

Super Easy Alternative

Quarterly Investment Option Update

30 September 2018

Aim and Strategy

To provide returns similar to the Hedge Fund Research Index (Customised) benchmark on a 3 year rolling basis. The option takes long and short positions using derivatives. Investments are made globally across equity, government bond, commodity and currency futures markets. The strategy does not make investments in underlying hedge strategies. Currency exposures are not hedged back to Australian dollars and are instead used as a value add strategy. The strategy is allowed to gear using short positions – no more than 30% of the Net Asset Value of the strategy.

Investment Option Performance

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

Investment Option Overview

Investment category	Alternative strategies
Suggested investment timeframe	5 Years
Relative risk rating	Medium
Investment style	Index

Asset Allocation	Benchmark (%)
Growth alternatives	100
Cash	0

Market Review

The September quarter saw developed share markets rise, with the US market hitting record levels; however the mood has been tempered somewhat by emerging market jitters. The rise in US shares has occurred despite escalating trade war risks over which the market seems relatively sanguine, at least in the short term. However, the US administration will now implement a 10% tariff on around US\$200 billion worth of Chinese goods, with the tariff increasing to 25% if negotiations do not turn out favourably, or if China instigates retaliatory measures. Rising tariffs will disproportionately affect the less well-off in President Trump's supportive demographic as large retailers, such as Walmart, source a high percentage of their goods from China. Hence, significant levies on Chinese imports would effectively translate into a 'tax' on this demographic, reflected through increased prices at the till. US businesses have also raised concerns that tariffs will impact supply and revenues. As widely anticipated, at the end of the quarter, the US Federal Reserve raised the federal funds rate target once more by 25 basis points to 2.00%-2.25%. The US 10-treasury bond yield also edged north of the psychological 3%, with the market anticipating the increasing interest rate trajectory to continue into 2019.

In the Eurozone, overall economic sentiment has fallen, with core inflation now around the 1% level on a year-on-year basis, leading the European Central Bank to adjust its forecasts lower for the second half of the year. The market currently expects the European quantitative easing programme to finish at the end of the year, with the first rate hike to take place in the third quarter of 2019. Germany factory orders have continued to pull-back; however stronger business conditions indicate economic resilience. Construction on the Nord Stream 2 Russia-Germany gas pipeline has increased tensions internally between Germany and the EU and also externally between the US and the EU, highlighting the fragile state of certain areas of European politics. Commission President Jean-Claude Juncker gave his State of the Union speech, highlighting the risks of having the US dollar as the reserve currency in the current trade war environment, particularly as energy imports are paid for in US dollars.

Negotiations over Brexit have become increasingly fraught, with tangible outcomes from the Salzburg summit remaining elusive, and initial conciliatory gestures turning sour. Other EU leaders have rejected the UK's latest proposals, known as the "Chequers Proposal" and have asked the UK to come up with alternative suggestions. German business lobbyists have also criticised the latest proposals for the UK to remain part of the single market for goods while excluding free movement of services, capital and people. This has emboldened critics and potential challengers to the Prime Minister Theresa May and has made her position less secure. There is now the increasing possibility of an exit from the union without a formal trade agreement.

In Asia, Japanese data continued to be mixed, with a very tight labour market however with falling industrial production. Japan kept interest rates unchanged as inflation remained well under the 2% target. The private Chinese Caixin business conditions purchasing managers indices have fallen marginally although the official index posted gains. Stimulus measures are likely to continue to maintain liquidity as credit concerns increase and act as a buffer against an escalating trade war with the US. Chinese growth, however, is likely to soften in the shorter term as rules on shadow-bank lending and general credit are still relatively tight despite an easing of some monetary and fiscal channels. The focus is on tax cuts and infrastructure investment. Overall however, these measures should lead to a generally supportive environment for growth in the medium term as well as provide some support to share prices, which fell heavily over the first half of 2018.

In emerging markets, the fear of contagion continued to rise as Argentina's economic woes started to spiral out of control; with the speed of decay wrong-footing many investors. As the peso collapsed the administration raised interest rates to 60% in an attempt to defend the currency as the spectre of hyper-inflation risk loomed. The International Monetary Fund said it would review its current agreement to provide US\$50 billion in aid and this stabilised the Argentinian market and currency to some extent. The administration is looking to implement an austerity budget to further stem the depreciating peso. Turkey also raised interest rates and released plans to cut public spending in an effort to shore up its ailing currency. However, the administration faces credibility issues with a history of non-standard responses to crisis issues and an increasingly authoritarian regime. Both the Argentinian and Turkish economic scenarios have focussed international investors on emerging markets in general, especially in regards to ongoing current account deficits and hard-currency financing requirements. A continuing strong US dollar will stress economies at the periphery that rely on foreign financing for liquidity and investment. A slowing Chinese economy would also impact demand in emerging economies. Worries of a downward spiral in economic activity remain, as emerging economies have generally been forced to raise their cash rates to stem currency outflows. Some positive signs however have emerged, with economic growth improving in Russia and tax reform in India.

Oil became increasingly supported amid concerns over global supply constraints, with Brent crude pushing above US\$80 a barrel towards the end of the quarter.

Availability

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