Macquarie Australian Small Companies

Quarterly Investment Option Update

31 March 2020

Aim and Strategy

The Fund aims to outperform the S&P/ASX Small Ordinaries Accumulation Index (Index) over the medium to long term (before fees). It aims to provide capital growth and some income.

The fund follows a quantitative strategy which utilises a risk-controlled approach to identify mis-priced securities. To achieve this, the Fund will utilise a set of systematic and event driven strategies. The systematic strategies aim to capture Quality, Momentum, and Value characteristics that have historically generated reliable excess returns in the Australian market.

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	5+ years
Relative risk rating	7/ Very High
Investment style	Quantitative
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Australian Shares	100%	95.98%
Cash	0%	4.02%

Sector Allocation	%
Energy	1.99
Materials	21.25
Industrials	10.06
Consumer Discretionary	7.55
Consumer Staples	9.43
Health Care	5.15
Financials & Property ex LPTs	6.25
LPTs	9.05
Information Technology	14.53
Telecommunication Services	6.61

Top Holdings	%
Spark New Zealand Ltd	2.39
Saracen Mineral Holdings Limited	2.34
Evolution Mining Limited	2.21
Charter Hall Long WALE REIT	2.11
Oz Minerals Limited	2.09
EML Payments Limited	2.08
Service Stream	1.92
Invocare Limited	1.72
Inghams Group	1.68
Beach Energy Limited	1.66

Portfolio Summary

The Investment Strategy returned -24.73% (gross fees) for the quarter, outperforming the benchmark.

Investment Option Commentary

In general, the Fund benefitted from being overweight in typically defensive sectors such as Gold (e.g Evolution Mining), Telecommunication Services (e.g. Spark New Zealand), and Utilities. It was interesting to note that due to the nature of the downturn, REITs (a typically 'defensive' sector) underperformed on concerns that rents will be cut sharply as tenants are forced to reduce operations during lockdown periods. REIT gearing levels also came under increased focus.

When the COVID-19 pandemic emerged (initially as a risk focussed on a slowdown in China), we conducted risk modelling and identified stocks that were expected to be impacted by restrictions on the movement of people to and from China. We initially identified the following segments of the market:

- Airline companies - Virgin Australia (VAH);
- Airports - Auckland International Airport (AIA);
- Travel businesses - Corporate Travel Management (CTD), Webjet (WEB);
- Tourism companies – Sealink (SLK); Ardent Leisure (ALG);
- Employment and education businesses - IDP Education Ltd (IEL).

As a result of this analysis, we moved to an underweight position across the companies most directly impacted by the pandemic. These were generally the companies that saw the sharpest share price movements during March (e.g Ardent Leisure -76.7%).

As the downturn accelerated throughout the quarter, we further identified companies that were exposed to associated risks such as retail REITs and tollroads. Companies with weaker balance sheets and potential liquidity concerns were also identified and exposures reduced accordingly.

As we reduced exposure in the Fund to companies directly impacted by the pandemic and subsequent global lockdowns, we selectively added to several high-quality companies with relatively defensive earnings streams. Such companies included Inghams (ING), Freedom Foods (FNP), Evolution Mining (EVN) and Coca-Cola Amatil (CCL).

Over the past few weeks we have observed a pick-up in activity in China as lockdown restrictions are lifted. We have therefore increased our exposure to companies that are poised to benefit from this, particularly those that will benefit from Chinese government stimulus, such as Mineral Resources (MIN).

Another important consideration we have accounted for is positioning the Fund for an eventual market rebound. A sustained market recovery will likely see higher beta companies outperform. We have been monitoring and moderating defensive positions in the Fund that have performed well, whilst simultaneously investing in higher quality, higher beta companies that are expected to performed well in a market recovery.

Examples of stocks that we have recently added include: Ansell (ANN), NextDC (NXT), Altium (ALU), Johns Lyng (JLG), Appen (APX), JB Hi-Fi (JBH) and Seven Group (SVW).

As at 31 March 2020, the largest overweight positions in the Fund were Spark New Zealand (SPK), Saracen Mineral (SAR), and Evolution Mining (EVN).

Market Commentary

The S&P/ASX Small Ordinaries Accumulation Index returned -24.93% for the quarter, underperforming the broader S&P/ASX 300 Accumulation Index which returned -23.41%.

After a strong 2019, global markets initially rallied hard through most of January on positive US/China trade deal momentum and increased certainty regarding Brexit. However, markets fell sharply in late February and March on COVID-19 fears as confirmed cases grew rapidly outside across the globe. From mid-February, volatility in equity markets began increasing as investors struggled to determine the ultimate impacts that the growing outbreak would have on the economy amid government-enforced lockdowns across most markets. Central banks and governments have leapt into action in an effort to fend off the worst of the crisis, with aggregate fiscal stimulus of approximately US$5trn being announced by the end of March.

The Australian market underperformed the US and MSCI World Index, dragged down by its large banking and energy sectors which were hit considerably throughout the quarter. Emerging Markets showed a little more resilience than Developed Markets for the quarter, with the MSCI Emerging Markets index and MSCI World index finishing the quarter down 19.82% and 19.98% respectively (in local currency terms). Geopolitical news included the formal signing of the "Phase 1" trade deal in the US-China trade saga and Brexit officially occurring

on 31 January. However, these outcomes were largely overshadowed by the impacts of COVID-19 and the related collapse of OPEC+ negotiations regarding the reduction of oil production. Investors continued to seek relative safety in the USD, causing the AUD to depreciate 12.67% for the quarter. Treasuries also saw high demand, driving the yield on both the US and Australian 10-year to record lows of 0.54% and 0.61% respectively.

The Healthcare sector lead the ASX for the quarter, seeing some buoyancy among manufacturers and distributors of health and safety protection solutions, as well as diagnostics groups. Energy was the worst performing sector for the quarter (-48.22%), hit by both a reduction in demand due to lockdowns, as well as a significant fall in oil prices detailed further below. Real Estate, typically a more ‘defensive’ sector, was the second worst performer for the quarter on the back of concerns that rents would be cut sharply as tenants are forced to reduce operations during lockdown periods.

On the commodities front, oil prices fell 65.55% owing to weak demand which was not met with a production cut during in March after the failure of key OPEC+ discussions on supply. Gold appreciated throughout the quarter (+3.95%) as investors sought safe haven and iron ore prices were softer (-8.70%) given widespread shutdowns in China for much of the quarter.

In domestic economic news, the RBA cut the cash rate from 0.75% to 0.5% in their March monthly meeting and implemented an emergency cut effective 20th March to bring the rate to a new record low, 0.25%, in response to the economic impacts of COVID-19.

Outlook

The COVID-19 outbreak will likely continue to drive global market sentiment in the short term as investors assess the implications on global growth. We will continue to monitor the risk closely and its evolution over the coming weeks and months will be critical for the performance of stocks and sectors going forward. The recent market volatility once again highlights that periods of risk aversion will continue to emerge, reinforcing the importance of remaining focused on a long-term and diversified investment strategy.

Availability

Product name	APIR
SignatureSuper	AMP0962AU*

* Closed to new members

Contact Details

Web: www.amp.com.au
Email: askamp@amp.com.au
Phone: 131 267

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