Alphinity Australian Share Fund

Quarterly Investment Option Update

30-June-2018

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.

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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	2.02%	0-10%
Securities	97.98%	90-100%

Holdings

Industry Exposure	%
CONSUMER DISCRETIONARY	3.43
CONSUMER STAPLES	9.08
ENERGY	5.65
FINANCIALS EX PROPERTY	34.75
HEALTH CARE	6.34
INDUSTRIALS	8.70
INFORMATION TECHNOLOGY	3.54
MATERIALS	17.68
PROPERTY TRUSTS	5.23
TELECOMMUNICATION SERVICES	0.66
UTILITIES	1.62
DERIVATIVES	1.31
CASH	2.02

Regional Exposure	%
Australian securities and cash	100%

Top Ten Securities	%
BHP Billiton Limited	7.85
Commonwealth Bank Of Australia	6.73
CSL Limited	6.34
Australia And New Zealand Banking Group Ltd	5.39
National Australia Bank Limited	5.18
Westpac Banking Corporation	4.76
Macquarie Group Ltd	4.41
Wesfarmers Limited	3.46
Rio Tinto Limited	3.44
Aristocrat Leisure Limited	3.43

Market Commentary

June marked the end of the 2018 Financial Year (FY18), a time to take stock of where we've been, where we are now and where we're headed. It didn't feel like it for much of the time, but the year actually panned out quite well for our investors. Total return for the market (ASX300 including dividends) was a little over 13%, and for Fund investors a good deal more than that.

The financial year to June 2018 turned out to be a pretty good one for equity market investors, unless they were keen on South America. Most global markets provided solid returns in $A terms, as well as or even better than ours. The $A itself finished at the lowest point for the year, US74c.

Commodity prices have been resilient despite fears of slowing China, however the biggest concern has been the price of copper. Alphinity have written previously about copper – it is one of the more reliable lead indicators of global economic activity as a key constituent of much infrastructure and many finished goods.

June was obviously the time for summits. There was the G7 in Quebec, attended by seven of the world's largest developed economies. There was also the lesser-known Shanghai Cooperative Organisation summit in Beijing, attended largely by what would once have been called eastern bloc countries. Then there was the most spectacular summit, between US President Trump and North Korea's Kim Jong Un. Over the course of a couple of days in Singapore, those two world leaders once and for all sorted out some of the issues dividing their regimes, just like their predecessors had several times over the past couple of decades.

The quarter finished off with a re-eruption of tariff wars between the USA and pretty much everyone else in the world. Markets were remarkably sanguine about it all – possibly not really believing it will come to anything. The rhetoric from the US has become increasingly strident, with numerous fights being picked with some of its traditional allies, like Canada and Germany, and a fair bit of cosying-up going on to some of its traditional foes, like Russia and the aforementioned North Korea. In short, there have been mixed messages going out to pretty much everyone. It seems that, as he approaches two years since his election, the not-so-new US president is living up to his promise to shake things up, not just in Washington but around the world. It is to be hoped that this is all part of a cunning and well-thought-out longer-term plan.

The Australian economy seems to be at another cross-road, with the housing market now apparently softening after several years of strong gains. Banks, a traditional mainstay of our market, are likely to be fairly subdued into FY19 as a result of regulatory action and the ongoing Royal Commission. Demand for resources out of China continues to be robust and although many commentators have been calling for its economy to slow for some time, our on-the-ground research suggests otherwise. It remains to be seen how the progress of the trade war between China and the US will change this of course. Commodities were mixed, as usual, with Base Metals generally softer but Energy continued to rise in price with Gas, Oil and Coal all sharply higher over the quarter, exacerbated by the soft $A.

Investment Option Commentary

The Fund outperformed nicely over the June quarter (before fees) with positive alpha in each month and good contributions from companies in a variety of sectors. Notable positive contributors included gaming company Aristocrat Leisure and financial services company Macquarie Group, both of which announced strong results during the period, as well as plumbing products company Reliance Worldwide which made a significant and quite accretive acquisition. Also helping were companies the Fund didn't own or are underweight which performed poorly during the quarter.

These included financial services group AMP, telecoms company Telstra and global logistics service provider Brambles. The only companies that detracted noticeably from returns were registry company Link Administration and financial services company IOOF.

The quarter topped off a pleasing financial year for Fund investors thanks to its holdings in companies like Rio Tinto, Macquarie Group, Aristocrat Leisure, Treasury Wine Estates, CSL, Reliance Worldwide, Costa Group, and having little or no exposure to Telstra, AMP or Origin Energy. The only detractors of any size were companies we didn't own: Santos, AGL Energy and A2 Milk.

Outlook

The Australian market has shown great resilience in what has become quite a choppy global environment. Some of the reasons for this were discussed above but, while macro factors are always important to be aware of, we find that company specific factors are typically more important drivers of share prices, even in cyclically exposed industries.

For example, Both Rio Tinto and Fortescue Metals are predominantly iron ore producers. Yet Rio Tinto shares generated a positive total return of 39% in FY18 while Fortescue had a negative return of 10%. An increased price discount for Fortescue's lower grade iron largely explains the difference, with Fortescue's earnings expectations more or less unchanged on a year ago while Rio has continued to enjoy consensus earnings upgrades. The difference was not as stark in the Bank sector but still, -7% for CBA vs +4% for ANZ illustrates the same point. As tighter monetary conditions and potentially slower economic growth pose valuation risks for highly valued so-called growth stocks and earnings growth risks for more cyclically exposed companies, in-depth stock analysis becomes even more important.

The Fund heads into FY19 and the imminent August reporting season with strong earnings momentum across multiple sectors. Pleasingly, most of this earnings momentum has been due to company specific drivers rather than macro tailwinds. Qantas is one stock in the portfolio that fits this description well. From a macro perspective there are both some tailwinds, such as an improving demand from the Resources sector, and headwinds, such as the rising oil price. Key to Alphinity's confidence in Qantas however is the overhaul of the company's cost structure that has been undertaken over the last 3-4 years, with additional opportunities still available. This has provided the company with a superior cost position to its rival in the domestic market and thus the ability to offset the increase in its prudently-hedged fuel bill, through increased ticket prices. Internationally, a reworked partnership with Emirates has freed up capacity for Qantas to increase its Asian route network as well as introduce the first direct flights from Australia (Perth) to London as the airline takes delivery of new long distance aircrafts. Together with the potential for further capital management, the company has unique earnings growth drivers to offset any significant rise in its fuel bill.