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Risk-adjusted TSR Overview

Spark Infrastructure uses risk-adjusted excess Total Shareholder Return (TSR), relative to the S&P/ASX 200, to determine the percentage of an executive's Long Term Incentive (LTI) that will vest. The measure used to determine risk-adjusted excess TSR used is Jensen's alpha (α). Alpha incorporates an adjustment for the relative risk of the security, in the same way that investment markets do.

Investors know that risk and return are related to each other. In general, if risk is high, then there is a requirement for higher returns, and vice versa.

Investors in Spark securities generally want stable returns and lower than average risk. Ideally, Spark's long-term performance would be benchmarked against a group of similar companies, with equivalent risk and return expectations. However, because there are too few of these to form a viable peer group, a broader group of companies is required.

The S&P/ASX 200 Index companies were chosen because the S&P/ASX 200 Index is a well-established benchmark in relation to Australian securities. However, it introduces many companies with significantly higher systemic risk than Spark. In fact, Spark is ranked below the 10th percentile within the S&P/ASX 200, based on beta (β), the measure of systemic risk used to calculate α .

There are many factors influencing returns, including systemic risk and non-systemic risk, like management performance. If we can adjust the returns for the relative *systemic* risk, then the variability in the adjusted returns should be more strongly related to management performance.

TSR (share price appreciation + dividends), though commonly used to benchmark long-term performance, fails to take into account the riskiness of an investment in a particular company. Ranking companies by their risk-adjusted return, over a specific period, provides a comparison that more closely reflects how investment decisions are actually made. That is, an investor will have a requirement for a company return that is informed by the perceived risk associated with the company.

Spark independent adviser calculates risk-adjusted excess returns using α . The calculation incorporates:

- A measure of risk called beta (β), a calculated figure based on the relative variability in actual return data for Spark and companies in the S&P/ASX 200
- The risk free rate, based on the Australian government bond yield
- Average S&P/ASX 200 returns

As with traditional measures of TSR, all data used in the calculations are public and transparent. No discretion or subjective judgement is applied.

Ranking Spark against a peer group based on α provides a quantitative approach to determine LTI vesting outcomes. The outcome is not determined using judgement or discretion and is entirely independent of management influence.

Guerdon Associates Pty Ltd ABN 67 112 483 940

www.guerdonassociates.com

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