that are active in real estate, with this number rising annually from the 121 investors active in the asset class in 2012 (Fig. 4.11). While the numbers have increased, new entrants, often with lower allocations (as a proportion of total assets), have led to a gradual reduction in both the average current and target allocations of Australia-based investors (Fig. 4.12). However, the target allocation of Australia-based investors is in line with the global average, while the current allocation is 70 basis points above the global mean.

Private funds and listed investments are the primary routes to access the real estate market for Australia-based institutions: approximately three-quarters of investors target both routes. A much greater proportion of Australia-based institutional investors target listed real estate than investors globally (32%), a reflection of the size of the listed real estate industry in Australia.

Core private funds are a preference for the vast majority (91%) of Australia-based investors, with reliable income streams providing a good match to those investors with long-term liabilities that make up a sizeable proportion of the Australian investor pool.

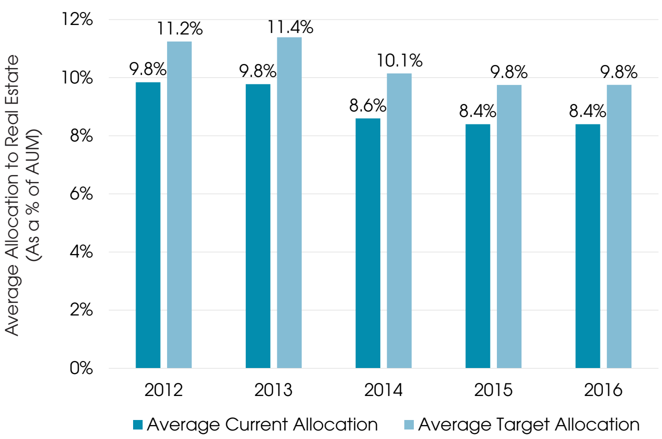
Superannuation schemes make up the majority (55%) of Australia-based real estate investors, far above the proportion of asset managers (17%, Fig. 4.13). Nevertheless, QIC, an asset manager based in Queensland, is the largest Australia-based institutional investor with A$13.8bn invested in direct assets and unlisted funds (Fig. 4.14).

Fig. 4.11: Number of Active Australia-Based Real Estate Investors over Time, 2012 - 2016



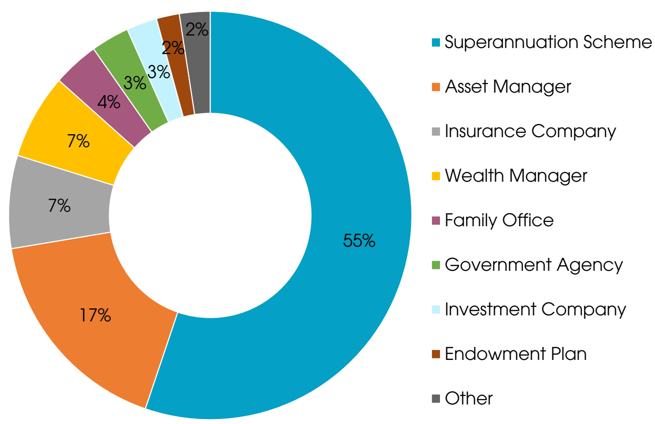
Source: Preqin Real Estate Online

Fig. 4.12: Australia-Based Investors' Current and Target Allocations to Real Estate over Time, 2012 - 2016



Source: Preqin Real Estate Online

Fig. 4.13: Australia-Based Real Estate Investors by Type



Source: Preqin Real Estate Online

Fig. 4.14: Top Five Australia-Based Real Estate Investors by Current Allocation

Investor	Location	Type	Current Allocation to Real Estate (A$bn)
QIC	Asset Manager	Brisbane, Queensland	13.8
AustralianSuper	Superannuation Scheme	Melbourne, Victoria	8.7
Future Fund	Sovereign Wealth Fund	Melbourne, Victoria	7.5
UniSuper	Superannuation Scheme	Melbourne, Victoria	6.7
QSuper	Superannuation Scheme	Brisbane, Queensland	4.9

Source: Preqin Real Estate Online

Australian Infrastructure Stands out in the 'Lower for Longer' Regime

- Michael Cummings, Head of Australia and NZ Funds, Infrastructure Equity, AMP Capital

Investors globally are facing a 'lower for longer' environment for investment returns. This weak return environment is largely due to the lack of sustainable economic growth in OECD economies. Policy makers in general have struggled to reignite economic growth in the period since the Global Financial Crisis (GFC) – a task that has proved harder than anyone anticipated.

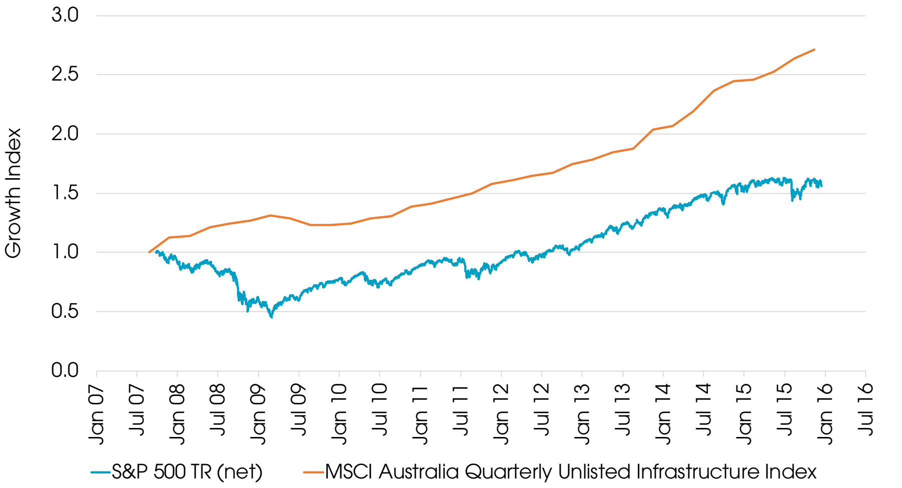
Despite aggressive quantitative easing and the consequential reduction in US interest rates to record lows, data from the US Bureau of Labour Statistics suggests that the required return on investment for capital assets is now at its highest level in 75 years. In short, despite developed economies being awash with liquidity, very little of it appears to be invested into generating economic growth. In the absence of a marked shift in policy making, we anticipate that this situation is likely to persist for the foreseeable future. Consequently, savvy investors are increasingly turning to alternative investments, particularly real assets such as unlisted real estate and infrastructure, to meet their investment needs.

In the context of the current return regime of 'lower for longer', this paper explores the opportunities and threats that Australian unlisted infrastructure presents for investors.

Unlisted Infrastructure Has Outperformed Equities over the Long Term

Unlisted infrastructure has become increasingly popular with investors looking to improve the resilience and diversification of their portfolio via exposure to an alternative asset class. Since the GFC, returns for unlisted infrastructure assets have consistently outperformed listed markets, serving to provide equity-like total returns but with lower volatility – this can be seen in Fig. 1.

Fig. 1: Comparison of Total Returns: S&P 500 Index vs. Australian Unlisted Infrastructure



Source: AMP Capital, Bloomberg, as at 31 December 2015

Some of the growth in unlisted infrastructure valuations is a consequence of ultra-low bond yields. However, an examination of current valuations suggests that they lag bond movements. That is, a continued 'lower for longer' return environment is likely to see further unlisted infrastructure valuation growth.

Australia Offers a Supportive Backdrop for Infrastructure Investment

Australia was a pioneer in the privatization of infrastructure assets and continues to generate a significant proportion of new OECD unlisted infrastructure opportunities. A number of factors have contributed to a positive environment for infrastructure investment in Australia, including supportive government policy, a strong pipeline of assets, innovation, a long track record of investment and close proximity to Asian growth markets.

Supportive Government Policy

Over the past 25-years, there has been significant private sector involvement in the delivery of infrastructure. While there will always be some level of doctrinaire opposition to private investment in the delivery of public services, the long-term experience of Australian governments has been positive. This trend has contributed to significant deleveraging of public debt relative to the economy and supported Australia's AAA+ credit rating. In turn, this has allowed for the provision of government services at a lower cost.

In July 2008, Infrastructure Australia was established as an independent statutory body to provide research and advice to the Australian government under the Infrastructure Australia Act 2008. The move to set up Infrastructure Australia and state and territory counterparts reflects the Australian government's commitment to prioritize and progress nationally significant infrastructure[1].

Strong Pipeline of Assets

Public Private Partnerships (PPPs) are now the default approach in delivering traditional infrastructure assets in Australia, and the role of PPPs is growing with expansion into new areas such as social housing. This has led to a strong pipeline of assets for infrastructure investment. Australia still leads the world in privatizing legacy government assets and services where significant efficiency gains are achievable. The maturity of the Australian market has resulted in a thriving secondary market for mature infrastructure assets.

The sophistication of Australia's infrastructure market – and the visibility of new projects and government divestments – will be enhanced by a bilateral infrastructure investment pipeline under development by the Australian

[1] *Australian Government, Infrastructure Australia, <http://infrastructureaustralia.gov.au/about/role.aspx>, accessed 23 August 2016*

and New Zealand Governments in partnership with independent think tank Infrastructure Partnerships Australia. The Australia & New Zealand Infrastructure Pipeline (ANZIP) was committed to by both governments in 2015 – and has been supported by AMP Capital during its development – offering better connectivity and showcasing the depth of forward activity in the Australian and New Zealand markets.

Innovation
The models for enhancing PPPs are still evolving, primarily around the sharing of demand risk. In high-risk projects, governments may retain demand risk or delay the sale of new assets until project demand has ramped up.

Long Track Record
Australia's long track record in infrastructure investing means that partnering arrangements and regulatory structures are mature; a strong understanding among the government and investors of the governance framework contributes to a robust environment for investing.

Proximity to Key Asian Growth Markets
In addition to a favourable local environment, relative to other OECD countries, investment in Australian infrastructure benefits from both a relatively strong local economy and Australia's close integration with high-growth Asian economies. Select Australian assets provide exposure to Asian growth without the risks associated with direct investment in emerging economies, making Australia a standout destination for total return investors.

Diversity across Australian Infrastructure Assets

In a low-return environment, high-performing and relatively low-risk investments are likely to attract a lot of interest. We have witnessed solid demand for large cap infrastructure 'trophy' assets, particularly from sizeable local and international institutional investors seeking to rapidly build exposure to direct infrastructure. This demand has driven prices higher for large cap assets. High-yielding assets have also been in demand. On the other hand, mid-cap and growth assets have not experienced the same intensity of demand and, as a result, offer better value. Investors are able to gain well-diversified exposure to mid-cap and growth assets through well-established infrastructure funds.

Assets in different social, energy & utility, and transport infrastructure sectors all offer diverse characteristics which need to be understood to ensure investor expectations are met.

Social Infrastructure
Social infrastructure includes a broad range of assets including schools, hospitals, car parks and convention centres. Increasingly, state governments are using PPPs for the delivery of a wide range of social infrastructure assets under concession arrangements. According to Infrastructure Australia, a growing body of evidence supports the view that PPPs are delivering better quantitative and qualitative outcomes than alternative procurement models. The advantages include improved value for money outcomes and better quality public services[2].

Growth Leverage Asset Case Study – Sydney University Village

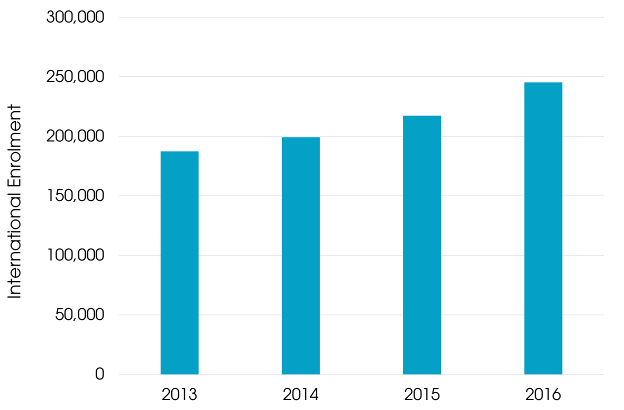
Sydney University Village is a 650-bed student accommodation facility located on campus at the University of Sydney. Construction of the facility was funded by AMP Capital in partnership with the University of Sydney and is operated under a long-term concession. The village caters to a growing demand for high-quality, affordable student accommodation and is a good example of an asset that is exposed to the high growth potential in the Asia-Pacific region.

Education consistently ranks as one of Australia's top goods and services exports behind iron ore and coal. International students are attracted to Australia for its highly ranked English-speaking universities and safe, attractive cities. Students from Asian countries dominate Australian international enrolments; demand is driven by the close proximity to Australia and increasing wealth and therefore mobility of those seeking a tertiary education.

According to the Department of Education and Training, international enrolment in Australian higher education has grown at a compounded rate of 7% per annum (see Fig. 2). Assuming there is no dramatic shift in the Australian dollar or visa policy conditions, this growth rate is expected to continue for the near to medium term.

International students require bespoke affordable accommodation; however, substantial land and construction costs in capital cities close to universities generally discourage these developments. Sydney is forecast to have a supply gap of approximately 30,000 beds across 50,000 international students, resulting in a strong demand for the current supply of beds[3].

Fig. 2: A Growing Number of International Students Enrol in Australian Higher Education



Source: Department of Education and Training, as at June 2016

Overall, the outlook for Australia's higher education sector is positive given that demand (primarily from Asian countries) remains strong and on the supply side, cost barriers and a shortage of available land will prevent a dramatic increase in affordable student accommodation. Quality facilities that offer a premium location, such as Sydney University Village, are best placed to perform over the long-term.

[2] *Bond University, Infrastructure Association of Queensland, A survey of alternative financing mechanisms for public private partnerships – research report, 31 July 2009*
[3] *JLL Australian Student Accommodation, Market Update 2015*

Social PPPs are typically availability-based; that is, the investor ensures that the assets are 'available for use' while the government counterparty takes the demand risk. Risk transfer to the private sector includes financing over the term of the concession, delivery risk, ongoing provision of operating services and maintenance.

For investors targeting yield, Australian social infrastructure PPPs are particularly attractive since yields are high relative to current bond rates. Given the high credit quality of the counterparties, many investors consider mature (post-delivery) social PPPs to be good bond proxies. This has led to a thriving secondary market in mature social infrastructure PPPs.

Other forms of social infrastructure, including student accommodation, attract higher levels of return relative to the availability model as they involve a greater degree of demand risk. Student accommodation in particular is also leveraged into high-growth Asian economies.

Ports and Airports

Port and airport assets represent growth assets which are geared towards the strong growth potential that is coming from Asian markets; international air passenger growth in the Asia-Pacific region has sustained double-digit compound average growth rates (CAGRs) for many years. However, a comparison with growth in developed countries still reveals a huge latent demand that will be unlocked in future years as per capita wealth grows. We believe that this suggests sustained, high future demand growth will prevail for attractive destinations.

Roads

Some legacy road assets were developed under PPPs with the concessionaire taking demand risk. Such roads broadly provide investors with direct exposure to Australian economic growth and, in some cases, significant growth opportunities. While the initial demand ramp-up in a number of these assets was problematic, they are now mature assets in which demand risk is well understood. Typically, new private sector toll roads are provided under the availability model, with governments taking demand risk. Currently, the government is developing an estimated A$16.8bn, 33km toll road network in Sydney through the WestConnex tollway project[4]. Funding via a PPP structure is a likely next step post-construction, and allows the state to 'recycle' the capital. Such assets provide investors with high-yielding opportunities.

Rail

Australian rail infrastructure underwent a period of reform whereby track and rolling stock ownership is now separate; most freight rolling stock is now owned by the private sector. Road congestion in major cities and improved rail services has seen strong growth in rail commuter volumes (for example, 8% CAGR in Sydney) as well as network expansions. Favourable policies coupled with the obsolescence of much of the legacy rolling stock, suggests that new passenger rolling stock could also be privatized along similar lines to the UK industry. Governments are also open to private sector proposals for greenfield track developments.

Electricity Utilities

Australia's electricity industry was reformed in the 1990s by eliminating vertically integrated state monopolies in favour of separate generation, transmission and distribution operators and retail suppliers. Consequently, in the eastern states, generation and retailing are now largely privately owned, while transmission and distribution assets have a mix of public and private ownership and operation. At a geographical level, assets in Queensland and Western Australia represent some of the largest potential future privatization prospects in Australia; New South Wales is in the midst of

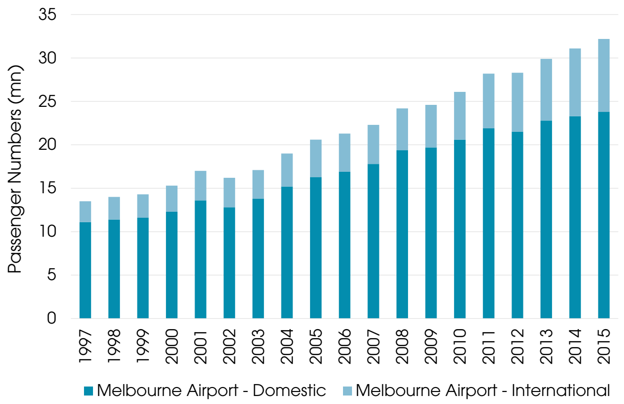
High-Growth Infrastructure Asset Case Study – Melbourne Airport

Melbourne Airport is a good example of an asset that is exposed to the high growth potential in the Asia-Pacific region. Situated in Australia's second largest city, Melbourne Airport was privatized by the Australian Government in 1997 and is now operated by the Australia Pacific Airports Corporation (APAC). APAC continues to work closely with Melbourne's civic leaders to establish Melbourne as a major tourist destination in its own right. These efforts have been rewarded with consistent growth in Melbourne's number of international passengers.

Since privatization, Melbourne Airport's total number of domestic passengers has grown at a compounded rate of 5% per annum. On average, Melbourne Airport's number of international passengers is growing at an annualized rate of 7% since 1997 or 9% since 2010. The strong demand reflects the fact that China travel volumes have increased 21.9% on the last financial year 2014/15[5].

To support growth, APAC has expanded the range of ancillary services available at the airport. This development extended to an air transport-related business park, hotel accommodation, car parking and additional retail offerings, such as duty-free shopping and food and beverage outlets. Consequently, air transport fees now amount to less than 50% of revenues and EBITDA growth has consistently outpaced passenger growth[6].

Fig. 3: Melbourne Airport's Number of Passengers is Growing



Source: Australia Pacific Airports Corporation, as at 31 December 2015

[4] *O'Sullivan, M., 2016, WestConnex: Extra tunnel, road widening makes $16.8b motorway even bigger, Sydney Morning Herald, published 19 July 2016*

[5] *Melbourne Airport, Victoria celebrates 9.5% growth in international travellers for FY16 – Media release, published 20 July 2016, <http://melbourneairport.com.au/about-melbourne-airport/media/media-releases/melbourne-airports-2015-16-passenger-traffic-results-2030.html>, accessed 23 August 2016*

[6] *Melbourne Airport, APAC2014/15 Financial report, <http://melbourneairport.com.au/docs/2015-2016-apac-annual-report.pdf>, accessed 23 August 2016*

leasing and contracting operations for the majority of its distribution assets.

Risks and Opportunities in Emerging Technologies

Australians are typically early adopters of new technology. The uptake of new technical developments is supported by strong consumer protection mechanisms and relatively open regulatory frameworks.

To illustrate this point, Australia's plentiful sunshine has seen household solar photovoltaic penetration reach 1.57 million installations (with a combined capacity of over 5.4 GW) in the 2016 financial year. This means the development of any new utility-scale baseload power plants is unlikely in the foreseeable future[7].

AMP Capital is of the opinion that the emergence of a range of mutually complementary disruptive technologies will seriously challenge some established infrastructure business models while providing investors with a wide range of alternative opportunities. Some disruptive technologies that are likely to impact on infrastructure development include:

- Cost-effective small-scale distributed photovoltaic electricity generation;
- Cost-effective small-scale energy storage devices;
- Electric and autonomous vehicles; and
- Peer energy trading platforms.

Most at risk is the established 100-year-old electricity utility model. On current costings it is now viable for larger domestic users to substitute high-cost and high embodied carbon peak and shoulder electricity with stored local green PV-generated energy. While still reliant on existing networks for the supply of off-peak energy, by flattening peak loads, this small-scale distributed generation has the potential to significantly increase the capacity of existing networks, greatly reducing the need for future network investment.

Electric cars will also have a major impact on road infrastructure, requiring large-scale charging facilities. Longer term, autonomous vehicles may blur the line between public and private transport and lead to a substantial increase in the utilization of vehicles and a corresponding reduction in road congestion.

Final Thoughts

In a world of low returns and lower interest rates, unlisted infrastructure has emerged as a compelling asset class for investors seeking relatively low volatility returns uncorrelated with equities, and opportunities to access growth assets with consistent income streams. However, unlisted infrastructure is not a homogenous asset class; detailed analysis and due diligence of the specific infrastructure asset and selection of an appropriate manager with experience and track record is key prior to making an investment.

[7] *Australian PV Institute Solar Map, funded by the Australian Renewable Energy Agency, June 2016*

AMP Capital

AMP Capital is one of Asia-Pacific's largest investment managers, responsible for over A$160bn in assets under management as at 31 December 2015. AMP Capital has over 50 years of experience managing investments for clients globally and has a presence in Asia-Pacific, Europe and North America.

AMP Capital is a majority-owned subsidiary of AMP Limited. Established in 1849 and with over 160 years of experience in providing financial services, AMP Limited (AMP), AMP Capital's parent company, has over 4 million clients and employs a network of more than 5,400 staff members worldwide. AMP is Australia's largest pension provider, with over A$215bn in assets under management as at 31 December 2015. AMP was listed on the Australian and New Zealand stock exchanges in 1998 and now has around 820,000 shareholders.

In March 2012, AMP Capital entered into a strategic business and capital alliance with a leading Japanese trust bank, Mitsubishi UFJ Trust and Banking Corporation (MUTB). As part of the alliance, MUTB acquired a 15% minority interest in AMP Capital Holdings Limited (AMPCH), the parent company of the AMP Capital group of companies.

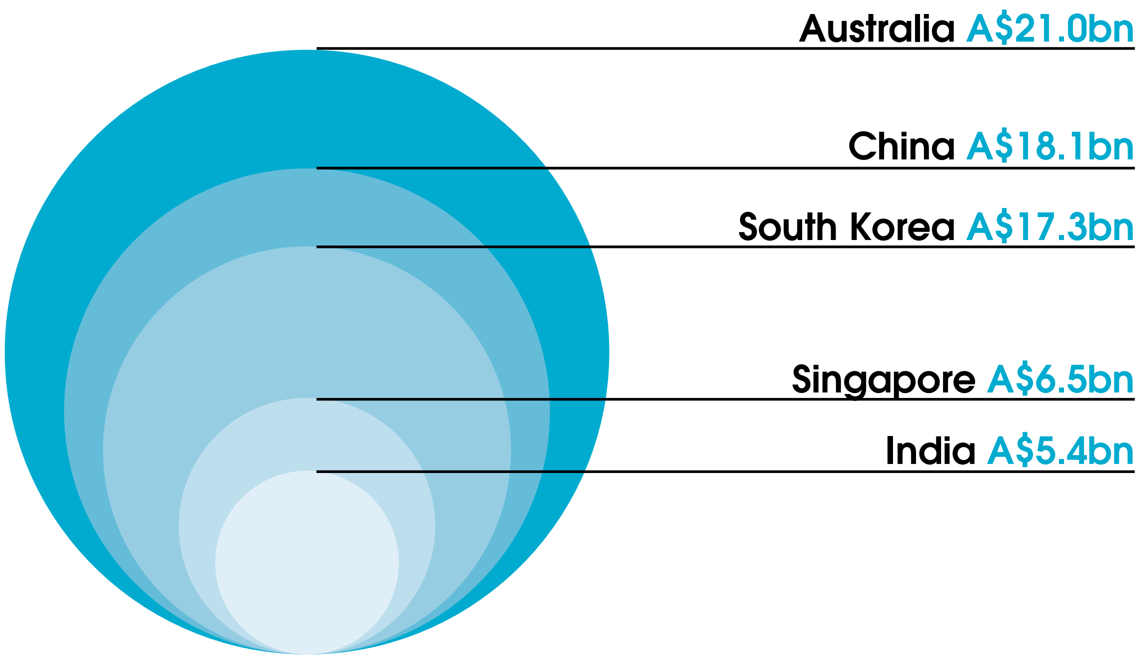
AMP Capital has been investing in infrastructure for around 30 years, beginning with its participation in the financing of the Sydney Harbour Road Tunnel in Australia in 1988. AMP Capital is one of the longest-standing participants in global infrastructure investments and has made over 125 infrastructure equity and debt investments throughout Europe, Asia, North America, Australia and New Zealand.

Michael Cummings is the Head of Australia and New Zealand Funds in AMP Capital's Global Infrastructure Equity division and the Fund Manager of the AMP Capital Diversified Infrastructure Trust (ADIT), which invests in a diversified portfolio of mature, well-performing infrastructure assets in Australia and New Zealand. ADIT has a since inception post-fee return of >11% per annum from 1995, including a 20.4% per annum post-fee return for the year to 30 June 2016. For more information on AMP Capital's infrastructure capability, please visit:

www.ampcapital.com/investing-with-us/infrastructure-us

Assets under Management and Dry Powder

Fig. 5.1: Asia-Pacific Infrastructure Assets under Management (As at December 2015)

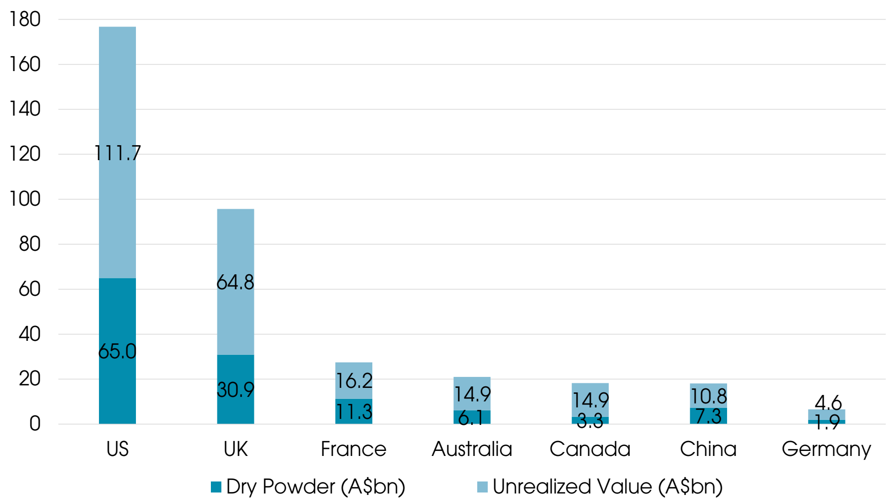


Source: Preqin Infrastructure Online

The Australian infrastructure industry is the largest among its peers in the Asia-Pacific region, with A$21.0bn in AUM, surpassing the A$18.1bn and A$17.3bn held by unlisted infrastructure firms in China and South Korea respectively (Fig. 5.1). While not comparable in size to the AUM of managers operating in the US and UK, the Australian market surpasses that of Canada (A$18.2bn, Fig. 5.2).

Furthermore, only 29% of Australia's AUM is held as dry powder, with the vast majority forming the unrealized value of portfolio assets. This represents the smallest proportion of dry powder among all major infrastructure markets in Asia-Pacific, and is behind only Canada in terms of major global markets, where 18% of infrastructure AUM is dry powder.

Fig. 5.2: Infrastructure Assets under Management by Location: Australia vs. Other Major Markets (As at December 2015)



Source: Preqin Infrastructure Online

Data Source:

Preqin's **Infrastructure Online** is Preqin's flagship online infrastructure information resource and covers all aspects of the asset class, including fund managers, fund performance, fundraising, institutional investors, deals and more.

For more information, or to arrange a demonstration, please visit:

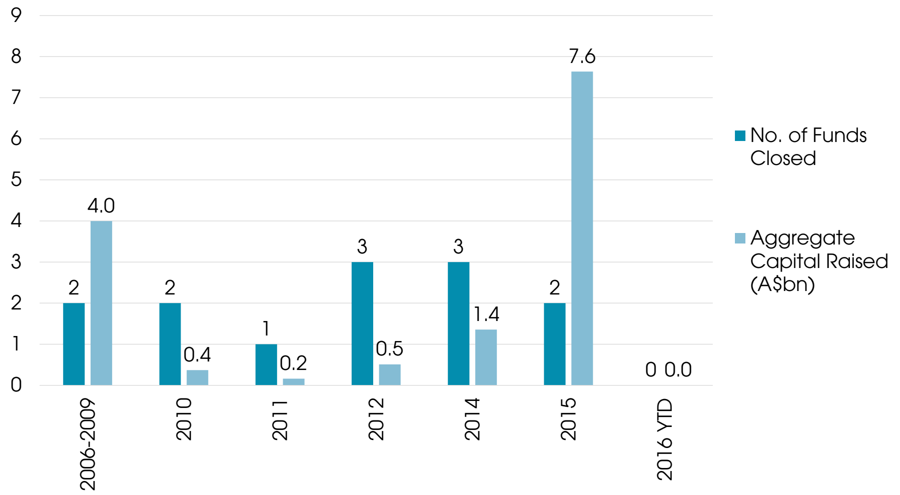
www.preqin.com/infrastructure

Fundraising

The unlisted infrastructure fundraising market by firms headquartered in Australia is relatively concentrated; only 13 vehicles have reached a final close since 2006, securing A$14.1bn in institutional capital commitments (Fig. 5.3). Between one and three unlisted funds close annually, although no funds closed in 2006, 2008, 2009 and 2016 YTD. Despite this, vehicles closed in recent years have been relatively large, with 2015 seeing record levels of capital raised by just two vehicles: Westbourne Capital secured A$4.8bn for Westbourne Capital Infrastructure Debt Fund Program 1, while Colonial First State Global Asset Management/First State Investments raised €2bn for First State European Diversified Infrastructure Fund.

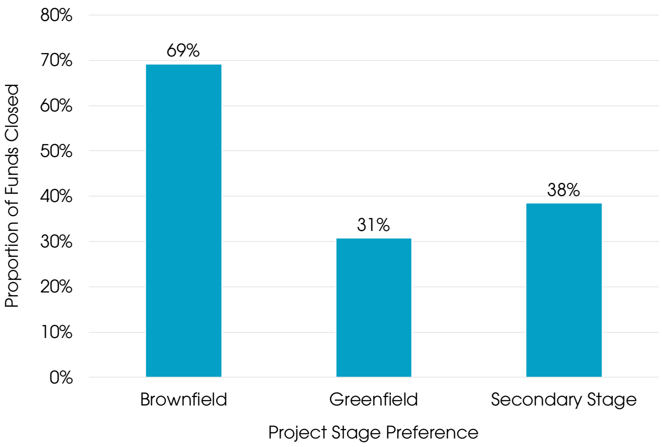
Since 2006, the majority (69%) of funds closed will target assets at the brownfield stage, although greenfield and secondary stage assets are targeted by 31% and 38% of funds closed respectively. After a record year in 2015 for Australia-based fundraising, managers in the country are keen to bring funds to market. There are currently a record nine Australia-based funds in market, seeking A$8.7bn from investors; the largest of these is AMP Capital Investors' AMP Capital Infrastructure Debt Fund III, which is targeting US$2bn for investment in the subordinated debt of defensive, non-cyclical infrastructure businesses in OECD markets including Europe, North America and Australia.

Fig. 5.3: Annual Australia-Based Unlisted Infrastructure Fundraising, 2006 - 2016 YTD (As at August 2016)



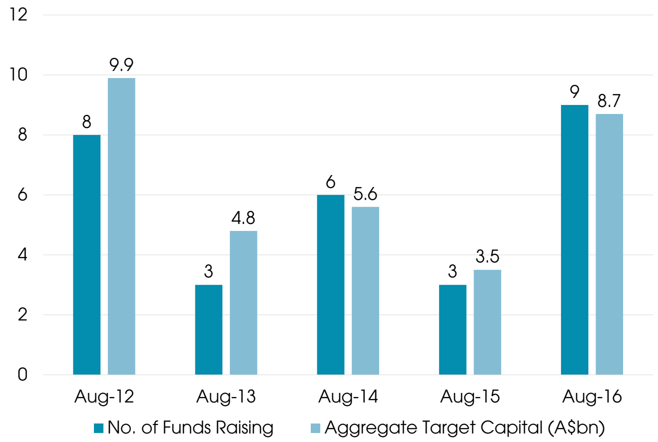
Source: Preqin Infrastructure Online

Fig. 5.4: Australia-Based Unlisted Infrastructure Fundraising by Project Stage Preference, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Infrastructure Online

Fig. 5.5: Australia-Based Unlisted Infrastructure Funds in Market over Time, August 2012 - August 2016



Source: Preqin Infrastructure Online

Data Source:

Use Preqin's **Infrastructure Online** to search for firms actively targeting infrastructure projects and assets, with detailed profiles on fund managers, institutional investors and trade buyers from around the world.

For more information, or to arrange a demonstration, please visit:

www.preqin.com/infrastructure

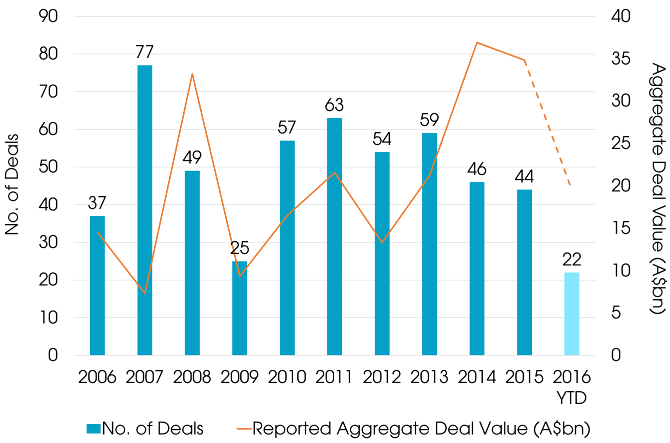
Deals

There have been 593 completed infrastructure deals in Australia since 2006 for a reported A$228bn. Annual deal flow peaked in 2007 with 77 transactions, although numbers fell for two consecutive years, reaching a nadir of 25 completed deals in 2009 (Fig. 5.6). Post-crisis saw a stabilization of infrastructure deals, with an average of 58 deals completed annually between 2010 and 2013. Despite numbers falling since, reported aggregate deal value continued rising and reached a record A$36.9bn and A$34.8bn in 2014 and 2015 respectively, surpassing the pre-crisis peak in 2008 (A$33.3bn). Driving the increase in aggregate deal value are the rising entry prices for infrastructure assets, with the average deal size increasing annually from 2012 to record levels in 2014 (A$930mn) and 2015 (A$943mn, Fig. 5.7).

Deals involving transport assets make up the largest proportion (33%) of deals since 2006, although recent years have seen the asset type rise further in prominence: transport deals completed in 2013, 2015 and 2016 YTD represent 46%, 50% and 55% of the annual number of deals respectively (Fig. 5.8). Conversely, deals involving utilities assets were more prominent between 2006 and 2012, with the annual proportion fluctuating between 7% and 12% in more recent years, down from 21-30% of deals in earlier years.

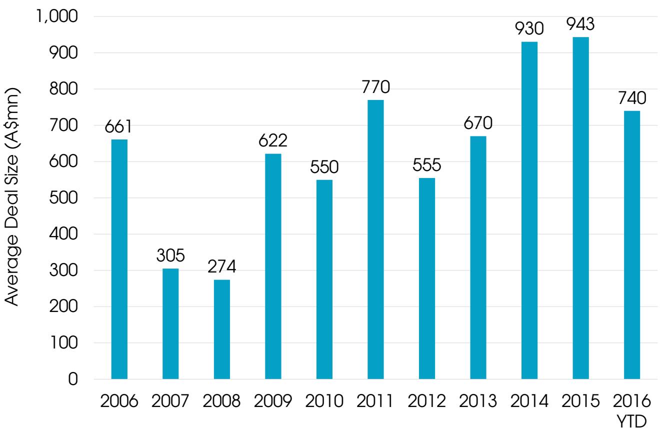
The majority of completed infrastructure deals were for established assets at the secondary stage; 62% of deals completed since 2006 have been for secondary stage assets, with a quarter of deals for greenfield and 13% involving brownfield opportunities. However, the proportion accounted for by secondary stage assets has fallen for three consecutive years, from 78% of transactions in 2013 to 50% in 2015; only 27% of completed deals in 2016 so far are for assets at the secondary stage of development, potentially a reflection of higher valuations for income-generating assets (Fig. 5.9). Correspondingly, there has been a rise in the proportion of brownfield deals; in 2013, brownfield assets were involved in just 2% of all Australian deals, and this has risen for three consecutive years to almost a third of deals in 2015 and 45% in 2016 so far.

Fig. 5.6: Number and Aggregate Value of Completed Australian Infrastructure Deals, 2006 - 2016 YTD (As at August 2016)



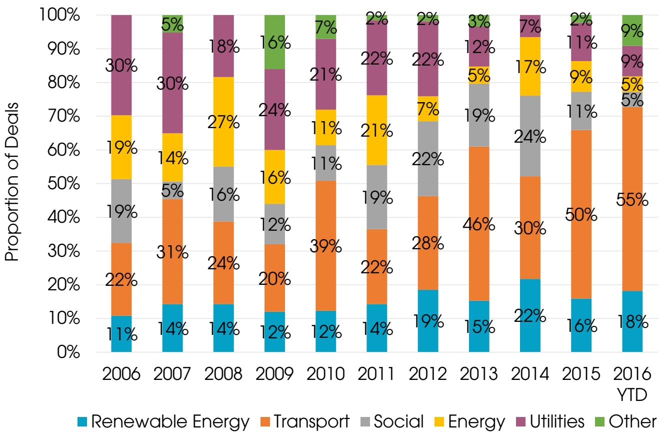
Source: Preqin Infrastructure Online

Fig. 5.7: Average Size of Completed Australian Infrastructure Deals, 2006 - 2016 YTD (As at August 2016)



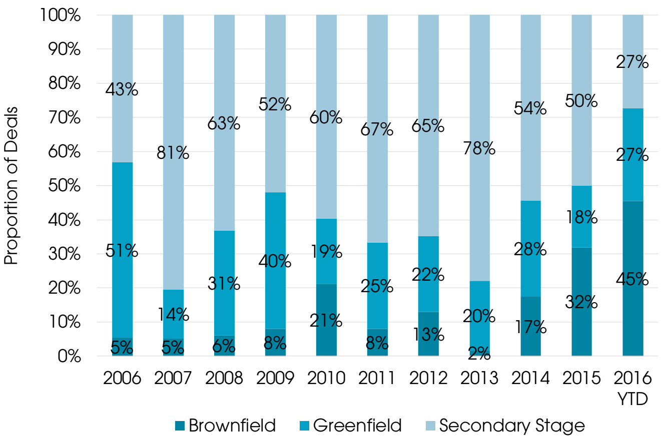
Source: Preqin Infrastructure Online

Fig. 5.8: Completed Australian Infrastructure Deals by Industry, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Infrastructure Online

Fig. 5.9: Completed Australian Infrastructure Deals by Project Stage, 2006 - 2016 YTD (As at August 2016)



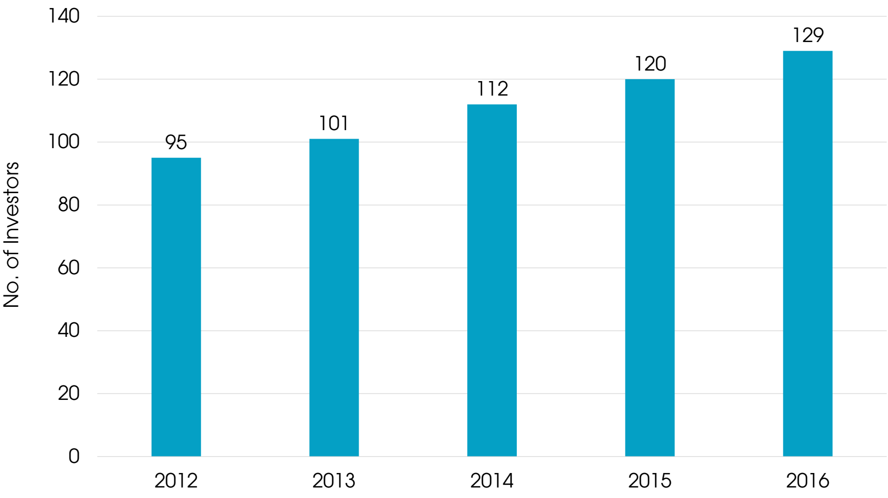
Source: Preqin Infrastructure Online

Investors

The number of Australia-based institutions investing in infrastructure has increased by 36% since 2012, standing at 129 investors in 2016 (Fig. 5.10). With increasing numbers of participants with varying levels of exposure, the average allocation to the asset class has remained relatively consistent at approximately 6.3% of total assets (Fig. 5.11). Furthermore, Australia-based investors have, on average, been under-weighted to the asset class, with a spread of approximately 160 basis points between their current and target allocations. This is encouraging for the future growth of infrastructure in Australia as investors will continue to commit capital over the short to mid-term in order to move closer to their targets.

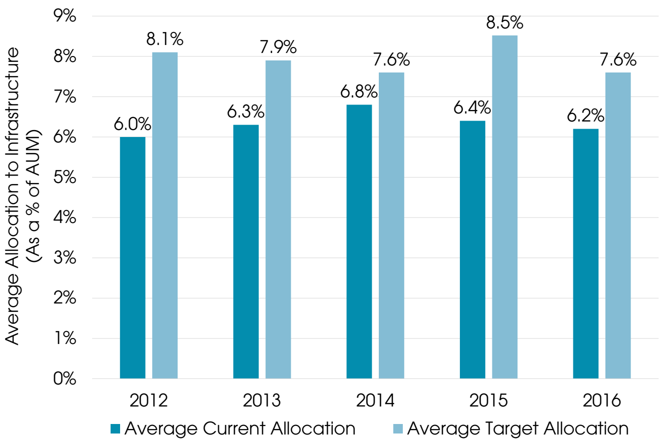
The longer term investment horizons, as well as infrastructure's ability to generate steady cash flows, makes the asset class compatible with superannuation schemes, which are looking to invest over longer timeframes, therefore allowing for more effective matching to their long-term liabilities against the returns of infrastructure investment. Consequently, superannuation schemes make up more than half (58%) of the infrastructure investor population in Australia, although asset managers also make up a notable 15% (Fig. 5.12). Furthermore, three of the top five infrastructure investors are superannuation schemes, including AustralianSuper, which currently has A$9bn invested in unlisted vehicles and direct investment in assets (Fig. 5.13).

Fig. 5.10: Number of Active Australia-Based Infrastructure Investors over Time, 2012 - 2016



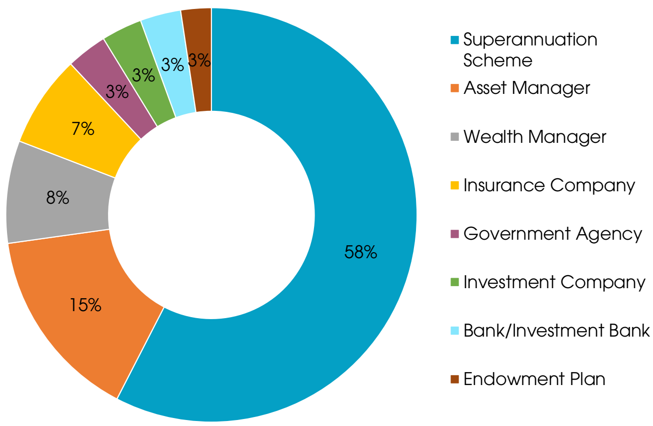
Source: Preqin Infrastructure Online

Fig. 5.11: Australia-Based Investors' Current and Target Allocations to Infrastructure over Time, 2012 - 2016



Source: Preqin Infrastructure Online

Fig. 5.12: Australia-Based Infrastructure Investors by Type



Source: Preqin Infrastructure Online

Fig. 5.13: Top Five Australia-Based Infrastructure Investors by Current Allocation

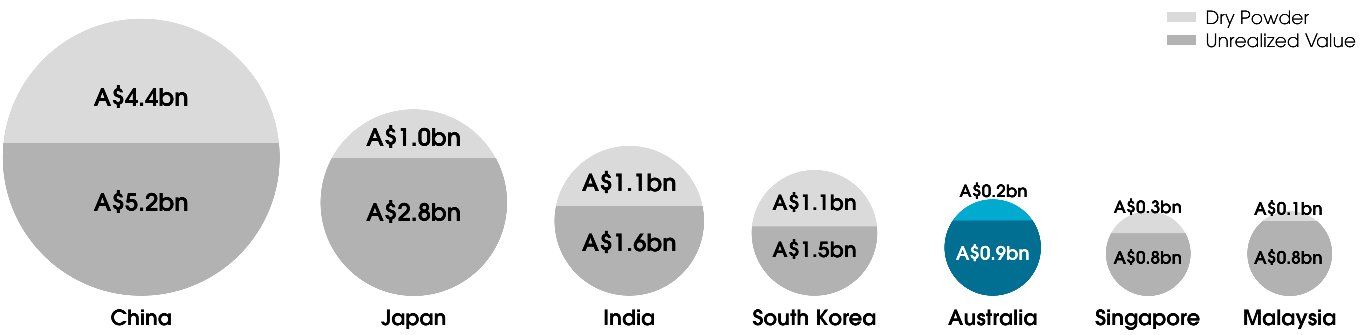
Investor	Location	Type	Current Allocation to Infrastructure (A$bn)
AustralianSuper	Melbourne, Victoria	Superannuation Scheme	9.0
Future Fund	Melbourne, Victoria	Sovereign Wealth Fund	8.2
QIC	Brisbane, Queensland	Asset Manager	5.7
First State Super	Sydney, New South Wales	Superannuation Scheme	5.1
QSuper	Brisbane, Queensland	Superannuation Scheme	3.9

Source: Preqin Infrastructure Online

Assets under Management and Dry Powder

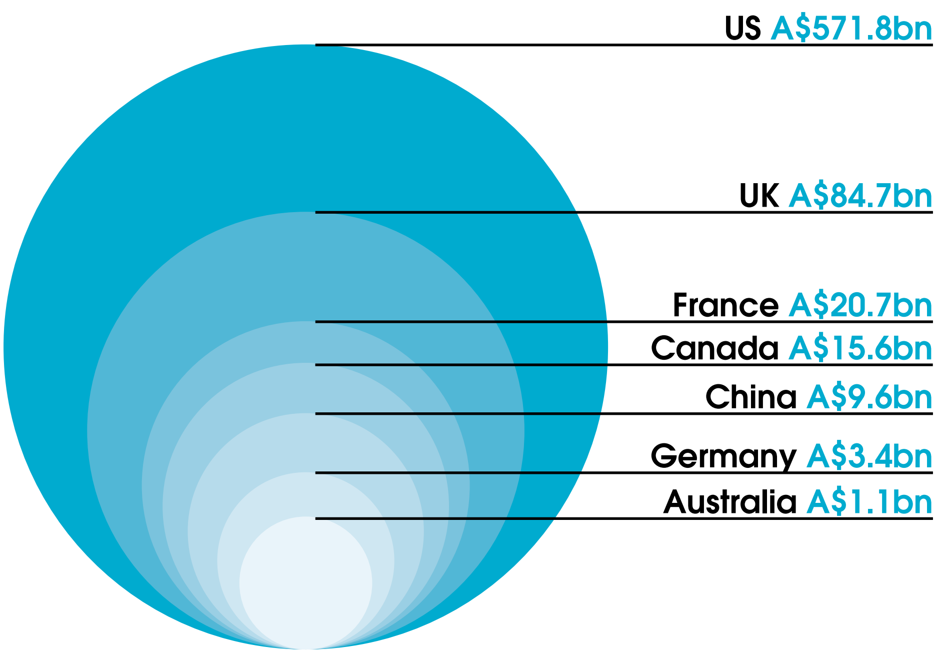
The Australian private debt industry is still nascent in its development as a distinct asset class – industry AUM lags behind that of the more developed debt markets in Asia-Pacific (Fig. 6.1). AUM of Australia-based private debt managers stands at A$1.1bn, equivalent to that of the Singaporean industry, but behind China (A$9.6bn), Japan (A$3.7bn) and India (A$2.7bn).

Fig. 6.1: Private Debt Assets under Management by Location: Australia vs. Asia-Pacific (As at December 2015)



Source: Preqin Private Debt Online

Fig. 6.2: Private Debt Assets under Management by Location: Australia vs. Other Major Markets (As at December 2015)



Source: Preqin Private Debt Online

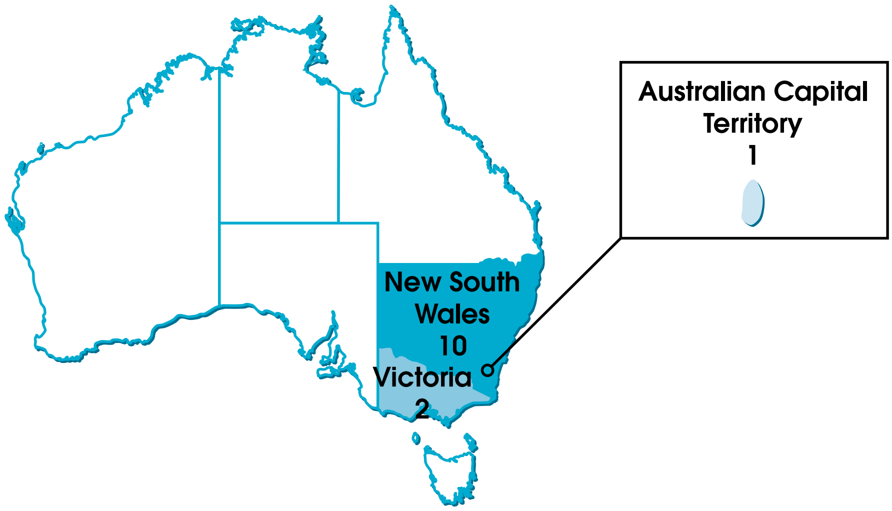
Fundraising

With the asset class just gaining a foothold in Australia, it is unsurprising that the majority (62%) of private debt fund managers operating in the country are first-time private debt fund managers (Fig. 6.4).

Of all Australia-based private debt funds raised historically, a larger proportion (44%) of special situations vehicles have reached a final close than any other fund type, although these vehicles are responsible for only 14% of the aggregate capital raised by managers in the region (Fig. 6.5). Despite only 11% of private debt funds closed following a distressed debt strategy, the fund type represents the majority of capital raised, likely due to the closure of GS Special Opportunities Asia, which secured $2.5bn to become the largest private debt vehicle raised by an Australia-based manager to date.

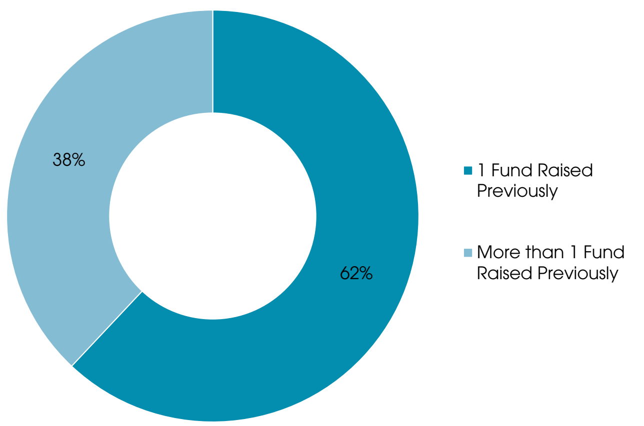
There is currently only one private debt fund in market from an Australia-based firm: Continuity Capital Partners is seeking $100mn for Continuity Capital Private Credit Fund No.2, a fund of funds vehicle focused on Australasia that works alongside credit managers to make co-investments.

Fig. 6.3: Australia-Based Private Debt Fund Managers by Location



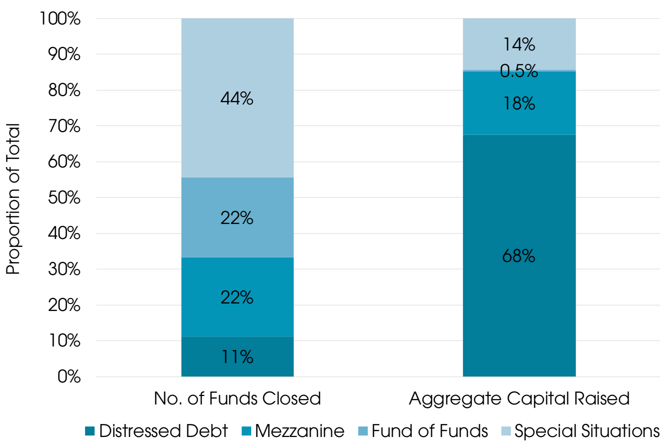
Source: Preqin Private Debt Online

Fig. 6.4: Australia-Based Private Debt Fund Managers by Experience



Source: Preqin Private Debt Online

Fig. 6.5: Australia-Based Private Debt Fundraising by Fund Type, All Time



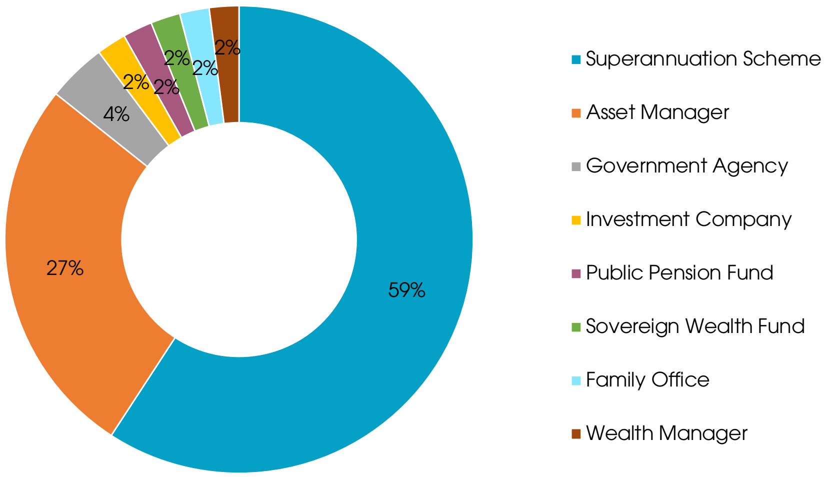
Source: Preqin Private Debt Online

Investors

Australian private debt has not historically been targeted by fund managers or investors on an international level. However, Preqin's **Private Debt Online** tracks 51 institutional investors that have made commitments to funds raised by Australia-based managers, with more than half (56%) of these commitments coming from investors in the US. There are also a further 49 Australia-based investors in private debt; the majority (59%) of these investors are superannuation schemes, although a notable proportion (27%) are asset managers (Fig. 6.6). With these being typically large institutions, the majority (54%) of private debt investors hold more than $10bn in AUM, and only 13% have assets of less than $1bn (Fig. 6.7).

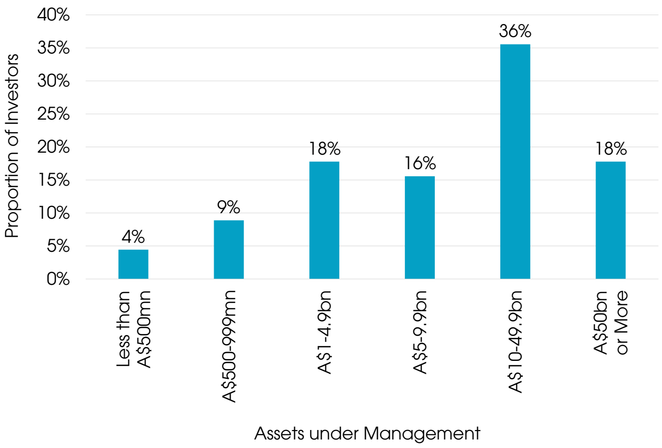
As seen in Fig. 6.8, most Australia-based private debt investors are based in Victoria or New South Wales, with Sydney and Melbourne the most prominent locations. IFM Investors is the largest private debt investor in Australia with A$5.7bn of its total assets allocated to the asset class (Fig. 6.9).

Fig. 6.6: Australia-Based Private Debt Investors by Type



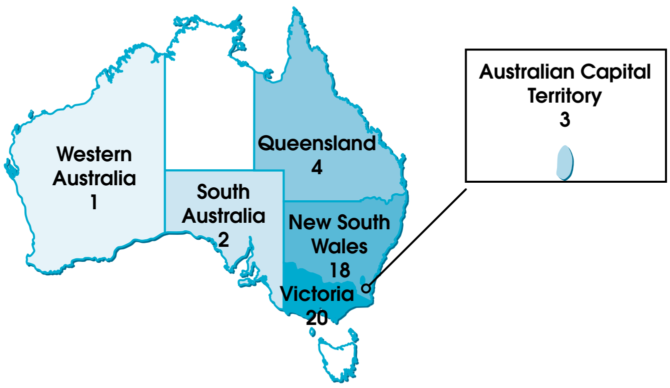
Source: Preqin Private Debt Online

Fig. 6.7: Australia-Based Private Debt Investors by Assets under Management



Source: Preqin Private Debt Online

Fig. 6.8: Australia-Based Private Debt Investors by Location



Source: Preqin Private Debt Online

Fig. 6.9: Top Five Australia-Based Investors by Current Allocation to Private Debt

Investor	Location	Type	Current Allocation to Private Debt (A$bn)
IFM Investors	Melbourne, Victoria	Asset Manager	5.7
Future Fund	Melbourne, Victoria	Sovereign Wealth Fund	5.1
QIC	Brisbane, Queensland	Asset Manager	3.7
Victorian Funds Management Corporation	Melbourne, Victoria	Asset Manager	3.1
Pinnacle Investment Management	Sydney, New South Wales	Asset Manager	0.9

Source: Preqin Private Debt Online


Source new investors for funds
Identify new investment opportunities
Conduct competitor and market analysis
Track firms with capital available to invest
Develop new business

Pivot to Top-Quartile Returns

- Andrew Duff, Policy Officer, Department of Agriculture and Food, Western Australia

Readers may have a sneaking suspicion that taking advantage of capital superabundance and unlocking value for investors in the future may not come from traditional models. However, taking concrete steps to implement a shift in approach is challenging.

If strong returns are to be generated from Australian agrifood then there is a need for business model shifts. Investors will readily accept this assertion for investees. General partners may also care to consider this for fund business models.

Australian Agriculture in Context

Australia, throughout its history, has needed to access capital from external pools. It has never had the scale of savings to be self-sufficient. As a result, there is a long history of international investors putting capital to work. Australia as a destination for investment steps through its top-level hygiene tests easily. Its separation of powers, rule of law and minimal industry subsidies create a strong platform for business. As a result significant agricultural assets are owned by foreign interests. UK, US, Dutch, Singaporean and Chinese investors are the top five foreign owners of Australian agricultural land with international interests collectively comprising 13.6% of the total according to a report released this month by the Australian Tax Office[1].

Some may also take the view that Australia offers an ideal risk-managed approach to engaging Asian growth markets while side-stepping direct investment. Agriculture is 12% of GDP in Australia. It generates over A$150bn annually and delivers above A$32bn in exports.

To illustrate the opportunities in Australian agriculture we focus on the case of Western Australia (WA). WA is the state with the largest land area occupying almost a third of the nation's land mass. Its geography is diverse, running from tall, timbered, temperate forests in the South to the harsh tropical climate in the North.

Globally, there are not many jurisdictions that extend over such a large range of latitudes. As well, WA is in the same time zone as most of Asia. Due to its southern hemisphere location, it offers counter seasonal production to Northern Hemisphere markets. WA has nine broad agrifood production platforms[2]. These are: beverages; processed foods; dairy and eggs; produce; seafood; meat; oilseeds, oils and fats; animal foods and feeds; grains. In sectors where it operates at scale (mostly grains), Western Australia is a low-cost producer and land cost per unit of production is also low. WA predominantly produces and exports bulk raw material ingredients transformed into finished goods by firms elsewhere.

While Western Australia has an enormous landmass, not all of it is suitable for agriculture. It is also true that agricultural performance is not uniform across or within industries. So where are the most compelling investment opportunities?

International Markets

Due to its small domestic market, the majority of investment-grade opportunities are export linked. China, the Southeast Asian common market, India and the Middle East are all experiencing unprecedented growth in demand for agriculture and food products.

The amount of capital required to support the development of Australian agriculture is well documented. The ANZ Insights Greener Pastures Report[3] estimates that Australia will need A$1tn in additional capital investment to achieve A$710bn in agricultural exports between 2011 and 2050.

If the investment opportunities in agriculture are so compelling, we would expect to see strong flows of capital from Australian institutional investors to funds specializing in the agriculture asset class. This is not the case. Federal Minister for Agriculture, Barnaby Joyce, is on the public record[4] encouraging Australian superannuation funds to commit more capital to support the growth of Australian agriculture. Currently, less than 1% of superannuation funds under management are put to work in agriculture[5]. University of Queensland researchers studying super fund investment allocations[6] developed the view that the lack of investable products and a shortage of managers with sector experience present obstacles to investment in the sector.

However, the opportunities represented by Australian agriculture are not being ignored. Many international funds have investments in Australia and new ones with a specific Australian targets are being formed. For example, at the end of July, Beijing-based Tsing Capital announced that it is establishing a new US$1bn capital fund designed to invest in downstream processing of high-value products in the Australian food and agriculture sectors for the Chinese market[7].

There is strong evidence that the Australian farming sector can achieve world class performance. Where it is internationally competitive, Western Australian agriculture has delivered exceptional returns. In one report, the financial performance of 270 broad acre farm businesses in Western Australia achieved better returns than the

[1] *http://apo.org.au/node/67304 page 6*
[2] *Coriolis Research (2016) Pathways to Competitiveness Report (page 16) https://agric.wa.gov.au/n/5807*
[3] *Accessed 18 August 2016: http://media.corporate-ir.net/media_files/IROL/24/248677/ANZ_insight_3_Greener_Pastures.pdf*
[4] *For example: Barnaby Joyce Australian Financial Review http://www.afr.com/news/policy/joyce-urges-super-funds-to-invest-in-agriculture-20160229-gn65ib*
[5] *Accessed 18 August 2016: http://www.bdo.com.au/getattachment/19e23d14-5beb-4309-b8c9-f5d22345329d/Agribusiness-Superannuation-Investment-Report-LOW-RES-120216.pdf.aspx*
[6] *Australian Superannuation Fund Investment In Agriculture 2014/15 (page 5), Accessed 31 August 2016: http://www.bdo.com.au/getattachment/19e23d14-5beb-4309-b8c9-f5d22345329d/Agribusiness-Superannuation-Investment-Report-LOW-RES-120216.pdf.aspx*
[7] *Accessed 18 August 2016: http://www.afr.com/business/agriculture/chinas-tsing-capital-backs-1-billion-australian-agriculture-fund-20160726-gqeazc; http://www.weeklytimesnow.com.au/agribusiness/tsing-capital-sets-up-food-and-agritech-fund/news-story/a50ddc631b64e897ef56d2b104c230b1*

Australian share market All Ordinaries Index during the decade from 2002 to 2011[8].

Strategic Data-Driven Insights

Readers may be heartily tired of opinion pieces observing that there is a lot of opportunity in Asia.

Defining the most compelling opportunity spaces requires a clear understanding of trade growth on a market-by-market basis.

Such work must provide answers to questions such as:

- What agrifood products are in strongest demand in Asia and the Middle East?
- Which markets are growing most rapidly?
- Where are prices highest?
- Which competitors are most active in those markets?

To enable evidence based agricultural entrepreneurship the Department of Agriculture and Food in Western Australia commissioned professional services firm Coriolis Research to target the most compelling international growth opportunities.

This work identifies that there are multiple instances where Western Australia's ability to produce meets the strongest demand from Asia and the Middle East. Coriolis maps this precisely and presents the results in the following reports:

Target Market Opportunities: highlights the intersection between what Western Australia produces and what Asia wants[9];

Pathways to Competitiveness: sets out the requirements for export market success including high yields, large operations, proven scalable systems and top-class skills and experience[10];

Growing the North: identifies the strongest 18 opportunities in Asia for agricultural products from new irrigation precincts opening in Northern Western Australia[11].

A Business Model Pivot?

Achieving the scale necessary to engage institutional investment requires creative approaches. Inevitably this includes adopting a networked perspective. Traditionally in grain and beef sectors businesses have managed risk and achieved scale in a dedicated area of focus by aggregating farms across regions, climates and soil types.

New models will extend this concept. Other network paradigms include businesses that participate across multiple segments of the value chain. Such whole of value chain approaches will include links in Australia and Asia. Another is assembly of networks of complimentary assets. For investors interested in water assets, linking land precincts with water sources of multiple different types could be contemplated e.g. rivers, dams, mine-produced water, aquifers, and aquifer recharge. This approach is applied now on pastoral properties. Irrigated agricultural crops, which include sorghum, perennial grasses, lucerne and tropical legumes, are helping to diversify the feed base accessed by beef cattle. Other solutions will see differentiated capabilities used to create a superior end-customer value. Businesses that have adopted tech and digital platforms are clear candidates in this space.

To optimize the value generated in new business models funds seeking top returns will also need an aligned approach. In broad terms this means that they will need operating experience and leadership capabilities that reflects the key needs and desired growth trajectories of their investees. For Australian agrifood this will often imply the ability to operate effectively in Australian and Asian business environments.

Conclusion

Significant value can be created by Australian production helping meet food needs in Asia. However, optimizing the opportunity is not about retaining traditional transactional business models. Integrated approaches developed first in other sectors are required to generate the best returns.

Australian businesses holding equity in value chain components closer to the consumer end will be key to achieving alignment of incentive. As well, partnering and alliancing (vis-à-vis cooperatives) will have a far stronger role to play into the future. Traditional win/lose producer/processor transaction models will not figure in the new highly competitive global business environment.

There is clearly a critical value added role for fund managers in enabling innovation, supporting execution and creating leadership teams to deliver successfully on these types of business models. This demands a fund structure and operational innovation to match the business model innovation required of potential investees. Limited partners, especially those with co-investment interests, should also weigh in on this debate.

[8]Kingwell, R (2014), Returns on offer from family farming: some observations, Proceedings of the Funding Agriculture's Future Conference, Australian Farm Institute, Canberra: http://www.farminstitute.org.au/newsletter/2014/August_2014/August_2014_featurearticle.html
[9]Target Market Opportunities Coriolis Research (2016) https://agric.wa.gov.au/n/5392
[10]Pathways to Competitiveness Coriolis Research (2016) https://agric.wa.gov.au/n/5807
[11]Growing the North Coriolis Research (2015) https://agric.wa.gov.au/n/5807

Department of Agriculture and Food, Western Australia

DAFWA drives the economic development of Western Australia's agriculture and food sector, with a focus on export-led growth. Our department's role is to support the success of the state's agrifood businesses by delivering our Agrifood 2025+ Strategic plan and, in turn, achieving our vision of 'a progressive, innovative and profitable agriculture and food sector that benefits Western Australia'. We support all aspects of food and fibre production at each stage of the supply chain. This is achieved by building market knowledge and conducting innovative research and development and marketing and extension programs. We also develop and enforce regulations that ensure the production of high-quality, safe and healthy food for our customers in Australia and overseas.

Andrew Duff is a Policy Officer within Irrigated Agriculture. He is a team member delivering the Agricultural Sciences Research and Development Fund project within the Department of Agriculture and Food, Western Australia (DAFWA)

GOVERNMENT OF WESTERN AUSTRALIA

Department of **Agriculture** and **Food**

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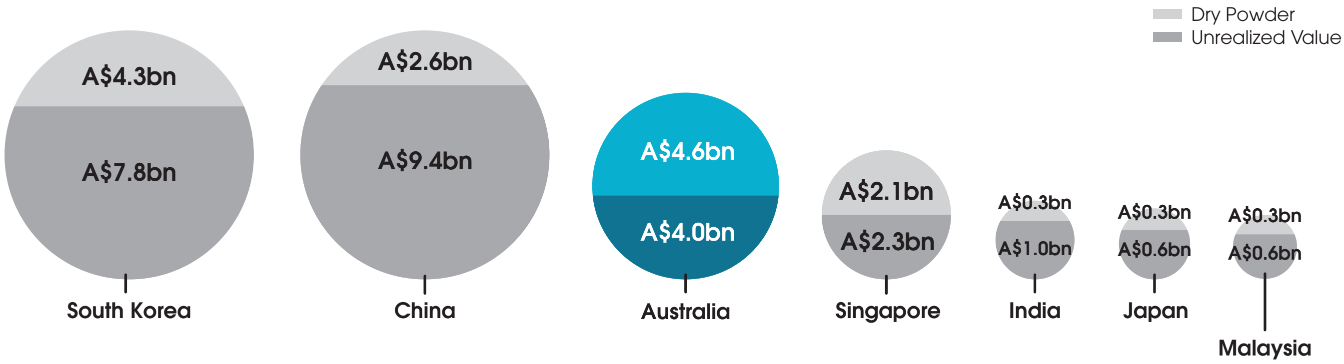
Assets under Management and Dry Powder

The Australian natural resources industry is the third largest in the Asia-Pacific region by AUM with A$8.6bn, below that of unlisted natural resources firms in China and South Korea which each hold A$12bn in AUM (Fig. 7.1). While US-based firms dominate global natural resources AUM with A$384bn, the UK and Canadian markets are still more than quadruple and double the size of the Australian industry respectively. However, Australia-based firms hold more than 6.5x the AUM of managers in India, and approximately double that of Singapore- and France-based managers.

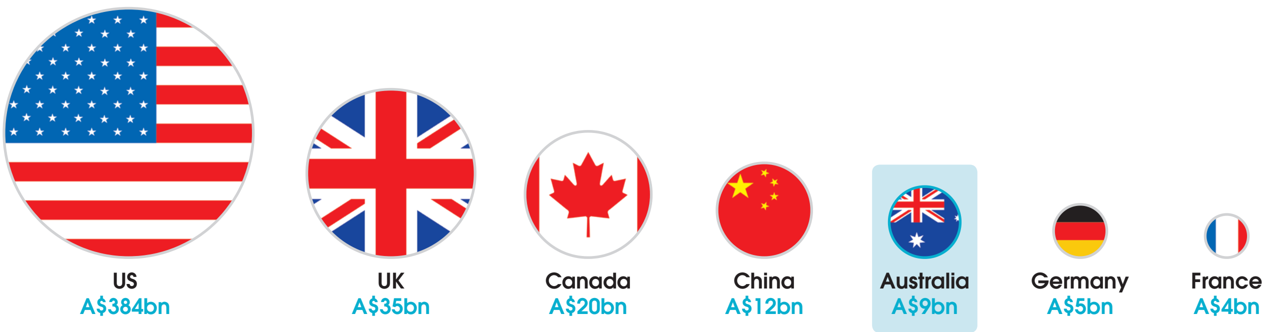
Australia-based firms do have considerable sums of uncalled capital at their disposal relative to the country's peers in Asia-Pacific: their A$4.6bn in dry powder is A$2bn more than that of China-based natural resources managers and A$300mn more than that of South Korea-based firms.

Fig. 7.1: Natural Resources Assets under Management by Location: Australia vs. Asia-Pacific (As at December 2015)



Source: Preqin Natural Resources Online

Fig. 7.2: Natural Resources Assets under Management by Location: Australia vs. Other Major Markets (As at December 2015)



Source: Preqin Natural Resources Online

Data Source:

Natural Resources Online offers a comprehensive overview of the natural resources fund industry, covering funds, fund managers and institutional investors. Information is constantly updated by our dedicated teams of analysts, ensuring that we provide the most extensive, up-to-date information available on all aspects of the industry.

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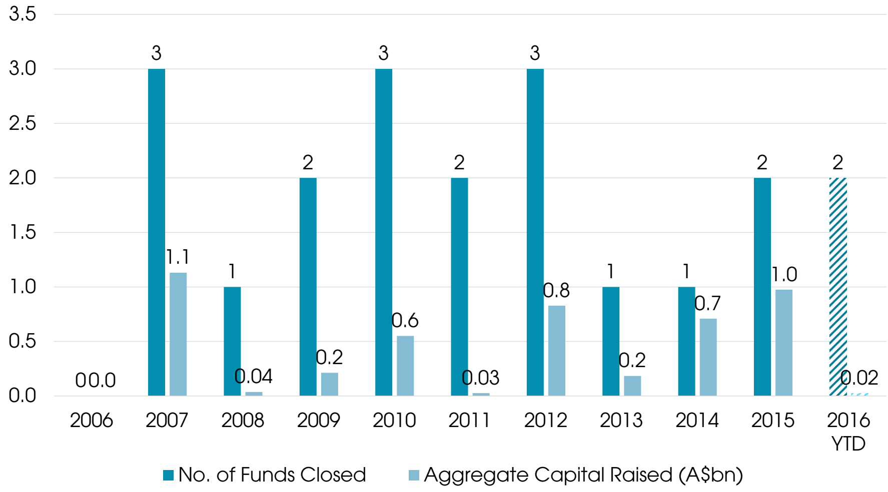
Fundraising

Similar to the infrastructure fund market, the number of Australia-based unlisted natural resources funds reaching a final close has failed to surpass three vehicles annually. Since 2006, 20 unlisted natural resources funds have reached a final close, securing A$4.7bn in commitments, although aggregate capital raised annually has fluctuated from lows of A$25mn in 2011 to highs of A$1bn in 2015 (Fig. 7.3).

Unsurprisingly for one of the world's largest producers of mineral products, the largest proportion of Australia-based vehicles closed focus on investments in metals & mining (Fig. 7.4): eight metals & mining funds have closed since 2006, securing an aggregate A$2.5bn. Energy-focused funds account for a much smaller proportion of the Australia-based fundraising environment than their peers globally, representing just 5% of funds closed and 1% of aggregate capital raised since 2006. Timberland natural resources funds are also prevalent in the market, accounting for a quarter of funds closed since 2006 and 31% of aggregate capital raised.

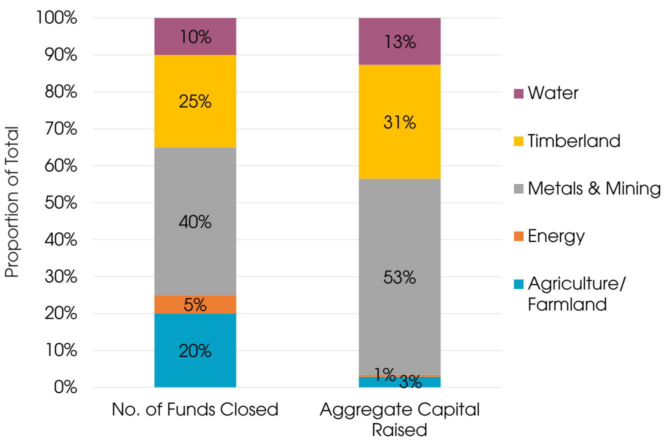
Fig. 7.3: Annual Australia-Based Unlisted Natural Resources Fundraising, 2006 - 2016 YTD (As at August 2016)



Source: Preqin Natural Resources Online

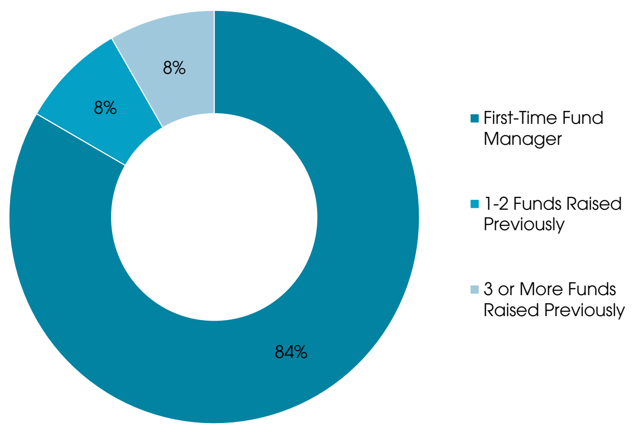
There are currently 13 Australia-based unlisted natural resources funds in market, targeting A$12.6bn in commitments from investors. With natural resources still in a nascent stage of development as a distinct asset class, it is unsurprising that 84% of these funds in market are being raised by first-time natural resources fund managers (Fig. 7.5). Interestingly, the composition of these vehicles differs from the historical fundraising statistics, with half of funds in market primarily targeting investments in energy and only one fund seeking investment in metals & mining.

Fig. 7.4: Australia-Based Unlisted Natural Resources Fundraising by Primary Strategy, 2006 - 2016 YTD



Source: Preqin Natural Resources Online

Fig. 7.5: Unlisted Australia-Based Natural Resources Funds in Market by Fund Manager Experience



Source: Preqin Natural Resources Online

Data Source:

Preqin's **Natural Resources Online** contains profiles for 13 natural resources funds currently being raised by fund managers based in Australia.

For more information, please visit:

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Forestry Investment in Australia and Asia-Pacific

- Radha Kuppalli, Executor Director and MaryKate Bullen, Associate Director, New Forests

The Asia-Pacific region has emerged as the centre of global timber demand. There is significant trade in logs, lumber, pulp, woodchips and bioenergy pellets among countries in Asia-Pacific, meeting demand from the growing middle classes across China, India and Southeast Asia, as well as industries exporting to global markets. Australia is a key player in this regional timber trade, represents an attractive geography for institutional forestry investors and is an entry point for timberland investment in the region.

Australian Forestry

Highly productive, professionally managed and sustainable plantation forestry investment is a core offering of the Australian market. The Australian forest industry is over 100 years old with well-established plantation management capacity, excellent growing conditions, infrastructure and markets. Australia has two million hectares of commercial timber plantations, approximately half hardwood (eucalyptus) and half softwood (pine).

Diversified Market Exposure

Australia offers diversification across domestic and export timber markets. The softwood timber primarily serves domestic residential construction markets. Australia has a wood products deficit of approximately A$2bn per year across all timber markets, reflecting the growing population and limited size of the plantation estate. In the past three years, however, with the decline of the Australian dollar, Australia has also begun to export small pine logs to China, with 10% of Chinese imports now coming from Australia. Eucalyptus plantations provide woodchip for the Asian pulp and paper industry based in Japan and China. Asian buyers are increasingly seeking out certified woodchip from Australia, which offers a stable, consistent and reliable supply of quality wood fibre. Australian timberland assets benefit from this diversified market exposure while offering low volatility returns, which is the most attractive feature of the timberland asset class.

Asia-Pacific Forestry Investment and Trade

The Australian timberland investment market is maturing, with more than half of Australian plantations held by institutional owners. New Forests has played a significant role in the acquisition and restructuring of plantation assets, generating very attractive returns for institutional investors. We expect the market to transition to mostly secondary opportunities over the next several years. Within a competitive marketplace, local expertise and active management are critical to strong investment performance, and investors should seek to expand their portfolio in other key forestry regions within Asia Pacific.

New Zealand also has about two million hectares of plantation forestry, nearly all pine plantations. New Zealand has a significant domestic processing industry, and over the past decade has emerged as the largest softwood log exporter to China, surpassing Russia. Like Australia, New Zealand benefits from an experienced forest industry with excellent infrastructure, technical capacity and growing conditions.

Investors seeking higher risk-adjusted returns and primary market opportunities in timberland should also look to Southeast Asia. Significant opportunities exist to develop new tropical timber plantations and improve the performance of existing under-capitalized plantation companies. Key species include teak, mahogany, eucalyptus and other specialty timbers for feature grade uses such as furniture and flooring. New Forests has been active in Southeast Asia for nearly a decade, building our local network and investment track record, where transactions require high sustainability credentials, excellent ESG risk management systems and professional forestry capacity. New Forests has worked with local businesses and other foreign investors in developing new plantations and improving existing assets. As harvesting of natural forests declines in the region – due to better regulation and sustainability concerns in the supply chain – certified, sustainable plantation forestry will be the future of the timber industry in Southeast Asia.

Local Manager with Strategic Reach

New Forests believes that investors can build a diversified portfolio of timber market exposures across mature and emerging markets in the Asia-Pacific region. With well-developed markets and low-risk environments, Australia and New Zealand form the core timberland market exposure for institutional investors in the region. Investors can expect net returns from these countries in the 6-7% real return range with strong, low volatility cash yield. Investors in Southeast Asian forestry can expect higher returns in the 10-12% real return range depending on jurisdiction and asset type. With the diversity of opportunities across the Asia-Pacific region, investors seeking to build a successful timberland portfolio should emphasize local knowledge, a regional presence and a dedicated focus on sustainability.

New Forests

New Forests is a sustainable real assets manager offering institutional investors targeted opportunities in the Asia-Pacific region and the United States. The company has over A$3bn in AUM across more than 700,000 hectares of forestry, land management, and conservation investments. New Forests is headquartered in Sydney, Australia with offices in Singapore and San Francisco.

www.newforests.com.au

To learn more about current trends in forestry investment, timber markets and opportunities for investing in the future of forestry, access the free download New Forests Timberland Investment Outlook, 2015-2019 at:

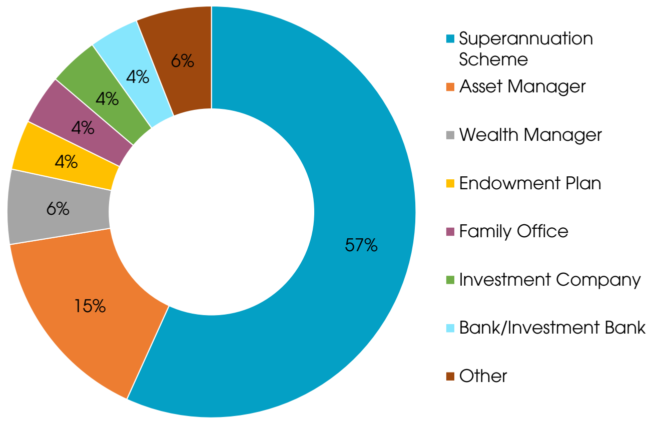
www.newforests.com.au/#insights

Investors

The majority (57%) of the 51 Australia-based natural resources investors profiled on Preqin's **Natural Resources Online** are superannuation schemes, followed by asset managers (16%) and wealth managers (6%, Fig. 7.6), a similar composition to those institutions seen investing in infrastructure (see page 38). With some typically large institutional investors, such as superannuation schemes and banks, it is unsurprising that a substantial proportion (44%) of natural resources investors have more than $10bn in total assets, while only a fifth of Australia-based investors have less than $1bn in AUM.

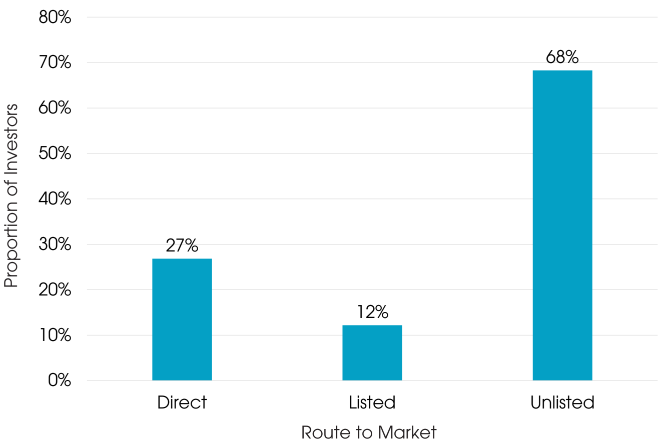
As seen in Fig. 7.7, the preferred route to the natural resources market is through unlisted funds (68% of investors), while 27% invest directly in assets. In terms of strategic preferences, the majority (76%) of Australia-based investors maintain a preference for energy investment, while a third target water and 31% invest in agriculture/farmland (Fig. 7.8). Despite metals & mining funds accounting for the largest proportion of capital raised by Australia-based fund managers since 2006, the strategy is only targeted by 16% of domestic institutional investors.

Fig. 7.6: Australia-Based Natural Resources Investors by Type



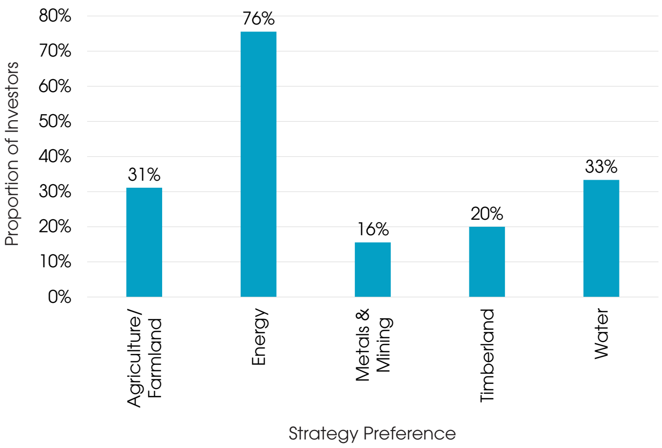
Source: Preqin Natural Resources Online

Fig. 7.7: Australia-Based Natural Resources Investors by Preferred Route to Market



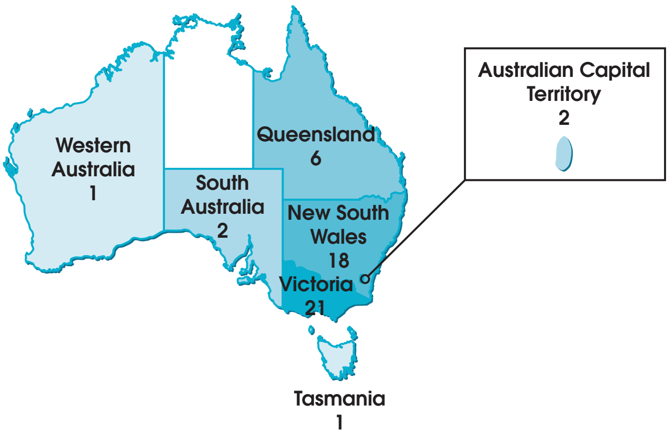
Source: Preqin Natural Resources Online

Fig. 7.8: Australia-Based Natural Resources Investors by Strategy Preference



Source: Preqin Natural Resources Online

Fig. 7.9: Australia-Based Natural Resources Investors by Location



Source: Preqin Natural Resources Online

Preqin Insight: Alternative Assets in Australia

October 2016

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