Elston Australian Large Companies (Income Series) Portfolio Update: Purchase of APA Group (ASX: APA)

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Across the Australian Equity component of investor portfolios, we have bought APA Group (ASX: APA). APA owns and operates many energy infrastructure assets across Australia.

APA is the leading gas pipeline owner and operator in Australia with a near monopoly position. It's pipelines play a critical role in transporting gas around the country for household use, industrial use, electricity generation and for LNG export. In addition to this it owns and operates several smaller gas & renewable electricity generation assets and a number of electricity transmission lines. Recently it acquired the Pilbara Energy Systems business from Alinta Energy which generates and transmits electricity for the miners based in the Pilbara.

We are attracted to APA for the following reasons:

- Monopolistic market position
- Well run business that has not overplayed their strong market position – this provides a sustainable long term base for earnings
- Stable, inflation linked, high margin revenues

APA has three key levers for value creation that we would like to highlight:

- APA has recent invested in capacity increases for the East Coast Grid. There are underutilised assets combined with an increasing need for gas to flow through APA's pipelines from Queensland to the southern states where government policy has led to underinvestment and falling supply
- Prospects for significant electricity demand growth in the Pilbara as miners look to decarbonise their operations by shifting from diesel fueled vehicles and trains to battery electric and hydrogen powered. The increased volumes will benefit their transmission assets and allow for further buildout of renewables in the region. A key attraction of this unique market is that it faces large, sophisticated customers in a sparsely populated area meaning it is insulated from the red tape created by a lot of the politics around energy
- APA's recently acquired Basslink transmission line was problematic for its previous owners and bought out of administration for significantly less than it cost to build. Basslink's previous owners struggled to make enough to look after the asset properly which led to outages and significantly higher Tasmanian Electricity Prices. APA is going through the process of moving this asset to a heavy regulation regime which will allow for more pricing stability, sustainable operations of the asset & returns

We have funded the purchase of APA via the remaining proceeds from the sale of Virgin Money UK (ASX: VUK). Virgin Money UK is a UK bank serving both retail and commercial customers.

As per our last email, VUK is currently subject to a preliminary takeover offer from Nationwide Building Society (Nationwide) at £2.20 per share which is approximately AU$4.20. VUK trades at a mid-single digit spread to the takeover offer and we believe it is

unlikely VUK sees a higher offer. In addition to this there are pressures to give building society members a vote on whether the transaction should go ahead which may create uncertainty around the transaction proceeding.