Schroder Australian Equities

Quarterly Investment Option Update

31 December 2018

Aim and Strategy

To outperform the S&P/ASX 200 Accumulation Index after fees over the medium to long term by investing in a broad range of companies from Australia and New Zealand. With an established pedigree of investing in Australian equities for over 50 years, the Schroder Australian Equity option is an actively managed core Australian equity portfolio with a focus on investing in quality stocks predominantly in Australia characterised by strong returns on capital with a sustainable competitive advantage. The option draws on Schroders' deep research capabilities, with a long term focus on investing, it is suitable as a core portfolio holding over the medium term to long term.

Investment Option Performance

To view the latest investment performances for each product please visit amp.com.au

Investment Option Overview

Investment category	Australian Shares
Suggested investment timeframe	3 - 5 years
Relative risk rating	6 / High
Investment style	Core

Asset Allocation	Benchmark (%)	Actual (%)
Equities	95%-100%	97.8%
Cash	0%-5%	2.2%

Sector Allocation	%
Energy	4.0
Materials	25.7
Industrials	8.3
Consumer Discretionary	6.2
Consumer Staples	6.8
Health Care	1.6
Information Technology	0.5
Communication Services	6.4
Utilities	2.9
REITs	2.2
Financial (ex Property Trusts)	33.0
CASH	2.43

Top Holdings	%
Commonwealth Bank of	7.8%
BHP Group Ltd	5.9%
ANZ Banking Group Ltd.	5.1%
Rio Tinto Limited	4.9%
Westpac Banking Corporation	4.8%
Woolworths Group Ltd	4.4%
National Australia Bank	3.8%
Telstra Corporation Limited	3.7%
Brambles Limited	2.6%
ASX Limited	2.3%

Investment Option Commentary

Contributors
Trade Me (o/w, +24.9). Interest from a couple of private equity buyers culminated in an agreed acquisition by Apax Partners for NZ$6.45, a multiple of nearly 20x reported 2018 EBIT. Although the bid is a more than fair price for a very good quality business, losing the business from the listed market leaves us with mixed emotions. Unlike many of their Australian listed counterparts, which often blend egos the size of Saturn with performance the size of Pluto, Trade Me management have consistently delivered strong results with humility and managed the business with a focus on customers and the longer term.

Navitas (o/w, +13.2%). An uncomfortable situation in which founding shareholder Rod Jones has joined with BGH Capital in a proposed acquisition of the business at $5.50 a share has to date resulted in a rejection of the proposal by the board and management. The publication of earnings targets for the coming years would, if achieved, leave the business on highly attractive multiples at the current share price. While a healthy degree of cynicism is always warranted in relation to forecasts concocted in times of hostile acquisition activity, Schroder have for some time been positive on the future for the education sector and the prospects for efficient operators in a sector often characterised by inefficiency and excessive government intervention.

Detractors
CYBG plc (o/w, -44.1%). The decision to invest in CYBG has been an exceedingly poor one. Perusal of the management presentation would lead one to believe things are progressing swimmingly. The list of strategic and financial objectives is accompanied by a management assessment which reads tick, tick, tick (all based on pro-forma numbers, of course). Having almost halved in value over the past quarter, the investor assessment is clearly cross, cross, cross. The root of most of the evil is the acquisition of Virgin Money (this pile of steaming manure bought at the investment bank car-yard for the perpetually optimistic is leaking oil and spewing smoke even before it’s out of the yard), although the further blowout in mis-selling liabilities and concerns over Brexit have also contributed significantly. The Fund Manager’s belief that the share price has overreacted to the level of value destruction has led us to retain the portfolio position.

LendLease (o/w, -40.8%). Despite frustrations on recent hiccups in the construction business across and the tendency of management in these businesses to expose shareholders to unacceptably large potential losses (relative to profits), the report card over recent years in the remaining businesses has generally been solid. Although the ability of highly competitive operations such as property development to digest heavy corporate cost structures such as those of LendLease always cause us some consternation, this is balanced by a sensible and measured approach to growth, where almost all initiatives have been organic.

Market Commentary

Domestically, with APRA having taken steps early in 2017 to control profligate lending, mild falls in house prices are already causing back-pedalling, with interest-only residential mortgage restrictions set to be lifted in January 2019. As the only purpose of an interest only loan seems to be to speculate on capital gain, any claims of ambivalence to asset price direction by policymakers appear disingenuous.

Outlook

We seem to live in the era of the increment. Attempting to look past the increment in data or earnings to form a longer run view of value has been painful. Behaviourally, investors with any ounce of contrarian inclination are struggling to recover from being run down by the quantitative freight train every time they step on to the tracks. It becomes progressively more difficult to step back on.

Equilibrium continues to feel some way off in the fund manager’s view as supposed capitalists justify their intervention while simultaneously ensuring capitalism does not function properly. While investing in the coddled has been lucrative as economic inequality is mirrored in the equity market, valuations reflect ever greater extensions of this inequality. Significantly lower valuations for those more subject to the vagaries of actual competition lead us to believe the shift back towards equilibrium will offer great opportunity when market forces become too difficult to overwhelm.

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP0465AU
AMP Flexible Super - Retirement account	AMP1375AU
AMP Flexible Super - Super account	AMP1504AU
CustomSuper	AMP0465AU
Flexible Lifetime - Allocated Pension	AMP0636AU
Flexible Lifetime - Term Pension	AMP0944AU
Flexible Lifetime Investment	AMP0995AU
Flexible Lifetime Investment (Series 2)	AMP1438AU
SignatureSuper	AMP0813AU
SignatureSuper Allocated Pension	AMP1177AU
SignatureSuper Select	AMP0813AU

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