Schroder Australian Equities

Quarterly Investment Option Update

30 September 2019

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
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Equities	95%-100%	97.5%
Cash	0%-5%	2.5%

Sector Allocation	%
Energy	4.1
Materials	25.6
Industrials	8.8
Consumer Discretionary	3.5
Consumer Staples	7.2
Health Care	2.0
Information Technology	1.2
Communication Services	5.8
Utilities	2.0
REITs	2.8
Financial (ex Property Trusts)	32.1
CASH	2.5

Top Holdings	%
Commonwealth Bank of Australia	6.0%
BHP Group Ltd	5.2%
Australia and New Zealand Banking Group Limited	5.2%
Westpac Banking Corporation	4.7%
Woolworths Group Ltd	4.6%
Rio Tinto Limited	4.1%
National Australia Bank Limited	4.0%
Telstra Corporation Limited	3.2%
Aurizon Holdings Ltd.	2.8%
South32 Ltd.	2.7%

Investment Option Commentary

Lendlease (o/w, +37.5) Leandlease has been rerated as it makes a case with the sale of Engineering that it should be valued more in line with peers such as Goodman Group given a $80b global urban regeneration pipeline, and access to third party funding sources to ensure this is a capital light source of growth for Lendlease shareholders. Execution has been mixed, with Engineering an operational snafu of high order, however Lendleases's fum is now within 15% of Goodman Group's and yet it is trading at about 1/3 of the multiple.

Aurizon (o/w, +11.6%) With prices which have encouraged a change in perception for the duration of Queensland coal mines, the owner of 2,670 kilometers of rail track linking 50 coal mines in the Bowen Basin in Queensland to five export terminals has seen an improvement in investor sentiment. A better regulatory outcome than the catastrophe which had been feared a year ago with the QCA ruling on network pricing. Aurizon has added self help to this improvement in the external environment with a structural review concluding with a proposal for a structural re-organisation which shall allow greater gearing levels in Aurizon in future years. A $300m buyback, the first of several expected to be funded through this restructure, was also announced. A focus upon maintaining efficiency whilst improving effectiveness and providing value to its mining customers has seen Aurizon's operating performance improve through the past year.

CYBG (o/w, -39.2%) Many exogenous events have hurt Clydesdale Bank through the past year – Brexit, UK interest rates and, most critically, ongoing penalties relating to the misselling of payment protection insurance policies. With a final date for PPI claims at the end of August, Clydesdale was hit with a greater quantum of claims than it had anticipated and was forced to downgrade, again. The incidence of claims being greater than anticipated afflicted the industry, with Lloyds, Barclays and RBS also downgrading for the same reason. The total cost for the UK industry from penalties arising from the mis selling of PPI is (pounds) 50b, or the entire market cap of CBA. The extent of claims that may be made against the Australian banks in the event of a downturn could yet prove to be far greater than current forecasts.

Market Commentary

Amidst all the noise in investment markets, some things are eternal and ultimately prevail. Cashflows drive valuations, for example; an eternal truth which will prevail 50 years hence, no matter the interest rate, trade war, Brexit or other issue de jour in 2069.

The past month has seen this play out to some degree, with the short lived "value rotation" interrupting what had been a monochromatic style environment for equity markets for several years. It had seemed intuitive and inevitable that a globally co-ordinated zero interest rate policy in the Western world led to high equity multiples for those companies offering the siren song of yield, or growth. Alas, the past month has highlighted that multiples are fickle, and lower discount rates don't just presage higher multiples; they also in theory, and now increasingly in practice, presage lower cashflows as well.

Outlook

Low to no interest rates are causing large dislocations in the price of Australian equities perceived to offer security of income, on the one hand, and growth on the other, with a squeeze in the ugly centre where a downgrade pimple in a flash is priced as a de-rated mole, no matter the sector. Sustainability of earnings and, more importantly, cashflows, has never been more important, nor securities more harshly dealt with if expected levels of cashflow evaporates. The better opportunities that exist in the current market tend to be idiosyncratic, where cashflows are hit albeit not by structural factors, and where derated multiples become attractive.

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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