

UBS Australian Small Companies

Quarterly Investment Option Update

31 December 2018

Aim and Strategy

To provide a total return (after management costs) in excess of the S&P/ASX Small Ordinaries Accumulation Index when measured over rolling five year periods. The investment option aims to provide investors with capital growth and income from a portfolio of small company shares that we believe are being undervalued by the market, based on our assessment of the company's future cash flows.

The portfolio comprises of securities listed on recognised exchanges in Australia and New Zealand, or those we reasonably expect to list within six months. The portfolio may also invest indirectly in listed Australian and New Zealand securities through investments in other relevant UBS managed funds. The portfolio may invest in financial derivatives to gain exposure to the Australian share market or to manage investment risk. Normally the portfolio will hold between 30 and 60 stocks in companies and sub funds with the majority of investments to be made in securities not in the S&P/ASX 100 index.

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	7 years
Relative risk rating	7 / Very High
Investment style	Small Capitalisation Shares

Asset Allocation	Benchmark (%)	Actual (%)
Australian & NZ Shares	90-100	94.35
Cash	0-10	5.65

Sector Allocation	%
Health Care	16.41
Consumer Discretionary	16.14
Materials	10.40
Information Technology	9.29
Communication Services	9.20
Consumer Staples	9.16
Financials	7.41
Industrials	7.27
Real Estate	5.18
Energy	3.89

Top Holdings	%
Atlas Arteria	4.52
Elders	4.19
Saracen Mineral	3.95
Independence	3.93
NextDC	3.60
Healius	3.56
Infomedia	3.54
BWP Trust	3.44
Collins Foods	3.42
Nanosonics	3.38

Portfolio Summary

- Small cap stocks underperformed their larger cap counterparts over the quarter
- The Australian economy is still performing well although the accelerating weakness in Australian house prices (especially in the economically important Sydney and Melbourne markets) may be an unfavourable economic portent for 2019.
- The S&P/ASX Small Ordinaries Index trades at a valuation premium to the S&P/ASX 100 (14.6x vs 14.4x)

Investment Option Commentary

Positive contributors for the December quarter included Technology One, Nine Entertainment (not held), Seven Group (not held), St Barbara, Worleyparsons, Mayne Pharma (not held) and Regis Resources. Technology One reported a solid full year result with the shift to a SaaS first model likely to generate faster growth in the future. The rallying gold price saw Regis Resources and St Barbara perform strongly. Having exited Worleyparsons post the recent acquisition the stock continued to fall on the weakness in oil price. Nine Entertainment completed the merger with Fairfax and increased synergy targets however continued weakness in advertising markets saw the stock underperform.

Negative contributors included Beach Energy, Bapcor, Starpharma, Domino's Pizza, Pilbara Minerals, Emeco Holdings and oOH Media. Beach Energy was lower on the significant decline in the oil price over the quarter. Bapcor entered the commercial truck parts sector via acquisition which the Fund Manager views as a logical addition to the business. The stock was however subject to profit taking following recent outperformance. Starpharma fell following the FDA requiring further clinical data before approving the company's VivaGel BV product. Pilbara Minerals fell on concerns around the pricing outlook for Lithium following a disappointing update from listed peer Orocobre. The media sector had a tough quarter with oOH Media also impacted by concerns of softening advertising markets.

Market Commentary

The S&P/ASX Small Ordinaries Index declined -13.70% during the December quarter, underperforming the ASX100 which declined -7.73%. The Small Resources sector fell -14.5%, underperforming the Small Industrials which fell -13.4%.

Best performing sectors for the December quarter were Metals and Mining - Precious +23% (Saracen +57%, St Barbara +35%, Regis Resources +30%), REITS +0.6% (Shopping Centres Australia +9%, Charter Hall Retail REIT +9%, BWP Trust +8%), and Agricultural Products -1% (Graincorp +17%, Select Harvest +15%).

The worst performing sectors during the December quarter were Energy -35% (Sundance Energy -55%, Senex Energy -45%, FAR -42%), Media -31% (Seven West -45%, Nine Entertainment -39%, Domain Holdings -36%) and Engineering & Mining Services -30% (RCR -100%, Worleyparsons -44%, Emeco Holdings -41%).

Outlook

The S&P/ASX Small Ordinaries Index finished December 2018 priced at PER of 14.6x, a premium to the S&P/ASX 100 at 14.4x. The Small Ordinaries index (-4.18%) underperformed the ASX 100 +0.27%.

The Australian economy is still performing well although the accelerating weakness in Australian house prices (especially in the economically important Sydney and Melbourne markets) may be an unfavourable economic portent for 2019. Beyond the fall in new car sales, recent softness in retail sales data points to more evidence of a fading domestic consumer. Adding to this mix, the next six months will be dominated by somewhat higher political uncertainty given key elections in NSW, Victoria and nationally. Clearly elections are not conducive to elevated levels of either consumer or business confidence. The global economic outlook remains equally clouded by the key macro risks, specifically trade war tensions, rising rates in the US and slowing Chinese and European economies.

There is no doubt that a 13.7% fall in a quarter can shake one's confidence in the longer term. Nevertheless, UBS continue to believe Australian small companies remain an attractive asset class. They still provide an abundance of opportunities for exposure to unsynchronised long-term growth, assisted in many instances by a number of enduring structural tailwinds. We continue to seek out such tailwind assisted growing small companies, especially those that are well managed with high or rising returns on capital and lower levels of debt. Such businesses should deliver investors attractive returns over a five- year investment horizon.

Availability

Product name	APIR
AMP Flexible Lifetime Super	AMP0469AU*
AMP Flexible Super - Retirement account	AMP1329AU*
AMP Flexible Super - Super account	AMP1458AU*
AMP Growth Bond	AMP1194AU*
CustomSuper	AMP0469AU*
Flexible Lifetime - Allocated Pension	AMP1094AU*
Flexible Lifetime - Term Pension	AMP1095AU*
Flexible Lifetime Investment	AMP0019AU*
Flexible Lifetime Investment (Series 2)	AMP1398AU*

* Closed to new members

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