Schroder Australian Equities

Quarterly Investment Option Update

31 December 2019

Aim and Strategy

To outperform the S&P/ASX 200 Accumulation Index after fees over the medium to long term by investing in a broad range of companies from Australia and New Zealand. With an established pedigree of investing in Australian equities for over 50 years, the Schroder Australian Equity option is an actively managed core Australian equity portfolio with a focus on investing in quality stocks predominantly in Australia characterised by strong returns on capital with a sustainable competitive advantage. The option draws on Schroders' deep research capabilities, with a long term focus on investing, it is suitable as a core portfolio holding over the medium term to long term.

Investment Option Performance

To view the latest investment performances for each product please visit amp.com.au

Investment Option Overview

Investment Category	Australian Shares
Suggested Investment timeframe	3 - 5 years
Relative risk rating	6 / High
Investment style	Core
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Equities	95%-100%	97.5
Cash	0%-5%	2.5

Sector Allocation	%
Energy	4.1
Materials	28.0
Industrials	9.5
Consumer Discretionary	3.2
Consumer Staples	6.7
Health Care	3.6
Information Technology	1.3
Communication Services	6.2
Utilities	2.0
REITs	2.8
Financial (ex Property Trusts)	30.0
Cash	2.5

Top Holdings	%
BHP Group Ltd	5.4
Commonwealth Bank of Australia	5.1
ANZ Banking Group Ltd.	4.4
Rio Tinto Limited	4.3
Woolworths Group Ltd	4.3
Westpac Banking Corporation	3.7
Telstra Corporation Limited	3.4
National Australia Bank Limited	3.3
South32 Ltd.	3.1
Alumina Limited	2.5

Investment Option Commentary

Virgin Money UK (the new and unimproved CYBG) (Overweight, +67.8%) Wild oscillations in the share price are more reflective of equity market conditions than rapidly changing business fundamentals. Onerous UK financial regulation and penalties imposed on financial businesses have come at great cost to shareholders while concerns over Brexit impact have added to the pain. Although we believe the Virgin Money acquisition was both over-priced and poorly considered, this has been more than reflected in the share price and management are now focused on the task of making acceptable returns in the merged business. Schroders expect market conditions in the UK to remain competitive and returns mediocre, however, with valuation still significantly below book value we still see strong valuation appeal in the business.

Market Commentary

2019 and the decade ended strongly for equity market returns nearly everywhere, and Australia was no exception. Profits were not the fuel, remaining anaemic. There will be no shortage of commentary from brokers and fund managers on the in-depth fundamental analysis and diligent company visits which allowed them to identify exceptional opportunities in Xero, Afterpay, Pro Medicus and a raft of others which allowed investors to double their money in a year. A day does not go by without an email justifying another upward move in the discounted cashflow valuation of these market darlings to ensure price targets remains slightly ahead of rampaging share prices. Slightly less attention will be paid to the role of the central banks in facilitating these extraordinary gains and the type of environment in which the dominant characteristic of market winners is absence of profit. In the period since the global financial crisis the strong performance of companies with zero or negative tangible capital has been pervasive across the globe. Nearly every list of admired or 'quality' businesses is replete with 'platform' or technology companies with virtually no capital employed. Exxon Mobil or Rio Tinto, not so much! The cause of this transition and its sustainability remains a perplexing question. Popular wisdom (and the claims of nearly all senior management with whom Schroders engage) dictates that disruption is a bigger issue than has been the case in the past. Given technology has been a pervasive influence on business for many years (the previous tech bubble was 20 years ago now) and the tangible capital trend has been more confined to the post GFC 'cheap money' era, Schroders remain sceptical of the popular wisdom

Outlook

In 1929, Irving Fisher commented "Stock prices have reached what looks like a permanently high plateau. I do not feel there will be soon if ever a 50 or 60 point break from present levels, such as (bears) have predicted". This forecast, along with approximately 50% of the remaining forecasts made by other economists in the last 100 years, did not go that well. The only honest answer on our expectations for returns in the coming year is we don't know. We can only observe that valuations of equity markets are high by historic standards and extreme in some sectors of the market. Aggressive valuation metrics by historical standards is a state of affairs shared by almost every major asset class on the planet, with monetary intervention the obvious reason. We remain of the view that engineering financial calm will become progressively more difficult as wealth inequality and discontent over political inertia make it more difficult to fool all the people all the time (there is no free lunch in altering the price and/or quantity of money). This does not change the conundrum for most investors; when you have capital to invest you must invest it all in something.

Given this backdrop we continue to believe there are many businesses which offer more than adequate returns, particularly those with more volatile income streams given the somewhat surprising coexistence of a high appetite for stable cashflows alongside rampant speculation in profitless businesses. Given bonds around the world have generally stabilised at very low yields and the mad scientists running central banks are generally backing away from experiments with negative interest rates, we believe the impetus to valuations from lower discount rates and the benefits of borrowing free money to buy back equity are behind us. However, when a world of high asset prices (the numerator) is balanced on a very low discount rate (the denominator), simple maths dictate that we should not be surprised by relatively large moves in both directions. Low volatility is almost by definition artificial and manipulated.

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP0465AU
AMP Flexible Super - Retirement account	AMP1375AU
AMP Flexible Super - Super account	AMP1504AU
CustomSuper	AMP0465AU
Flexible Lifetime - Allocated Pension	AMP0636AU
Flexible Lifetime - Term Pension	AMP0944AU
Flexible Lifetime Investment	AMP0995AU
Flexible Lifetime Investment (Series 2)	AMP1438AU
SignatureSuper	AMP0813AU
SignatureSuper Allocated Pension	AMP1177AU
SignatureSuper Select	AMP0813AU

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