

(AMP) Moderately Conservative Index



Quarterly Investment Option Update

30 June 2016

Aim and Strategy

To provide moderate returns from a balance of income and capital growth over the medium to long term, by investing in a diversified mix of growth and defensive assets. Exposure to individual asset classes will be attained through the use of index focussed fund managers. The investment option seeks to provide an index focussed solution to diversified investing. Through a process of diversified market analysis combined with selection of the most appropriate fund managers for each underlying asset class, the fund is designed to provide market tracking returns over the recommended investment time frame.

Investment Option Performance

To view the latest investment performances please visit www.amp.com.au

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP1521AU
CUSTOM SUPER	AMP1521AU
Flexible Lifetime - Allocated Pension	AMP1533AU
Signature Super	AMP1545AU
Signature Super Allocated Pension	AMP1557AU

Investment Option Overview

Investment category Diversified - Moderately Conservative

Suggested investment timeframe 5 to 7 years

Relative risk rating Medium

Investment style Index Focussed

Asset Allocation	Benchmark	Range (%)
International shares		10-30
Australian shares		10-30
Alternative assets (growth)		0-20
Direct property		n/a
Listed property		0-15
Total Growth	55	45-65
Alternative assets (defensive)		n/a
International fixed interest		0-20
Australian fixed interest		5-25
Cash		5-25
Total Defensive	45	35-55

Top Ten Australian Shares Exposure	%
Commonwealth Bank of Australia	8.98
Westpac Banking Corp	6.79
Australia & New Zealand Banking Group Ltd	5.05
National Australia Bank Ltd	4.83
Telstra Corp Ltd	4.69
BHP Billiton Ltd	4.12
CSL Ltd	3.55
Wesfarmers Ltd	3.38
Macquarie Group Ltd	1.85
Westfield Corp	1.63

Top Ten International Shares Exposure	%
APPLE INC	1.53
Alphabet Inc	1.23
MICROSOFT CORP	1.16
Exxon Mobil Corp	1.03
Amazon.com Inc	0.84
Johnson & Johnson	0.82
Facebook Inc	0.80
Nestle SA	0.79
Procter & Gamble Co/The	0.79
WELLS FARGO & COMPANY	0.73

Actual Allocation	%
International Shares	19.65
Cash	18.64
Australian Equities	17.08
Australian Fixed Interest	14.87
International Fixed Interest	13.88
Alternative Assets	9.52
Listed Property	6.36

Investment Option Commentary

Global

Economically, the quarter was dominated by event risk, volatility and switches between a risk-on and risk-off bias. For most of the period speculation on the likely timing of a US interest rate rise dominated sentiment, but towards the tail-end of June the UK referendum (Brexit) on whether to remain or leave the European Union was the key focus. Other influencing events during the period included the validation by Germany's constitutional court of the European Union's Outright Monetary Transaction (OMT) Programme, the ongoing US primaries and the Spanish election.

The UK referendum, on 23 June, resulted in a decision to leave the European Union. The result blindsided global markets, which had largely factored in a decision to remain, and led to an immediate risk-off stance. Following the decision, the British Prime Minister, David Cameron, resigned. The decision has also brought into focus current dissent within the union and fears that it may lead to contagion, with some European political parties now openly suggesting other member countries should also conduct a similar referendum. Both the UK and Europe now face a protracted period of political and economic uncertainty. The British pound and shares fell sharply following the decision, as did the euro and European shares, albeit to a lesser extent. Global shares were also swiftly impacted. Safe haven assets including gold, the US dollar, the Japanese yen and bonds all rose. Following the decision, central banks were quick to emphasise they would provide whatever liquidity is required to stabilise markets. Should the result to leave result in a persistently strong US dollar, it would have the potential to negatively impact the renminbi, commodities and emerging markets, reigniting global growth fears.

However, it is important to put immediate post-referendum market movements in perspective, given the generally elevated level of markets recently and pre-referendum move up in European stocks, on expectations of a remain vote. This is not to preclude further falls and volatility, but rather to emphasise it will take a while for the market to fully digest the implications of the referendum. During June, US shares at one point edged close to an all-time high before pulling back. German 10-year bund yields also moved into negative territory and Australian 10-year bond yields hit an all-time low.

Although the UK referendum result eclipsed other economic events during the quarter as a whole, there was nevertheless the resolution of some other important issues. The German constitutional court validated the European Central Bank's Outright Monetary Transaction (OMT) programme. The programme underpins the European Union's commitment to do "whatever it takes" to preserve the euro and therefore provides some relief in the current uncertain global economic environment. The Spanish general election on 26 June failed to deliver a majority for either main party or alliance, in line with the market's expectations. This will likely lead to a continuing centre-right minority government that will struggle to pass further reforms but won't see earlier substantial reforms unwind. The UK referendum decision, and associated uncertainty, also means the timing of US interest rate rises is likely to be pushed out further.

Australia

Australian economic data released in the quarter was generally reasonable, with solid Manufacturing and services Purchasing Managers Indices (PMIs), retail sales figures, new home sales figures, and a narrowing in the trade deficit recorded. Consumer confidence figures however are still on the low side – perhaps aggravated by talk of cuts to tax concession in the pre-election build-up, while business confidence levels are a little better – with moderate but still reasonable capex intentions. Inflation and wages growth however remain muted, and against this backdrop, the Reserve Bank of Australia (RBA) cut interest rates to a record low of 1.75% in May.

Australia capital city home price growth continued to moderate, with an annual price growth of 7.6%, down from a recent peak of 11.1% last July. Housing price momentum continues to slow, with supply continuing to rise. Investor-

finance and population growth are also both slowing. These factors, along with a raft of media reports on Australian debt-levels and valuation to income ratios, have combined to raise concerns of over-valuation. Another recent spike in residential apartment approvals, combined with high personal debt levels in Australia is posing an increasing risk of a property bust down the track, despite prudential measures put in place last year to temper any market frothiness. While population growth is slowing (down from its 2% peak late last decade to 1.4% last year) this is still obviously aiding demand, though whether housing prices have over-factored this into their current valuations is a question analysts are beginning to ponder.

Aside from significant changes to superannuation, the Australian 2016-17 Federal Budget was relatively uneventful, being pre-election aware and with an emphasis on the incumbent government being fair in its approach. Hence, higher income earners were demonstrably affected, with superannuation tax breaks being wound back at the top end and, for some changes, retrospectively applied. In a highly progressive tax system such as Australia's, making superannuation less attractive and uncertain for any bracket has the potential to discourage longer-term investing and make other strategies, such as negative gearing, relatively more appealing.

Australian dollar

The Australian dollar had a volatile quarter against the US currency, closing slightly lower, and was heavily influenced by the tone of US Federal Reserve (Fed) commentary in regard to monetary its policy intentions. Growing expectations from analysts of further RBA rate-cuts appear to be keeping a lid on the Australian dollar climbing much higher at the moment. The Australian dollar gained heavily against the pound post-Brexit referendum, (as did many of the perceived safe-haven currencies), and is now approaching a three-year high.

International shares

Developed international share markets produced moderate, yet still positive returns for the three month period with emerging markets performing similarly. Global markets remain supported by very easy monetary conditions, good growth in consumer-spending and an overall reasonably positive macroeconomic backdrop, though are unsurprisingly suffering bouts of volatility based on news-flow such as Fed commentary or speculation on election results. Japan's TOPIX Accumulation Index fell by another 7.4%, and is now down nearly 22% year to date. Notably, the UK's FTSE 100 Accumulation Index rose by 6.5% during the quarter, despite a sharp fall post-Brexit referendum, which was more than recovered by month's end.

Australian shares

Australia's S&P/ASX 200 Accumulation Index rose over the quarter, closing higher by 3.9%. The materials sector did particularly well amid improved commodity prices relative to the depths of early 2016. Australian economic figures are still generally positive - yet unexciting, and the RBA seems to be maintaining a reasonably dovish undertone in their wording. International investors continue to be wary of macro-prudential intervention by governments and potential further changes to tax (though this is a risk to the positive-side too, particularly with smaller companies). Small-caps yet again outperformed the broader market, returning 5.8% as measured by the small S&P ASX Small Ordinaries Accumulation index.

International bonds

Global bond yields continued to fall over the quarter, some to new record lows. Yields dropped precipitously after the UK's referendum result to leave the European Union, as traders bought-up fixed interest assets in a typical 'flight-to-safety' reaction that market-shocks (such as the Brexit referendum) tend to produce. US, UK, German and Japanese 10-year government bond yields all fell, to finish the quarter respectively at 1.52%, 0.95%, -0.13% and -0.23%.

Australian bonds

Australian bond yields fell further in the June quarter, with three-year and ten-year government bond yields closing respectively at 1.55% and 2.00%. The long-term trend for Australian bonds remains downward, given continued concerns over domestic (and global) growth prospects along with the RBA's moderate easing bias, demonstrated in May when they lowered the official interest rate to 1.75%. The RBA appears to now be holding fire on a further reduction until newer inflation figures are released.

Cash

Australia's official cash rate was cut to a record-low 1.75% earlier in the quarter in an attempt to further stimulate growth. Following its most recent meeting, the RBA expressed a degree of comfort with current interest rate settings, and while Brexit related risks have added to the case for another rate cut, at this stage the RBA is likely in 'wait and see mode'. Both three and six-month bank bill rates were again lower, closing the quarter at 1.94% and 2.10% respectively.

Listed property securities

During the second quarter the Australian REIT market performed strongly, comfortably outperforming the wider equity market which posted a positive return despite the Brexit-related market turmoil towards the end of the period. The market generally performed well, especially towards the end of the quarter when it was regarded as a relative safe haven, as investors looked to reduce exposure to perceived riskier assets following the UK referendum vote. Office and diversified investments performed strongly in the quarter; Stockland performed robustly following its

acquisition of 95 hectares of land in north-west Sydney for A\$290 million, Dexus Property Group's share price rallied after its bid for the Investa Office Fund failed to secure the required 75% of unitholders and GPT performed well following strong asset price growth in its wholesale office fund.

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Direct property

Each month this quarter has seen momentum strengthen in commercial property investment markets, after share market volatility subdued things the previous quarter. June was particularly active for institutional and private investors. The fall in interest rates in May and weaker momentum in residential markets saw a notable increase in private investor activity in June, culminating with some record low yields paid for smaller assets with secure income, even in cities with weaker economic momentum ahead such as Perth. May and June also saw some large portfolio transactions complete in the retail and industrial sector, purchased by a mixture of both foreign and local investors, some at higher prices.

While investment markets improved, there wasn't much change in leasing market and retail sales momentum over the quarter. Sydney and Melbourne are clearly outperforming the rest of the country across in all the major property sectors and this is being reflected in lower vacancy rates and stronger rental growth.

In the office space, tenant demand continues to be supported by growth in small tenants, centralisation of companies back towards CBDs, and high incentives supporting a flight to quality in most of the main markets. Sydney and Melbourne remain the stars, Perth continues to decline, and the rest of the country is patchy. Investor demand remains positive, but a reduction in assets on-market for sale has resulted in lower sales volumes, with yields remaining stable in the quarter across most major markets. The majority of the \$2.6bn worth of sales this quarter were B grade assets or suburban assets with yields generally in the 6.5-7% range.

In the retail sector, spending improved slightly over the period as lower interest rates and fuel prices flowed through to consumer confidence. However after a period of stability, specialty shop vacancy rates have started to rise again as retailers look more closely at their bricks and mortar footprints, particularly in cities where economic momentum is weakening. Rental growth has thus been allusive outside of Sydney and Melbourne where fundamentals are strongest. JLL Research estimate that there was \$1.8bn worth of major transactions this quarter dominated by Blackstone and Mirvac's purchase of four sub regional malls from Vicinity for \$841.4m. Yields were generally more stable this quarter.

Like the office market, tenant demand for industrial space continues to be quite varied between the various capital city markets with no notable rises in rents besides parts of Sydney. The industrial investment sector has been more active this quarter, with a number of larger portfolios sold, the highlight being Blackstone's purchase of 15 Goodman assets in Queensland, SA and Victoria for \$640m.

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