Ironbark Karara Australian Share

Quarterly Investment Option Update

31-December-2017

Availability

Product name	APIR
AMP Flexible Super – Choice (Retirement)	AMP1343AU
AMP Flexible Super – Choice (Super)	AMP1472AU
CustomSuper	AMP0056AU
Flexible Lifetime – Allocated Pension	AMP0588AU
Flexible Lifetime – Super	AMP0056AU
Flexible Lifetime – Term Pension	AMP0887AU
MultiFund Flexible Income Plan	AMP0983AU
SignatureSuper	AMP0736AU
SignatureSuper Allocated Pension	AMP1125AU
Flexible Lifetime Investment	AMP0832AU
Flexible Lifetime Investment (Series 2)	AMP1407AU

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.

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Overview

Aim & Strategy: The Karara Capital is an active investment manager whose approach to Australian equities is built on the belief that original, forward-looking research can identify underappreciated companies. Karara Capital's approach emphasises the development of insights into a company's longer-term prospects. They look to consider all factors that they believe are relevant and carefully assess whether this view is reflected in the market place. Portfolios are built from a diverse range of insights and close attention is paid to understanding the interplay between the holdings. The strategy will primarily invest in 25-35 companies included in the S&P/ASX 100 Index plus an allocation to smaller companies. The allocation to smaller companies is generally between 0-20% of the portfolio, however this can vary over time. Investments of the strategy may also include derivatives such as index futures, which would be used for risk management purposes or as substitutes for physical securities.

Investment category: Australian shares – core

Suggested Investment Timeframe: 5+ years

Standard Risk Measure: 6/ High

Asset Allocation	Actual (%)	Range (%)
Australian Shares	98.09%	90%-100%
Cash	1.91%	0-10%

Holdings

Industry Exposure	%
Consumer Discretionary	8.28
Consumer Staples	5.99
Energy	9.58
Financial ex Property Trusts	32.89
Health Care	6.16
Industrials	8.38
Information Technology	2.04
Materials ex Metals & Mining	7.76
Metals & Mining	11.03
Property Trusts	0.37
Telecommunications Services	0.54
Utilities	5.07
Cash	1.91

Regional Exposure	%
Australia	100

Top Ten Securities	%
Westpac Banking Corporation	6.86
ANZ Banking Group	6.48
Commonwealth Bank of Australia	6.18
National Australia Bank	5.04
BHP Billiton	4.47
AGL Energy	4.42
Rio Tinto	4.07
Origin Energy	3.94
Brambles	3.63
Wesfarmers	3.17

Market Commentary

Global equity markets maintained their strong momentum during the quarter with the MSCI World Index delivering a total return of 5.44% during the December quarter resulting in a total return of 20.6% during 2017. The key drivers being a positive scenario of synchronised global economic growth, tame inflation, a lower US dollar ('USD') and the successful passage of the Trump administration's tax reform bill. Commodity prices also rallied through the quarter, supported by strong Chinese import data. In this context, Australian equities performed strongly as the broad-based S&P/ASX 300 Accumulation Index rose 7.74% to close out the year 11.94% higher, while the small company index rose 13.69%, or 20.02% for the year.

Unsurprisingly, strong economic growth has been a key contributor to stronger commodity prices than was broadly expected at the start of the year. The strength in commodity prices enabled the Australian equity markets to outperform global benchmarks with the S&P/ASX 300 Accumulation Index providing a total return of 7.74% over the December quarter. This represents a 2.3% outperformance compared to the MSCI World Index, albeit over 2017, it underperformed by approximately 8.7%.

Investment Option Commentary

Energy positions, particularly Santos (up 36%) and Origin (up 26%), were the strongest contributors. They benefitted from both the improvement in the oil price but also the actual and the potential for further strong productivity improvements in their respective coal seam gas LNG projects. Santos was also assisted by another takeover approach. Whilst the investment manager does not have a high expectation that Harbour Energy, backed by EIG Global Energy Partners, will produce an acceptable bid, they do think that perceptions around the quality of Santos's assets have been permanently revised higher. The threat of a low bid gaining traction is likely to make management more inclined to spell out the implications for future growth and dividends.

The Fund's position in Oil Search (up 11%) was added to following share price weakness after their surprise $400 million (in USD terms) acquisition of an Alaskan development project. Although the project looks attractive, Oil Search was not short of organic growth options and this move pushes out and re-risks future cash flows.

The gains from energy producers were partially offset by Qantas (-14%), although they finished the year up 51%. Concerns around oil price sensitivity and uncertainty around international capacity additions provided the excuse for abrupt profit taking. The investment manager believes an improved domestic market structure will reduce sensitivity to these factors going forward and that current earnings will be broadly sustained, or rise if current demand conditions are maintained. This is still not reflected in the price. The position, which had been reduced, has been partially rebuilt following weakness.

James Hardie's (up 28%) second quarter results showed very strong unit cost improvement, better-than-expected price outlook and confident statements that lost customers were returning supporting the confidence that the issues faced earlier this year are behind them. The company was also refreshingly direct with their rationale for acquiring Fermacell, a European producer of a niche sound and fire resistant plasterboard product. Hardie's paid a full price for a good business but believes it has the brand and distribution strength to meaningfully establish Hardie's fibre cement siding in Europe.

Star (up 16%) and Crown (up 15%) gave annual general meeting updates in October that showed VIP play is returning much more quickly than the market had anticipated. Star trading was flat relative to the prior period (which was not impacted by the arrests in China) while Crown's VIP activity was down only 17% whereas it had been 57% lower in the six months to June. Crown also announced a series of transactions in December regarding non-core assets that will aid in strengthening its balance sheet during the development of Crown Sydney at Barangaroo.

Strong stock selection also assisted with other portfolio holdings, Navitas (up 20%), Resmed (up 13%) and Brambles (up 12%) were all key contributors. The position in Navitas was reduced given the recent strength seems largely attributable to broader market factors.

Underweights in Bluescope (up 40%) and Westfield (up 21%) were amongst the top detractors. Bluescope benefitted from higher steel spreads emanating from China and Westfield agreed to a takeover by European mall operator, Unibail-Rodamco, with the merged entity to remain listed on the ASX post completion of the transaction.

The Fund's small overweight position to the major banks detracted during the quarter. Also underperforming was AGL (up 4%) despite the recent policy announcements from Federal and Victorian governments that have materially reduced the risk of a negative intervention in the National Electricity Market.

The position in Clydesdale (up 13%) was increased post their result in late November. The investment manager views it as a cost and capital self-help story coupled with leverage to UK base rate increases underpinned by reasonable valuation parameters and strong forecast earnings per share growth.

Outlook

Global growth indicators remain robust, although inflationary expectations currently remain modest. The investment manager anticipates above-trend global growth to continue for some time and for slack in the global economy to decline resulting in higher rates of inflation in due course. With the durability of this period of growth doubted by many market participants, large pools of global capital remain defensively positioned.

Slack in the US economy and labour market is now relatively low and rapidly decreasing in Europe and Japan. Given this, the significant expansionary monetary policy pursued by the three key central banks is increasingly less appropriate and risks are rising that the market is underestimating the pace of tightening that may be required. However, the investment manager anticipates that the key central banks will have some tolerance around inflation exceeding their targets as wage inflation picks up.

Whilst the global growth improvement is relatively synchronised, Australia is lagging. The investment manager anticipates that Australian gross domestic product ('GDP') growth will remain modest at around 2-3%. Strong population growth is assisting headline growth numbers with per-capita growth quite low in a historical context.

The recent pickup in domestic economic data is encouraging, particularly the recent employment data. Overall, the investment manager expects aggregate consumer spending to be broadly in line with household income growth (3-4%), which is still low in a historical context. Further strength in the Australian dollar could jeopardise this.

House prices are high by any measure and conditions in the housing market vary considerably outside of Melbourne and Sydney. The tightening of credit to the investor segment of the market has had a cooling impact on the housing market with a reasonable likelihood of small real price declines over the next couple of years. As a small open economy, the key risk to house prices remains external macro shocks which have, if anything, diminished of late.

Moderate global growth and the return of pricing power in some sectors suggest a reasonable backdrop for many stocks. Although, after the expansion in valuations in recent years, sustained gains will require continuing profit delivery.

The high-levels of valuation dispersion that were observed last year have returned, and exceeded, driven by ongoing increases in the valuations of stocks with defensive growth characteristics. This group of stocks now trades at historically high valuation levels and the Fund remains underweight to this area.

The Fund remains generally positioned for a more reflationary environment than is currently priced by the market and the investment manager continues to believe there are good risk adjusted returns available in many sectors. Within this, the emphasis is on attractive quality companies whose prospects are unappreciated by the market.