

Schroder Australian Equities

Quarterly Investment Option Update

31 March 2020

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	2.77
Materials	28.30
Industrials	10.18
Consumer Discretionary	2.83
Consumer Staples	7.89
Health Care	4.16
Information Technology	1.01
Communication Services	6.89
Utilities	2.18
REITs	2.44
Financial-X-Property Trusts	26.70
Cash	2.51
Other	2.13

Top Holdings	%
BHP Group Ltd	7.10
Commonwealth Bank of Australia	5.18
Woolworths Group Ltd	4.28
Australia and New Zealand Banking Group Limited	4.01
Telstra Corporation Limited	3.98
Rio Tinto Limited	3.90
Westpac Banking Corporation	3.65
South32 Ltd.	3.54
CSL Limited	2.92
Brambles Limited	2.90

Investment Option Commentary

ASX Limited (o/w, -0.14%) Low levels of debt has seen ASX perform less well than many of its peers with a perception of revenue certainty through the market upswing. Turning a vice into a virtue as the market changed course, as a lowly geared company with higher volumes through the market sell-off, it was unsurprising that ASX has performed well.

Woodside (u/w, -45.6%) Not owning Woodside aided portfolio performance as it underperformed following the collapse in the oil price. Whilst operating reasonable quality projects in the North West shelf, our fear is that Woodside is determined to make increasingly large investments into increasingly marginal projects in Browse and Scarborough. We are also concerned the LNG linkage to the oil price continues to decline, halving almost halved through the past decade, and whilst demand has been and will remain strong, supply has and will continue to overwhelm demand leading to ongoing pricing pressure.

CSL (u/w, +8.1%) As one of what we believe is the best managed, globally diversified companies in Australia, we struggle reconciling only two things with CSL. Firstly, it has grown profits by US\$1b in recent years through an aggressive pricing strategy, especially into the US market. Profits are forecast to grow at the same rate in coming years, well in excess of underlying volume demand, which connotes further pricing increases from a base where excess returns are already generated. The second and larger issue is the multiple paid for the earnings, which at more than 30 times EBIT remains at extreme levels for a large company on the ASX.

Market Commentary

In navigating the current landscape in the short to medium term, Schroders have a few guiding principles. Firstly, fiscal stimulus is dedicated to job preservation, especially for those in full-time employment. Consequently, scope for government support for other claimants, such as landlords, equity owners (even foreign owners of a listed airline) and the NRL and AFL is not likely to be plentiful. Secondly, the duration of the pandemic is unknown, with our Healthcare analyst Dr Sally Warneford not optimistic a vaccine will be available for public use within 18 months and the general view being that the social cost of Australia pursuing the herd immunity policy of the UK appears to be too great. In turn, it is hard for us to envisage a “V” shape pattern to economic activity and company profits. Thirdly, equity markets remain vulnerable because the sensitivity of earnings to this downturn is obviously high, but the capacity for them to bounce back just as strongly where earnings are linked to the consumer in particular, is limited. And finally, equity market vulnerability remains because multiples on mid-cycle earnings remains well off lows seen in prior market corrections as seen by Schiller multiples, albeit the dispersion in multiples across the market on this basis is also wider than ever, with Healthcare trading two standard deviations expensive.

Outlook

Multiples are now at reasonable but cheap levels across the market, but the bifurcation within the market remains wider than ever even after the market correction. Earnings growth is still wildly optimistic, and the investment manager expect an ongoing drag through not just FY21 but also into FY22. They remain very wary of consumer-facing names, and for example are assuming long run turnover through shopping centres to be circa twenty per cent below last year's levels. Indirect exposures to the consumer – retail banks and landlords – may also see ongoing earnings pressure in that environment. The inevitable broadening of supply lines outside of China ostensibly supports manufacturing; however, there is little listed exposure to that trend. Changes in their portfolio structure are minimal following the recent ructions as our portfolio biases – lower levels of gearing, and exposures away from the consumer and domestic consumer especially – have been reinforced by what they believe are the likely longer-term impacts. Having said that, the investment manager are ever mindful of the wisdom of Obi-Wan Kenobi; “You're going to find that many of the truths we cling to depend greatly on our own point of view”.

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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