March 21, 2014

Dear clients and colleagues,

Infrastructure is becoming a very popular asset class on its own. Investors are attracted to the long-term cash flow and lower volatility of the asset, offset by much reduced liquidity.

One of the investment themes in our portfolio is Infrastructure. Developed countries are having to replace aging infrastructure, emerging countries are still in the early stage of urbanization and infrastructure spending is also a favorite policy tool of worldwide governments to counter economic slowdowns (trillions of dollars have been pledged over the next few years). All this results in the largest global build-out in history.

What may surprise many is that numerous infrastructure-related companies are publicly traded, from airports like Zurich or Frankfurt, to highways, ports, etc. The MSCI World small cap index weight for infrastructures is around 6% and comprises over 300 companies.

Many companies in our portfolio directly benefit from this theme: Citic Telecom International (telecom interoperator, based in HK), Nabtesco (construction and transportation equipment, Japan), Outotec (construction and engineering, Finland), MasTec (infrastructure construction, US), Eagle Materials (cement, construction materials, US), Astaldi (general contractor and concession, Italy). And many more indirectly.

This week we shall profile Astaldi, a name added to the portfolio in the last year. The company may sound familiar as it signed a C$1bn contract last December for the construction of Muskrat Falls Hydro project in Labrador. It also signed a contract to extend the I-95 in Florida last year.

Astaldi (AST IM €6.90)
http://www.astaldi.com/home/

History and Business Overview
Astaldi was set up in the 1920s by engineer Sante Astaldi. The company worked mainly in Italy and Africa until the Second World War. Between the late 1950s and the 1970s, Astaldi increased in size and complexity and went global. As Italy experienced its economic boom in the 1960s, the company constructed the Autostrade del Sole (A1), the first major highway in Europe, and the Rome-Florence Fast Railway (1976), the first high-speed railway line in Europe. The company continued to expand in the 1980s and started doing work in the United States on motorways such as the Orlando beltway. It also entered the concessions sector, building and managing car parks and water projects in Honduras. The company went public on the Milan Stock Exchange in June 2002.

Today, Astaldi is a leading Italian general contractor with €13bn in backlog at the end of 2013 and more than €2.5bn in revenues. The company has more than 100 sites in operation in 18 different countries. It operates in six macro areas: Italy, Central Europe + Turkey, the Middle East, Maghreb, Latin America and North America. Transport infrastructure is its key focus (80% of revenues). The company is also active in water and renewable energy (10% of revenues) and civil and industrial building. Astaldi generated 39% of its revenues in Italy.

Target Market

The company is focused on the transportation, water and energy, civil and industrial buildings sectors, and those sectors will see in excess of $200bn in spending in 2014 alone in the markets where Astaldi operates. As discussed in our introduction, infrastructure spending is in a secular uptrend.

Management

The Astaldi family still controls 52.5% of the company. The Board and management have been in place since the IPO.

Market data

Market Cap €0.7bn, p/e (12/2013) 8.0x, Sales: €2.5bn, ev/ebitda (FY13) 4.9x, dividend yield 2.9%, net debt/ebitda 2.7x, ROIC 12.3%

Competition

Astaldi competitors are international construction companies with an integrated dual construction-concession model such as OHL, Bouygues, Skanska, ACS and Salini-Impregilo. Astaldi is smaller than these competitors. The market is very fragmented.

Growth strategy

- The company has a record pipeline of new projects (construction and concessions)
- The group will grow in Asia (only 3% of revenues)

Competitive advantages

- Excellent track record: over 400 major projects completed around the world.
- Core expertise in tunneling (underground), excavating and bridge construction.
- Integrated quality, environment and safety management system, ISO 9001, ISO 14001, OHSAS 18001.
- Solid market positions and strong visibility provided by sizable backlog.
- High profitability and resilient margins.
- Diversification in concessions.
- Family ownership.

Risks

- The company has major projects in Turkey and Venezuela. Political troubles could postpone the delivery of projects and additional costs for Astaldi.
- Fixed price contracts.
- Small size in an international industry which is highly cyclical.
- Dependent on public sector spending.

Catalysts for value creation

Most of the group's concessions are still in the construction or in the financing phase with only a few operational. Today, concessions are around €70 million in revenues (2% of total revenues) and €40 million in Ebitda (10% of total ebitda).

Concessions should generate around 20% of revenues in 2017. New concessions include Metro 5 in Italy (2013), Tuscany hospitals (2014), the 3rd Bosporus Bridge in Turkey (2015), the Istanbul-Izmir highway in Turkey (2015) and Metro 4 in Italy (2017).

These concessions will increase the Group's profitability, cash flow generated will reduce the debt and these assets will be extremely attractive to Pension Funds and Endowments at a significant premium to carrying costs.

We often mention to our investors that we can find exposure to emerging markets via companies solidly established in less risky markets and traded on developed markets. This is the case with this week's profiled company, Astaldi.

Have a nice weekend.

The Global Alpha Team