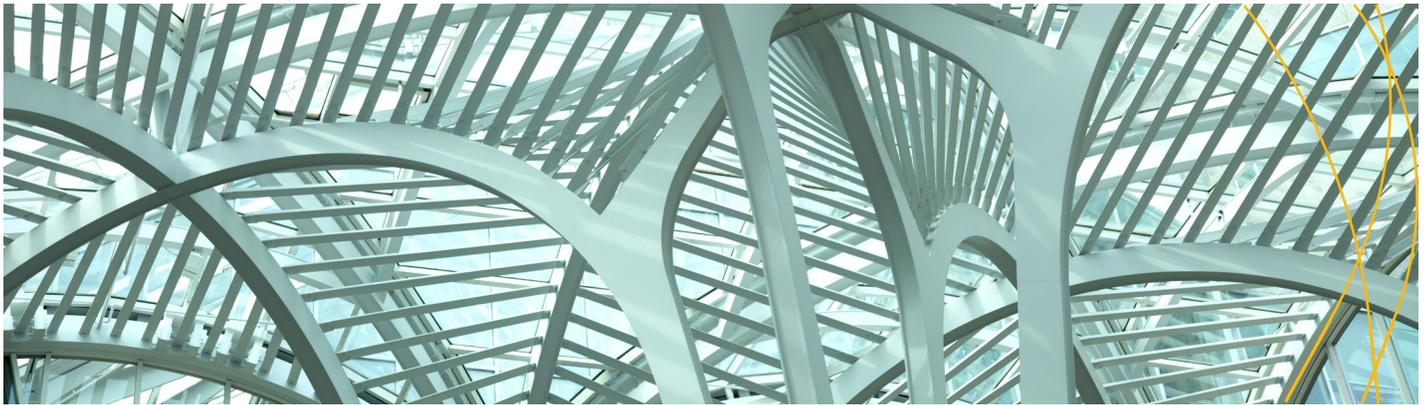


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On September 10, 2019, James Black, Vice President, Canadian Equities led a fire-side chat with Bruce Flatt, Chief Executive Officer at Brookfield Asset Management for the latest event in our Beutel Goodman Speaker Series. Bruce joined Brookfield in 1990 and was named CEO in 2002. Under his leadership, the company has developed a global operating presence in over 30 countries, giving him unique insight into many of the issues facing the world today.

Brookfield Asset Management, a company with over US\$350 billion in assets under management and investments in real estate, infrastructure, renewable power and private equity, has been an investment in our Canadian Equity strategies for several years. What follows is an edited transcript of a highly insightful exchange that covers everything from the origins of the company to recent acquisitions to Bruce's outlook for the global economy.

In Conversation with Bruce Flatt



James Black: Thanks very much and welcome everybody. We are thrilled to have you join us today, Bruce. Full disclosure: in addition to Beutel Goodman having owned the stock since 2014, I was an employee at Brookfield Asset Management for about two and a half years, around 12 years ago. Brookfield has been a substantial contributor to the investment performance of our funds, and most importantly, to the capital appreciation of clients' portfolios. So Bruce, on behalf of all of us, thank you.

I was hoping we could start by stepping back in history a bit and talking about the origins of Brookfield to help people who are less familiar frame how the company has evolved from an owner of assets across a number of asset classes to both an owner and an asset manager.

Bruce Flatt: Thanks James, and I'll just start off by saying thank you everyone for coming. I am proud that Beutel Goodman is an investor in Brookfield.

As to the origins of Brookfield, here's what I would start with: sometimes you get lucky in business. One of our people came upon a very interesting idea 25 years ago, and we invested into all of the things we do today at that point in time. At that time we were also invested in a lot of other assets, but we disposed of them because they were commodity-related, highly volatile businesses and although they tended to do really well if you picked the right timing, they did poorly over long cycles. If you invested in them on a cost-of-capital basis, it was very tough to make a return over a long period of time as a permanent investor.

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Instead, we decided to focus on core businesses that we still have today: real estate, infrastructure, renewable power and our industrial business, which we call our private equity business. At that time, we concluded that the only legitimate way that we could expand the business and get to the scale we needed was to find capital to invest beside us. We thought about different ways we could do this and came upon the idea that if we could provide these products to institutional clients, they would place them into their portfolios and we could earn them a reasonable return. At that point in time, some competing funds were investing directly in real estate, but nobody did infrastructure or renewables, and private equity was just starting out as an allocation in U.S. plans via some of the big private equity players.

I'd say this is where luck played into it: over the last 25 years, institutional pools of money grew exponentially, while interest rates declined from 8.5%-9% to 1-2%. This combination of events meant that our first institutional investors did very well with us and with others who provided the same types of alternative products. It gave them the confidence to continue to invest, but more importantly—and this is the luck—some of the institutional funds are so large now that they almost have no other choice than to put money into alternatives. When you get to a point where you can't roll a 2% coupon over in a fund; when those coupons are now negative, you just can't legitimately invest in fixed income when rates are negative. Every Japanese client we have, every Korean client we have, every European client we have is in this situation.

We experienced this for 10 years in Japan and it's starting in Europe today, so the wall of money is pushing somewhere else. I'm not a macro-economist and I don't try to be, but I think the enormous pressure on the U.S. Treasury at 30 years and 10 years is because of these institutional clients with massive rollovers of capital and nowhere else to go. There really are only three places in the world where all of that money can go: equity markets, alternatives, and U.S. treasuries. U.S. treasuries are at least positive today, but it's scary to buy them at 1%—at best you're going to earn 1% for 30 years, and they [rates] might go up to 2% and you'd lose a lot of money.

We got really lucky. We executed and took a business that was largely investing for our own balance sheet—and we still do that—but now we're investing on behalf of an enormous client base. With every transaction, about 20% of the money is sourced from one of the discretionary balance sheets we have control over and 80% from institutional clients. That has been a big change in the business and we've had a great ride. We've compounded at 17%, 18% for 20 years. But I really think the wall of money is only starting.

James Black: In addition to the private funds and the institutional clients, you have a second source of third-party capital—your listed investments in your four major asset category partners: Brookfield Property Partners, Brookfield Infrastructure Partners, Brookfield Renewable Energy Partners, and Brookfield Business Partners, your private equity listed fund. What roles do they fill in your asset-management strategy?

Bruce Flatt: Fifteen to twenty years ago, we thought what we needed was broad access to liquidity, because the things we buy, own, build and run have enormous asset values. The one tower at Brookfield Place – which we are looking out at—alone, for instance, is worth \$1.6 billion to \$1.7 billion. We looked at master limited partnerships in the United States and thought, "How can we adapt those models to benefit our investors?"

We created all four of our partnerships listed on the New York and Toronto stock exchanges through spin outs. Brookfield Asset Management kept 30%-40% and gave the balance of the shares of the spinoffs to existing shareholders, thus creating the permanent partnerships that invest beside our institutional clients. The way we think of them is we provide our institutional clients real estate expertise,

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infrastructure expertise, power expertise, or private equity expertise and we provide the same thing to retail investors in the stock market by having these listed vehicles. We have discretion over the investments just like we have with our institutional clients, and it just gives us a different source of capital, which allows us to do things that most other investment managers we compete with can't do. These permanent capital vehicles give us access to the capital markets and they help us build the business significantly. They participate in exactly the same areas our institutional clients participate in.

James Black: Can you talk a bit about Brookfield's investment strategy?

Bruce Flatt: Our view is that capital in a business should either have a strategic advantage when invested or it should be given back to shareholders and somebody else should take that capital and invest it where there is strategic advantage. We care a lot about capital allocation and organically over the last 25 years, we've come upon three things that give our capital an advantage:

1. Because of our institutional clients, our partnerships and our own balance sheets, we have access to more money than most people in the world, so a \$100-million transaction may have 35 investors who can bid for it; a \$1-billion transaction may have 8; and a \$5-billion transaction may have 3—and once in a while, there may only be 1 or 2 people who can bid for it. That is an enormous advantage, so we try to use that as a strategic advantage and we've gotten to a point where most things we do have a scale.
2. We have people in 30 countries around the world who ensure that when we make mistakes, we can dig our way out. We know how to get money into and out of a country. We know the rule of law and whether or not a nation respects capital. We only go to places that adhere to our strict criteria. Most importantly, we are value investors, and the only way we felt we could continue to be value investors was to be diversified not just across industries but also across countries, because countries don't all act the same way at the same time. This allows us to move money to the places that require capital, and therefore the large sums of money on the margin are always being allocated to these value-based places.
3. The value of having strategic partners is the 100,000 people who work for Brookfield. They work for those partnerships; they stay within those businesses; they are permanent to us. This gives us an enormous differentiation of the capital that we have.

James Black: What we find attractive about Brookfield as an investment is that in many ways, your approach is value-based, long-term—you buy stuff that in most cases you can own forever. That's very much how we look at investments. We have a minimum three-year time horizon and we want a 15% annual return over that time horizon with new investments. Brookfield has a similar approach, depending on the asset class, but would look for a mid-double-digit return on assets over time. So this is a very easy company for us to own because we understand the basis on which the investment decisions are being made. I'd love to hear a couple of war stories when it comes to investments. Maybe one that worked out better than you thought it would and one that didn't, and what you took away from those.

Bruce Flatt: Well James, in a record that is pretty good over a long period of time, I can tell you that we've made a lot of mistakes. Maybe the most important thing we've found about making mistakes is never bet the franchise on anything, and if you do bet, be very aware of the mistakes you make and learn from them instead of letting them destroy the franchise.

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The biggest thing for us is going into new industries or new businesses or new countries – and I'll say this about Canadian companies – about 30 years ago I started going to the U.S. and trying to build the business. The horror stories you'd hear about Canadian companies going to the United States and getting their feet blown off was just tragic. It destroyed a lot of management teams' incentive to build their businesses in the U.S. We did it slowly and I think that was really important because if you blow your feet off in an investment, even if it doesn't harm the company irreparably financially, what it does is take away the confidence of the management team or the board, and it takes years or decades to reverse that in a corporate culture. So for us it's really important that we don't make any really large mistakes, although we have made lots of small ones.

One mistake that may be relevant to some of you is investing in foreign places, even if that is just buying stocks outside of your native currency. Often people don't think about currency; they think they're a genius to have bought something that has gone up 40%, until they figure out that 40% after a 40%-decline in the currency is actually a loss.

We had been in Brazil for a long time, just due to some of the history of the company. We sold a lot of assets back in 2005-2007, but then the financial crisis arrived there and we doubled down, tripled down. We bought some amazing assets—in fact, we bought a lot of these assets, I would say, at 25 cents on the dollar. But the currency declines took an amazing turn and made it just okay. I'm not sure that the risk we took was compensated by the return we got after the currency loss. We kept investing and kept doubling down, which I would say is an important tenet of value investing, and because of that some of the returns we had were stunning. So we did fine overall, but the point is, when investing in international markets, paying attention to currency is really important.

By and large, we hedge – even though it costs us – in most currencies back to U.S. dollar if we can. The sums of money we deal in are very large and posting collateral with currency hedging is in itself risky, so most people don't pay attention to that. We spend a lot of time thinking about it and we've learned a lot over the years through mistakes in that area.

James Black: Building on that, one thing that Brookfield has been able to do very well is take advantage of dislocations at different points in time and make transformational deals that either establish you in a new asset class or help you build critical mass. A couple that spring to mind are the World Financial Centre in the early nineties and Babcock & Brown post-financial crisis on the infrastructure side. Do you think we might see that kind of dislocation again, where Brookfield can step into the void?

Bruce Flatt: Our view is always informed by what we see within our business. Overall, we see nothing that really says there is going to be a total meltdown in the economic situation of any country, particularly in the United States, which continues to do pretty well even though some people quote technical problems. In general, the global economy is operating quite well.

Despite that, we're worried that we're 11 years into an economic recovery, stock markets are at highs, bond markets are at highs and politics are crazy everywhere. I have the benefit of travelling country to country to talk to our people, and every one of them is focused on their own politics. If you just go through the list it's very worrying, but while we're cautiously investing in more defensive areas than we would have five years ago, it's not because we see anything out there. It's because our business is about ensuring we earn a reasonable return over the long term, and the enormous amounts of money are prepared so that we have capital when others don't. To give you an indication of what we're doing, we have more cash on the balance

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sheet than we ever have before and more capital available for institutional clients than ever before. We also bought Oaktree, which is a credit manager, and we partnered with the founders of it because we think at some point in time our balance sheet and relationships, combined with the capital behind their franchise, will allow us to do extremely well coming out of a market downturn.

James Black: Culture in successful companies is extremely important, and Brookfield has always had a culture of ownership among its employees, meaningfully investing in the stock of the company alongside shareholders. My view is that this differentiates you from other asset managers where staff is more transitory in nature and more focused on short-term compensation than long-term. As you've grown, how have you been able to retain that same culture that was in place when I was there, and how do you integrate—or not integrate—a new investment, a new asset class like Oaktree, into that culture?

Bruce Flatt: It's more difficult as you get larger for any organization to ensure that the culture stays the same. Despite that, I think the advantages of scale we have in place outweigh the disadvantages that come with the issues of size. We've tried to keep our principles, which are pretty simple: eat your own cooking, be invested alongside everyone that is there, and make money for your clients. The one thing I learned in life is that if you make money for your clients, they will come back for more. If we didn't make money for you, James probably wouldn't have invited me here. We've tried to keep it simple. People can make a lot of money with us over a long period of time if the company does really well.

With respect to Oaktree, it's run by a man named Howard Marks—he's what I'd call a legend in distressed investing. He and Bruce Karsh started the firm 24 years ago and still run it, and their record is exceptional. We visited them and said 'we'd like to take the public out of the company and become your partner'. They looked at me and said 'it's the wrong time to sell, we don't want to sell'. And we said 'no, no. You're not selling, you're actually staying in. If you're selling were not buying.'

So we're buying the public out, in a half cash, half Brookfield Asset Management shares deal, which we very seldom do. So they are coming along with us, the public market investors, and Howard, Bruce and their management team will own 40% of the franchise after the deal closes, so they will remain highly incentivized alongside of us to continue to build the business. Simply stated, our machine behind them should allow them to do more with what they have than what they could do on their own.

James Black: ... and will they give you some interesting client relationships as well that you don't have access to today?

Bruce Flatt: I think it will be additive both ways. We have an amazingly strong franchise for fundraising in the Middle East. For unusual reasons, we invest capital for virtually every sovereign plan and institutional client in every country in the Middle East. And they have, I'm quite sure, fewer relationships there than we have, and therefore we will be very helpful to them in that market. Howard's been raising money in the U.S. for a long time and has an amazing track record, and I think his shine on us will help us a lot. So I think it will be additive both ways, and I think we can help them scale up their business in ways that they otherwise would not be able to do.

James Black: Great, I'd now like to turn it over to our audience, if anyone has something they would like to ask Bruce.

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Q1: Who would you consider your top three competitors?

Bruce Flatt: There are competitors in each of the areas we work within, but the one that is the most similar to us, that we compete with the most, and is formidable from a fundraising and an investment perspective is Blackstone. They are similar in scale to us, we're roughly the same size (our market caps are around \$50 billion), and there are only two major real estate franchises in the world—ours and theirs. Our infrastructure franchise is very significant; theirs is small, but they are growing it.

Another competitor that is private is Global Infrastructure Partners (GIP). Our current infrastructure fund has similar amounts of capital. In renewables, there are a few others; in private equity there are all of the names that you would know. Really I'm amazed that this occurred, but on a scale basis, there are only five to six institutions in the world that raise the amount of capital that we do with institutional clients—KKR & Co., Apollo, Blackstone, ourselves and a few others who are smaller, but those are the biggest names.

Q2: There is a lot of money being raised through private equity, such that some observers would suggest the valuations for private companies in some cases exceed public companies. There are also large companies in the public markets that are arguably largely undervalued in certain sectors. Have you ever looked at taking significant stakes in large public companies that you like, and holding them over long periods of time?

Bruce Flatt: The points you made are right. I think the passive market, indexing, is pushing valuations on things that aren't hot, to the point where they are value stocks. The opportunities, therefore, can be significant in some areas. I also think private-market valuation on technology is a good process to find fundamental value, and I think going public was a great thing for that industry to figure out. I'll leave it at that.

For Brookfield ... we try to stick to things we do well. We stay in areas where we have knowledge of the operations, we buy businesses for value, and we work them really hard. And when you buy a quarter or a third of a company, it's tough. I mean often we're splitting things apart, we're growing the businesses, but we need to invest enormous amounts of capital up front and we believe that's better done privately.

Q3: Bruce, when you see what other people are saying about Brookfield, is there anything you feel is not fully appreciated?

Bruce Flatt: We're always undervalued! So here's what I think, and this isn't specifically the stock and it's not specific to us, but I'm going to use it to make the point, because I think it's relevant for us as well and you can all make your own decision as to whether or not you think this is true. If we're entering a new world of capital where interest rates are in the range of -2% to +2% globally, and the biggest markets are closer to -2% than they are to +2%, then the world is different from the one in which we've lived for a long period of time. And if we're in that world, I don't think stock markets, businesses, entrepreneurs, and investors have yet adjusted their thinking towards what asset values are.

For example, people think that buying a fully let office building in New York City on a 4% yield is a high price. Historically that has been a high price, but if we're in a 1% 30-year bond for the next 15

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years, maybe longer, maybe for an extended period of time, then probably cap rates should be 2%. I think it's just not accepted yet, and it makes sense because it takes time for people to adjust because that 4% used to be 6%, then it was 5%, then 4%, and people don't want to get hit with a snap back. Mr. Powell thought it was going to be X but now it's going to be Y. So I think it just takes time. Like I said earlier, we think valuations of the stock market are at highs but it's also possible they are cheap. If we're at a zero-rate environment, the average P/E multiple is 17x. At 17x, you're earning a pretty good return versus zero. So it's possible.

I think that's one thing we're thinking about more broadly now. When I meet with institutional clients about investing in real assets, they are at close to a zero allocation in their portfolios and they need to go to 50%. This is tens of billions of dollars of capital and this is happening everywhere in the world.

Q4: I think I understand the buy side of value, but what about the other side? How do you get out of some of these assets? What's the process and what has your turnover been the last five to six years?

Bruce Flatt: First, on our current balance sheets sometimes we hold things for a long period of time. For example, the tower at Brookfield Place—we finished building that in 1993 or 1994.

When they are in the funds, we turn assets when it makes sense. The closed-end funds we raise with institutional clients, which have capital from our partnerships as well, are 12-year funds. So we have a pretty long period of time to deal with assets if and when we choose to. Sometimes we sell into the public market; we took two companies public last year. We also took eight companies private.

Our job generally is to buy on a value basis the more time-consuming, complicated assets because of our ability to work them out, clean them up and make them perfect. Then we sell them to institutional clients and they want to own those assets forever. Increasingly, the largest number of exits for us is to our institutional clients. And the biggest issue we have today is when we're selling things, we're trying to maximize the value for the constituents of that fund, but we may have nine clients on the other side who all want the assets because they are all starving to direct-invest. The Canadians are one of the exceptions because they build investment capabilities like Brookfield, but most institutional investors want to be direct investors but they just can't do most of the things that we do. But when we sell things that are more completed, they're participants, particularly in infrastructure and real estate.

Q5: What assumption about relative valuation of the Canadian and U.S. dollar fits into your strategic planning?

Bruce Flatt: So the question is, do I have a view on the Canadian/U.S. dollar relationship. Brookfield Asset Management and our four traded partnerships are U.S. securities. They trade in Canada but they are U.S. balance sheets in U.S. dollars. Our Canadian assets, therefore, just like what we do in every other country, are hedged back to the U.S. dollar, so we don't have a view on the Canadian dollar. We're U.S. investors and we hedge the Canadian dollar, so to the extent that we have assets, they are generally hedged. And it's not because we have a view on the Canadian currency; it just costs very little to hedge with the U.S. and why should we take the risk? That's our thinking—it's just not worth the risk. This is particularly true in our institutional client funds—because we can easily hedge in those funds and we just don't want to take the risk, most everything in our funds is hedged in that way.

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Q6: In some ways from the outside it looks like you have four very different areas you're working in. What are the synergies and the tensions when you're managing those businesses?

Bruce Flatt: The common thread in what we do is that we buy tangible assets. And everything that we invest in generally is backed by an asset that generates cash or an asset that will ultimately turn into generating cash. So we may buy a property that's not full, that we need to find the tenants for and invest in, but ultimately it will generate cash flow. So all the things we have are tangible, and virtually every investment we make—using a 10-year cash flow model, you can produce what your internal rate of return will be.

We have office buildings, which are a little bit different than our power plants, which are a little bit different than our toll-roads—but from an investment perspective, these are “real” assets. We don't bet on new technologies, we don't do bio-tech; we invest in hard, tangible-type things that generate cash.

Jeff Young: Thank you very much, on that we will wrap it up. I'd just like to say thank you to Bruce and James for letting us sit in on your conversation. Thank you for taking questions from us all; it was very interesting and informative. Thank you everyone here for attending today as well.



**Bruce Flatt, CEO
Brookfield Asset Management**

Bruce Flatt is Chief Executive Officer of Brookfield Asset Management, a leading global alternative asset manager with over US\$350 billion in assets under management. Mr. Flatt joined Brookfield in 1990 and became CEO in 2002. Under his leadership, Brookfield has developed a global operating presence in more than 30 countries.



**James Black, Vice President,
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James is a large cap portfolio manager with Beutel Goodman and has equity research responsibilities covering both Canadian and global companies in the Communication Services, Utilities and Financials sectors. James has over 25 years of investment experience. Prior to joining Beutel Goodman in 2007, James worked in private equity at Brookfield Asset Management.

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