Walter Scott Global Equity

Quarterly Investment Option Update

30-June-2018

Availability

Product name	APIR
AMP Flexible Super – Choice (Retirement)	AMP1625AU
AMP Flexible Super – Choice (Super)	AMP1616AU
CustomSuper	AMP1601AU
Flexible Lifetime – Allocated Pension	AMP1637AU
Flexible Lifetime – Super	AMP1601AU
SignatureSuper	AMP1607AU
SignatureSuper – Allocated Pension	AMP1631AU

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: To achieve a long term (at least 5 to 7 years) total return before fees and expenses that exceeds the MSCI World ex-Australia Index in Australian dollars unhedged with net dividends re-invested. The portfolio invests primarily in shares of companies listed on stock exchanges around the world, but may also have some exposure to cash and derivatives (e.g. foreign exchange contracts to facilitate settlement of stock purchases). Derivatives will not be used to hedge, leverage or gear the portfolio. The portfolio adopts a 'buy and hold' strategy (approximately 40 to 60 stocks) to allow time for a company's earnings growth to translate into strong share price performance for investors. On average, 15% to 25% of stocks held will be turned over each year. Unlike a top-down investment approach which allocates stocks to country or industry sectors, the portfolio is constructed with a primary focus on stock-based analysis (bottom-up investment approach). As a result, both sector and geographic allocation will generally be significantly different from benchmark indices. As exposure to international assets is not hedged back to Australian dollars, investors will also be exposed to movements in exchange rates. Exposure to derivatives is not reflected in the ranges.

Investment category: Global Equities

Suggested Investment Timeframe: 5 – 7 years

Relative Risk Rating: High

Investment Style: Growth

Asset Allocation	Actual (%)	Range (%)
Global Equities	97.96%	90-100%
Cash	2.04%	0-10%

Holdings

Industry Exposure	%
Consumer Discretionary	16.73
Consumer Staples	7.89
Energy	7.37
Financials	3.07
Health Care	21.04
Industrials	5.79
Information Technology	28.73
Materials	3.90
Real Estate	-
Telecommunication Services	0.46
Utilities	2.98

Regional Exposure	%
Asia Ex Japan	6.05
Europe Ex Uk	18.03
Japan	7.48
North America	56.37
United Kingdom	4.77
Emerging Markets	5.27

Top Ten Securities	%
Adobe Systems Inc	3.33%
Aia Group Ltd	3.07%
Nike Inc	2.90%
Eog Resources Inc	2.88%
Mastercard Inc	2.84%
Keyence Corp	2.84%
Microsoft Corp	2.76%
Edwards Lifesciences Corp	2.63%
Inditex	2.47%
Tjx Companies Inc	2.43%

Market Commentary

From a sector perspective, the portfolio's energy holdings were the standout absolute performers against the backdrop of a firmer oil price; CNOOC and EOG Resources were two of the portfolio's strongest individual stocks. Consumer discretionary companies were also notable absolute contributors, with Nike and TJX Companies particularly strong. Industrial stocks were the only absolute detractors of note, with Fanuc the weakest stock in the portfolio. A low exposure to the weaker financials sector was the largest positive relative contributor, while sole financial holding, AIA Group, led its sector index and also added to relative return. The portfolio benefitted from a higher exposure to the stronger technology sector, but a mixed performance from the portfolio's holdings, which in aggregate lagged their sector index, were the only noteworthy relative detractors.

From a regional viewpoint, US companies drove the portfolio's absolute performance; the aforementioned Nike, EOG Resources and TJX Companies, as well as Intuitive Surgical and Automatic Data Processing, were amongst the key individual performers. US stocks were also key relative contributors. Europe ex UK stocks were the other noteworthy absolute and relative contributors. Japanese holdings were the largest absolute and relative detractors, with Fanuc, Shin-Etsu Chemical and Keyence amongst the most significant detractors.

Investment Option Commentary

Stock Comments

After a challenging couple of years, there has been evidence that Nike has been starting to turn a corner in North America. The company has launched a new initiative – 'Consumer Direct Offense' – that it hopes will set it up for its next leg of growth. It involves stream-lining the organisation to speed up product lead times, narrowing focus on key influencer cities, and sharpening efforts to enhance its direct-to-consumer approach with improved apps and digital engagement. These efforts are starting to bear fruit, as Nike Direct sales grew double digit in the quarter. Momentum is building and the stock has reacted positively.

In the last couple of years, shale oil and gas pioneer EOG Resources has reset its cost base to thrive in a lower oil price scenario. It has sharpened its focus on drilling predominantly 'premium wells', which have an after-tax rate of return over 30% at an oil price of $40. When oil prices rise above that mark, the incremental returns are exceptional, as demonstrated by the company's first-quarter results which demonstrated that it generated triple-digit returns on new wells drilled in the quarter. EOG was already a clear leader in the shale patch, drilling the most productive wells and generating the best returns, however recent efforts have helped it extend its lead.

Adobe performed superbly in 2017 and that strength has carried into 2018 as the fundamentals of the business continue to improve. The shift to a subscription model is exceeding expectations and the potential benefits are enormous: an increased addressable market due to the lower up-front cost, increased up-sell and cross-sell opportunities, and a more predictable, stickier revenue stream. The company has already raised guidance in 2018 after generating 25% sales growth and 46% earnings per share growth in 2017.

Fanuc announced strong quarterly numbers showing a deceleration in revenue and order growth from a high base. The recent weak performance was mainly driven by company guidance and was mirrored by the leading names in the industrial automation sector. Fanuc's management have been prone to providing conservative guidance, which it has beaten in six out of the last eight semi-interim periods.

Portfolio Activity

Tractor Supply was sold in June. While in many respects well placed to withstand the threat posed to its business by e-commerce, Walter Scott nevertheless took the decision to exit the position in Tractor Supply. This was largely the result of new lessons learnt about one of Tractor Supply’s key product categories: pet food. Previously thought to be relatively immune to the online threat due to its bulky nature, Walter Scott’s experience with another investment, in the UK, undermined this assumption. While pressures had yet to manifest themselves in the case of Tractor Supply, the competitive environment is only becoming more intense; so following strong quarterly performance thwe Fund took the decision to be prudent and to sell the holding.

Outlook

For some, deep analysis of how companies think and work will seem a million miles away from the current market preoccupation with trade wars and interest rates. For Walter Scott, however, this is a more important exercise than pontificating over the vagaries of the stock market given their long-term investment horizon. That is not to say they are disinterested in how the trade spat develops, as it has the potential to alter and disrupt the operating environment for companies across the globe. With the first salvoes being fired in the current Sino- US trade spat, it remains to be seen if this is the start of a brutal dispute with the two economic heavyweights slugging it out, or more a case of the US employing a form of gunboat diplomacy to secure a better trade deal from China. This trade fracas comes at a time when the US is also seeking to alter some long-term, multilateral trade agreements with longstanding trading partners. The ultimate outcome is uncertain, but it might be argued that in the process of Trumpian deal making, his 'playing hardball' will induce some degree of trade concessions without causing massive disturbance of trade flows with questionable economic effects. Neither are Walter Scott fazed by the creeping normalisation of interest rates, as this is reflective of the fact that much of the global economy is in decent shape.

That said, against this equity market backdrop, it is all the more critical to stick to the ethos, and invest for the long term in wealth-creating companies with market-leading positions and strong balance sheets. Walter Scott’s diverse holdings of leading companies can be characterised as having 'moat' qualities: dominant businesses occupying prime positions within their sector. The pursuit of such companies is the best means of protecting client money in this volatile environment.