IFM Investors Chief Executive David Neal's speech to the South Australian Investment Conference 2022

FRIDAY 2 DECEMBER 2022 – CHECK AGAINST DELIVERY

I would like to begin by acknowledging that the land that we meet on today is the traditional lands for the Kaurna people and that we respect their spiritual relationship with their country.

I also acknowledge the Kaurna people as the custodians of the Adelaide region and that their cultural and heritage beliefs are still as important to the living Kaurna people today.

We also pay respects to the cultural authority of Aboriginal people attending from other areas of South Australia and Australia.

May I also acknowledge:

- Premier of South Australia the Honorable Peter Malinauskas
- Federal and State Members of Parliament who are with us today
- My fellow speakers and other distinguished guests

Thank you to the South Australian Government and the Committee for Adelaide for having us over the past two days.

At a time when all of us are dealing with so many short term issues, spending time on longer term challenges is important.

And speaking as a long-term investor, it is refreshing to see this type of long-term thinking.

It is with that in mind that I am going to focus my address on one of the most important systemic challenges we are facing today – climate change.

Here in South Australia – we've seen significant leadership when it comes to investing in the long-term energy security of the state through renewables, battery storage and hydrogen.

The essential need for energy security is something we are seeing play out in Europe in real time. The Russian invasion of Ukraine has seen Europe grapple with a near-term shortage of energy sources and supplies.

While this is leading to security-linked energy initiatives aimed at identifying reliable gas supplies from "friendly countries" or "friend-shoring", the real focus of policymakers remains on accelerating the long-term transition to clean energy sources and the energy security that brings.

As a firm that is owned by and invests on behalf of superannuation funds, I wanted to highlight how such funds and fund managers working together are well placed to tackle longer-term systemic risks, such as climate change and social inequality, and indeed take advantage of the opportunities they present as well.

I also want to talk about how the long-term thinking of super funds make us the natural partners of governments like South Australia, who are looking to unlock capital for state-building or indeed nation-building projects.

Nation-building projects

It does seem puzzling to me, however, that in the recent debate about nation-building in Australia, there has been in some quarters a kneejerk response that suggests that super funds or long-term investors have no place in supporting such projects.

The argument seems to be that you can either support nation-building endeavours, like the energy transition or social housing. Or you can generate returns. But you can't do both.

To me, that is a false debate. And simply not accurate.

As long-term investors in assets that communities rely on every day, including renewable energy generation, we are always interested in partnering with governments on projects that can help maximise long-term returns to industry super fund members.

So to speak as plainly as I can, funds are not going to make investments that don't make sense financially or are not in the best financial interests of members.

We all have fiduciary obligations to investors.

There are plenty of investable opportunities already that help accelerate the energy transition, for example, and can also help generate returns for investors. And as collaborations with governments increase, and policy-settings become clearer and more reliable, I'm confident that the number and scale of great long term investment opportunities in this area will continue to increase.

And given the amount of capital required for such a transition it suggests to me that investors with long time horizons, like superannuation funds, are the natural partners of government.

For example, the International Energy Agency says that by 2030, close to US$1 trillion will be needed annually for clean energy infrastructure.

This is likely to spur the creation and adoption of new technologies, products and modes of transport, which in turn create new business and investment opportunities.

At IFM we are certainly active in this space, building our skills, resources and networks to keep pace with developments, and deploying substantial capital into these new energy opportunities.

We do this because we believe they can help deliver long-term returns to our investors, and indeed reduce long term risks. I'll return to this risk point later.

IFM and the energy transition

Across our infrastructure portfolio, we have a pipeline of renewable projects that now exceeds 10GW.

We have also overseen a sevenfold increase in renewable energy generation capacity at our assets - since 2020, from 100MW to 700MW .

Across our airports in Australia, we have significant behind-the-meter renewable energy generation capacity.

Given we are here in South Australia, let me talk a bit about what is happening at Adelaide Airport, one of our investments.

There is already a large rooftop solar installation in place, which has been materially reducing the airport's carbon footprint for over 5 years. Interestingly, at the time of installation in 2016, it was the largest single rooftop solar array in Australia.

The airport is also working on the design for a new 2MW solar installation project, while a $4 million project to install more energy efficient lighting in the terminal and car park is being implemented now.

The airport is also working closely with the government here in South Australia, as well as industry and airline partners to progress sustainable aviation fuels locally.

This includes both exploring production opportunities and supporting sustainable aviation fuel flights.

I am sure the work that is being done here in South Australia will be helpful for us at other IFM assets here in Australia and globally.

Alongside being able to take what we learn at one asset and apply it another, the scale of our portfolio also brings other benefits. In Australia we have set up a renewable energy Power Purchasing Agreement program across many of our Australian assets.

We worked on the PPA in collaboration with another asset owner to facilitate the supply of more than 400Gwh of renewable energy every year by 2025. It will help many of these assets achieve net zero earlier than they had planned.

For example, Melbourne and Brisbane Airports have announced in the last few months that this program will help them become fully powered by renewable energy by 2025.

And critically, all of these initiatives are accretive to the financial performance of these assets.

We are also actively investing in the new assets that will help drive the energy transition.

One of our funds has recently invested in ERG – one of the largest independent green power producers and developers in Europe. ERG has an established portfolio of 2.5GW and a high visibility near term pipeline of a further 3.5GW of renewable power generation.

As I said earlier, the fossil fuel dependence of Europe is all too apparent at the moment, and businesses like ERG will be critical to the continent building both energy security and achieving net zero emissions.

Another of our assets, Nala Renewables is targeting 4GW of renewable capacity across wind, solar and battery storage by 2025, and is building a 25MW battery in Belgium and developing four similar projects in Long Island New York.

Together, ERG and Nala have more than 150 assets secured across 15 countries.

I could go on talking about our portfolio for a while. Another investment I love to talk about is where one of our businesses – Swift Current Energy – is helping the city of Chicago achieve its target of 100% renewable energy for all its facilities and operations by 2025. Swift Current is developing a 593 MW solar installation – one of the largest solar projects in Illinois to date.

But I think you've probably got the idea. This is a large and rapidly growing part of our investment activity globally.

Green Hydrogen

Now we heard yesterday and today about the significant leadership position South Australia is taking when it comes to investment in renewable energy projects and battery storage.

South Australia was the first State to invest in a big battery – which is now being replicated by other States.

South Australia's hydrogen plan is also putting the state ahead of the curve.

Alongside the potential it has to create jobs, and unlock additional renewable investment, we see green hydrogen – while in its infancy – as a dominant theme for the future.

Globally, there are strong national and EU policies aimed at developing reliable sources of green hydrogen as a low carbon fuel alternative, and in the United States green hydrogen projects also featured strongly in the actions recommended by the recent US Inflation Reduction Act.

Heavy industrial activities, like steel and cement, are not easy to electrify, hence green hydrogen is seen as a viable, clean alternative to their current reliance on fossil fuels. Key chemical industries are reliant on natural gas as feedstock, which may be able to be replaced by hydrogen.

Green hydrogen-related infrastructure, including production, transport and storage, is potentially a significant investment opportunity as hydrogen can play a pivotal role in the NetZero transition of industrialised economies such as Germany, the UK, Italy, Japan, Korea, Singapore and the US.

Not all of these countries can produce cheap, reliable green hydrogen, so many will rely on imports from "friend-shoring" countries to help ensure energy security.

This suggests export projects in geographies such as Canada, US and Australia are well placed to benefit from the green hydrogen revolution.

I can't resist one more IFM portfolio company example – earlier this year through one of our businesses we made an investment in Bear Head Energy – an early-stage development project that seeks to convert renewable energy into green hydrogen.

The goal is to build a large-scale green hydrogen and ammonia production, distribution, and export hub in Atlantic Canada with a target hydrogen electrolyzer capacity of more than 2GW to supply markets such as Europe and the US East Coast.

If the green ammonia generated from the contemplated phase 1 project is used as a marine fuel, for example, it is estimated that would result in around 800,000 metric tons of CO_2e being avoided annually through the displacement of traditional fuel in the market.

The equivalent of taking more than 172,000 cars off the road.

Transitioning assets

Investing in new clean energy assets and the infrastructure that supports them such as enhancements to the grid is important and a rich source of opportunities for us.

But from a long-term investing perspective, I also believe we need to drive capital into the existing stock of essential infrastructure assets to accelerate and support our transition to this new clean economy, and to ensure that this transition is as smooth and efficient as possible.

If we don't manage this part of the transition effectively, and it becomes disorderly and chaotic, we will see energy security and affordability suffer, the economy and markets suffer, with an impact on investment returns, and likely an overall slowing of the energy transition as well.

Because of the importance of getting this transition of existing assets right, my view is that long term investors should be willing, and indeed keen, to buy assets with significant emission profiles, investing in those assets to support a transition plan to get those emissions down.

In the case of infrastructure, by definition these are essential services. We cannot simply turn them off today.

If a district heating business in Poland runs out of power in the winter, millions of people potentially freeze. It's crucial we recognise the urgency of the transition task, but equally we must plan and be organised about how we achieve it.

So our job is to deliver expertise and capital into those businesses to find a way to reduce emissions without jeopardising their critical service provision. All of course with the ultimate objective of delivering a great return to our investors.

One of the challenges we face as an investment manager is that in the rush to appear at the leading edge on ESG, many investors are designing their policies to screen out assets with emissions.

Investors, of course, make their own decisions.

But driving the emissions of individual portfolios down by selling emission-heavy assets won't have a systemic impact.

And taken too far, it risks starving the businesses we most need to transition of the capital they need to do so.

It's also the case that in many situations it's these businesses that have the skills, industry knowledge and resources to support the transition most efficiently and effectively. Our midstream pipeline business in the US, Buckeye, is able to use its understanding of the energy industry and its full suite of skills and resources across major project execution to rapidly scale its own clean energy business.

Now of course there's a point where if a business is unwilling to engage then selling out is the appropriate thing to do – if you can't influence change then managing your portfolio risk is the only consideration left.

But this should be a last resort.

Systemic Risks

I have spoken about some of the trends we are seeing globally and given some examples of the work we are doing across our individual assets. This portfolio activity at an asset level is important and makes a difference.

But I want to conclude my remarks by talking more broadly about the systemic risks we are facing here in Australia and globally, and are likely to face in the years and decades ahead.

We continue to understand more about the environmental and social systems around us, and how they are changing. And it is becoming clearer that as a global community we are not making the progress we need to regarding climate change at the pace we need to.

It is also becoming clear that to deliver strong long-term returns for our beneficiaries, and the generations of beneficiaries after them to whom we also owe a fiduciary responsibility, investors like ourselves need to be working to strengthen the system itself, not just individual assets within it.

This means extending our analysis beyond the footprint of the specific investments we make and understanding how our investment activity and the activity of our assets might influence the health of the economic, environmental and social system around us.

We need to orient our activity to strive for positive impact on this system.

We have to do this mindful of our ability and opportunity to produce positive financial outcomes that our scale and scope can deliver, and again, critically, this is entirely consistent with fiduciary duty, and I'd even argue is required by fiduciary duty.

Healthy long term investment returns are dependent on healthy environmental and social systems, now and in the future.

The quality of investment returns in ten and twenty years' time depends on the quality of the system in ten and twenty years' time.

And also, by their nature superannuation and pension funds invest on an intergenerational basis and have a duty of impartiality to treat members of different generations fairly.

So again, we have a duty to think about the impact we are having now on the investment returns of the future. Superannuation funds are investing for decades for their members – a horizon that comfortably encompasses the horizon for the systemic risks we are facing. And most large pension funds can now be considered universal owners – institutional investors that are sufficiently diversified in their investment allocations that they effectively own a slice of the whole economy.

The implications of this are that they can't avoid the effect of externalities, for example. They might not own a company producing the externality, but they are still very likely to own the effect of the externality across their portfolio.

You can't stock pick your way out of systemic risks like climate change. And risks like this are impossible to diversify away from.

They will and are impacting our entire economy. And these impacts will compound such that future market returns will deteriorate and many of the superannuation members we are investing for will have much lower retirement incomes as a result.

A couple months ago, the Thinking Ahead Institute at Willis Towers Watson analysed the financial impacts of climate change and concluded that institutional investors "could see a 50-60% downside to existing financial assets in a business-as-usual scenario where climate risks are not addressed."

Losses of that order applied to the 75 trillion dollars of global pension assets is an awful lot of value destroyed, and a lot of pensions not paid. That is a lot of people not getting the retirement they were expecting or deserve.

So the financial case to act with urgency is clear. Every fiduciary focused on the best financial interests of their beneficiaries needs to do their part in the global push to address climate risk.

Almost by definition, the impact of a single investor or investment manager on these systemic risks is tiny. But if everyone says "my part in this is small, I can continue with business-as-usual" we will collectively fail.

So we must not only take all reasonable steps within our own perimeter of influence and control, we must organise ourselves to collaborate much more strongly to influence systemic risks.

The good news is that large long term investors like superannuation funds and pension funds globally should be well suited to such collaboration.

They have a very simple, clear purpose in common – to protect and grow long term retirement savings for everyday people. And as profit-to-member businesses (by and large) they are focused on generating great absolute outcomes for their beneficiaries – the nurses, construction workers, teachers and other workers that they are investing on behalf of.

If they can improve these outcomes by working with others, they are highly motivated to do so. Its a lot harder in practice for profit-to-shareholder businesses to choose to collaborate with their peers – who are by definition also their competitors, potentially weakening the shareholder outcome.

Government

Governments must also play their part in addressing systemic issues. The sheer scale of the challenge ahead cannot be delivered by public sector finance alone of course – we are talking about trillions of dollars a year globally, and hundreds of billions a year in Australia, for decades to come.

But the capital markets powered by long term investors have the scale and reach to do amazing things. What this market system needs though is a clear, reliable vision and well-defined regulations and incentive structures. The more governments can provide this, the more confidence long term investors will have, and the more capital will flow.

We are seeing that here in South Australia and in other Australian states. And we are also seeing significant commitments and action globally to tackle climate change. There are reasons to be optimistic.

Conclusion

So to finish, I believe that superannuation funds in Australia, and indeed pension funds globally, are well placed to support the energy transition.

- These funds have the scale and, through organisations like IFM, access to the skills and experience to make an enormous contribution.
- The flow of opportunities will provide strong returns for the nurses, teachers, construction workers, hospitality workers and the rest of the population that relies on superannuation for a dignified retirement
- Investing in these opportunities will also not only generate returns from the projects themselves, but also help contribute to a much healthier, lower risk system in the future, helping to create sustainable long term returns for our members, not to mention a stronger, healthier economy and society more broadly, with more jobs and stronger wellbeing.

I also believe that superannuation funds are well placed to work with and alongside governments – like South Australia - to help deliver this transition.

Superannuation funds, like democratic governments, represent the community at large. For funds like industry superannuation funds, all the profits flow to the members who make up that community. This means superannuation is an ideal, trusted and aligned long term partner for governments in embarking on this challenging long term journey. But quite possibly the most important journey any of us here today will ever make.

Thank you so much for having me.

It's been a pleasure to be part of this conference

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