

NEWS

DIVINING AN OPPORTUNITY IN THE WATER CRISIS

As demand for water grows in inverse proportion to its availability, investing in water sector companies is a win-win



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Two words frequently seen in relation to water these days are 'vital' and 'crisis'. Vital because without it human life cannot function and crisis because water resources on earth are growing increasingly scarce. Ten years ago, the proportion of people living in countries chronically short of water stood at 8%. By 2050, this will have risen to 45%.

This alarming projection is due to a simple supply/demand imbalance: while the amount of water on the planet is finite, use of it is rising exponentially.

The soaring demand for water is due to a combination of population growth, changing diets and improved standards of living. As people get richer, so their water usage rises. Flushing toilets, dishwashers and washing machines, for example, all use far more water than their primitive alternatives.

By the time you get as 'developed' as the US, water usage per capita is extreme. For example, the average American draws 215 cubic metres a year for domestic use while the average Malian draws four cubic metres a year. Swimming pools and golf courses are thirsty luxuries.

Such imbalances present opportunities in terms of emerging industries to provide solutions to the problems, and as such represent an interesting long-term investment opportunity.

The water sector is appealing to investors because it is growing fast but generally is not as volatile as, say, the alternative energy sector. It is relatively sparsely followed by larger broking houses and so tends to be understood only by specialist investors. The sector is fairly fragmented, and we believe consolidation is likely as large companies snap up assets in those companies providing solutions to the growing problem of water shortages.

Solutions fall into several sub-sectors, the first being demand control. If people and industry know and understand how much water they are using, they will



Water: Usage is much more extreme in the developed world than it is in less developed countries

set about finding ways to be more efficient and preserve it better. Thus, advanced water metering is a key investment theme for us.

Upgrading meters is a \$6.5 billion (£4.4 billion) opportunity in the US alone. Companies such as Itron and Badger Meter, both world leaders in this area, are using automated meter reading technology to enable more efficient water usage.

We also invest in Geberit, the Swiss company that pioneered the dual flush loo and a range of other sanitary ware that dramatically improves domestic water efficiency. Also on the theme of preservation of supply, we like Insituform, a US water and sewer pipeline repair company which uses 'cured in place' technology rather than 'dig and replace'. In the US alone it is estimated that between \$30 billion and \$40 billion needs to be

spent annually on regenerating water infrastructure. With technologies such as Insituform, you will see fewer roads being torn up by water companies while they replace ageing infrastructure.

Another important area of development is increasing supply to those parts of the world where it is scarce. Waterborne diseases remain the biggest cause of childhood deaths. Two thirds of people in rural China currently have no access to clean drinking water. We therefore hold Sound Global (formerly Epure), a company which is rolling out water treatment facilities across China. Not only is it providing a vital function, but it is one of the best performing stocks in our portfolio, up over 60% since we bought it a year ago.

Desalination is an appealing option given the fact that over 97% of the earth's water is salty, but has been prohibitively expensive and energy intensive. Now Spain, the driest country in Europe, is using desalinated sea water to irrigate crops in certain areas.

A company in our portfolio, Flowserve, recently acquired a leading desalination business to increase its water infrastructure capabilities, while Abengoa, a Spanish conglomerate that is investing in a number of renewable energy technologies, is pursuing the Holy Grail of solar-driven desalination. Using the sun's energy to take the salt out of water would literally be a life saver in the hottest parts of the world.

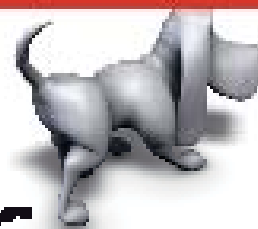
The outlook for the water sector remains positive. Climate change is still at the top of the political agenda and with droughts and flooding becoming an all too regular occurrence worldwide, the argument of whether water is a valuable resource or not and how we use and reuse it was won some time ago.

Companies providing solutions to this pressing problem represent the very best sort of long-term investment: good for the planet and good financially.

Clare Brook co-manages WHEB's Sustainability Fund with Nicola Donnelly

SOURCES: UNEP; The Economist May 22 - 28, 2010; WHEB research

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