# Alphinity Australian Share Fund

Quarterly Investment Option Update

31-December-2017

## Availability

| Product name | APIR |
|---|---|
| AMP Flexible Super – Choice (Retirement) | AMP1617AU |
| AMP Flexible Super – Choice (Super) | AMP1608AU |
| CustomSuper | AMP0345AU |
| Flexible Lifetime – Allocated Pension | AMP0629AU |
| Flexible Lifetime – Super | AMP0345AU |
| Flexible Lifetime – Term Pension | AMP0936AU |
| SignatureSuper | AMP0805AU |
| SignatureSuper Allocated Pension | AMP1164AU |
| Flexible Lifetime Investment | AMP0834AU |
| Flexible Lifetime Investment (Series 2) | AMP1639AU |
| MultiFund Flexible Income Plan | AMP0358AU |

## Investment Option Performance

Investment performances are subject to product fees and where relevant tax as outlined in the product PDS. Therefore investment performance may differ between products. In addition, activity on your account such as contributions and deductions will also impact the investment performance specific to you. To view the latest investment performances for each product, please visit **www.amp.com.au**. You can also view the last investment performance specific to you by visiting your My Portfolio account.

## Contact Us

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## Overview

**Aim & Strategy:** The strategy aims to outperform its benchmark after costs and over rolling five-year periods. The strategy is managed by Alphinity who seeks to build a portfolio of Australian stocks listed on the ASX that is well diversified across different industries and sectors and aims to meet the strategy's investment objectives in a risk-controlled manner. The strategy is intended for investors who are happy to invest for at least five years, are seeking high levels of return and are comfortable with high volatility, including the possibility of periods of negative returns.

**Investment category:** Australian shares

**Suggested Investment Timeframe:** 5+ years

**Standard Risk Measure:** 6/ High

**Investment style:** Growth

| Asset Allocation | Actual (%) | Range (%) |
|---|---|---|
| Cash | 1.9% | 0-10% |
| Securities | 98.1% | 90-100% |

**Holdings**

| Industry Exposure | % |
|---|---|
| CONSUMER DISCRETIONARY | 5.08% |
| CONSUMER STAPLES | 9.01% |
| ENERGY | 4.49% |
| FINANCIALS EX PROPERTY | 37.66% |
| HEALTH CARE | 5.10% |
| INDUSTRIALS | 7.37% |
| INFORMATION TECHNOLOGY | 3.52% |
| MATERIALS | 17.72% |
| PROPERTY TRUSTS | 3.53% |
| TELECOMMUNICATION SERVICES | 1.25% |
| UTILITIES | 3.36% |
| CASH | 1.90% |

| Regional Exposure | % |
|---|---|
| Australian securities and cash | 100% |

| Top Ten Securities | % |
|---|---|
| Commonwealth Bank Of Australia | 9.05% |
| National Australia Bank Limited | 7.36% |
| Westpac Banking Corporation | 6.24% |
| Australia And New Zealand Banking Group Ltd | 5.16% |
| CSL Limited | 5.10% |
| Macquarie Group Ltd | 5.02% |
| Wesfarmers Limited | 4.44% |
| BHP Billiton Limited | 4.20% |
| Rio Tinto Limited | 3.84% |
| Aristocrat Leisure Limited | 3.14% |

## Market Commentary

The Australian share market (ASX300 including dividends) had another modest upward move in December, rising by a little less than 2% making it a bit over 7% for the quarter and a pleasing 12% for the year. Alphinity wistfully remember the days when activity died early in December as the thoughts of market participants turned to the beach or the snow rather than making deals. This has not been the case for some years but in December 2017 the deals were frenetic. Some were of very significant size and inference, including those involving Westfield and Fox Broadcasting (see BTW2 on p4). Other deals involved initial public offerings, acquisitions, divestments, capital raisings, capital management – you name it, everything happened right up to the Friday before Christmas.

The long-promised tax cuts in the US finally passed through the legislature, meaning that corporate America will go from one of the highest corporate tax rates in the world, 35%, to around the middle of the pack at 21%. While this is higher than the 15% originally proposed, it does make Australia's 30% appear very high, further reducing our fine country's appeal as an appealing destination for global investment capital. A lower US tax rate may however be a fillip to future earnings for the companies in Alphinity's portfolio with meaningful US operations, including Sims Metal Management, Treasury Wine Estates, Aristocrat Leisure, Macquarie Group and Reliance Worldwide. So too would any meaningful amount of $A weakness. The little Aussie battler remains stubbornly high despite the many pundits who have been calling it to fall below US70c for years, and the $A finished the quarter where it started, just above US78c. It actually appreciated by 8% against the $US during 2017, but fell 5% versus the Euro. The least surprising development in the market was another increase in official US interest rates; more surprising was that the $US subsequently fell.

Most equity markets held up well in the December quarter and Australian shares' total return of over 7% was the second-best of major markets, behind Japan's 12%. The US, UK and Hong Kong returned about 6% and most European markets were in the 1-3% range. For the year however we didn't fare quite so well relative to some other markets, at least in $A terms, although strong gains were experienced pretty much everywhere.

While our market matched the US's 12%, there were some better outcomes from markets like the UK (14%), Japan (15%), and most of Europe (14-20%). Hong Kong achieved an amazing 29% although, just across the border, Shanghai was only up 6.5%. Russia brought up the rear, being the only market to fall in 2017.

Most commodity prices were buoyant during the December quarter. Oil was very strong, rising by close to 20% after a bit of geopolitical tension in the Middle East and some supply disruption. Metallurgical Coal, used in the making of steel, was up a whopping 36%, bringing smiles to the big miners and their shareholders. Copper, which is generally a lead indicator of global economic growth, finished the year strongly, rising by 12% in the quarter and 20% for the year to close at a four-year high.

## Investment Option Commentary

The Fund underperformed the market in the December quarter, with positions in Bluescope Steel, Origin Energy, and diversified miners Rio Tinto and Oz Minerals contributing nicely. Against that, however, were major bank NAB and global property group Lendlease which detracted slightly. The Fund outperformed for the year with help from Aristocrat Leisure, Treasury Wine Estates, Rio Tinto, produce grower Costa Group and Qantas, and the underweight in Telstra, offset somewhat by the fund's positions in Fletcher Building and pallet-renter Brambles. The Fund outperformed for the year with help from Aristocrat Leisure, Treasury Wine Estates, Rio Tinto, produce grower Costa Group and Qantas, and the underweight in Telstra, offset somewhat by the portfolio's positions in Fletcher Building and pallet-renter Brambles.

## Outlook

Regular readers might think Alphinity is starting to sound a bit repetitive, but their view remains that, in the current environment in which global growth and especially interest rates are more likely to surprise to the upside than the downside, an overweight to global cyclicals (i.e. Resource and potentially Energy stocks) continues to look like a reasonable position. These sectors stand to gain the most from any better-than-expected global growth and, although not completely immune to higher interest rates, should be less vulnerable than many so-called long duration stocks (a rise in the interest rate causes a decrease in value). While obviously also exposed to any growth disappointment, the relative valuation appeal of many of the stocks in these sectors (or perhaps the unusually high premium afforded to more operationally defensive companies) also makes Alphinity lean towards them.

China, as always, remains the key risk for the Resource sector. Chinese leader Xi Jinping's "Beautiful China" speech at the Communist Party Congress in October signalled an increased focus on quality of life and environmental controls, however the rate of economic growth required to realise this vision appears not too different to recent years' growth outcomes which bodes well for resource demand. Furthermore, Alphinity's most recent visit to China suggested that order books and production growth remain healthy.

It's too early to be too definite about the impact of the recently-approved tax cuts in the US for individual Australian companies as each has its own debt structure and transfer pricing framework, and changes to US tax deduction criteria are difficult to assess from the outside. However, overall, Alphinity believe the portfolio is well positioned to benefit from what will in some cases be a significant reduction in tax liabilities.

Investment cases are often the strongest when there are multiple earnings drivers and, in Alphinity's view, Computershare is one such company. At the core of Alphinity's investment case has been the growth in its Mortgage Services platform which, after some large business wins, is starting to deliver increased scale benefits and a new source of earnings growth. This, combined with a successful cost-out program based around process automation, led to management raising its earnings guidance for the current financial year at the company's Annual General Meeting late last year. However, Computershare also has some cyclical tailwinds. Corporate activity – Mergers and Acquisitions and other capital management – are now picking up from cyclically depressed levels; and interest income from the company's significant cash balances is gradually increasing along with higher short term rates in the US and elsewhere. Finally, over time the company will likely benefit from the lower US tax rate. For these reasons Alphinity believe the company has entered an earnings upgrade cycle which they expect will continue in the year ahead.