Magellan Global

Quarterly Investment Option Update

31 March 2021

Aim and Strategy

The primary objectives are to achieve attractive risk-adjusted returns over the medium to long term, while reducing the risk of permanent capital loss. The investment option seeks to invest in companies that have sustainable competitive advantages, which translate into returns on capital in excess of their cost of capital for a sustained period of time. The investment manager endeavours to acquire these companies at discounts to their assessed intrinsic value. The portfolio primarily invests in the securities of companies listed on stock exchanges around the world, but will also have some exposure to cash. The portfolio can use foreign exchange contracts to facilitate settlement of stock purchases and to mitigate currency risk on specific investments within the portfolio. It is not the investment manager's intention to hedge the foreign currency exposure of the portfolio arising from investments in overseas markets.

Investment Option Performance

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

Investment Option Overview

Investment Category	Global Shares
Suggested Investment timeframe	7 years
Relative risk rating	6 / High
Investment style	Specialist
Manager style	Single Manager

Asset Allocation	Benchmark (%)	Actual (%)
Global Shares	80-100	94.7
Cash	0-20	5.3

Regional Allocation	%
China	10.1
France	1.5
Germany	4.0
Switzerland	7.1
United Kingdom	4.2
United States	67.8
Cash	5.3

Top Holdings	%
Microsoft Corporation	7.3
Alphabet Inc	6.8
Facebook Inc - Class A Shares	5.8
Starbucks Corporation	5.5
Alibaba Group Holding Ltd	5.1
Tencent Holdings Ltd	5.0
Visa Inc	4.4
Netflix Inc	4.3
Reckitt Benckiser Group	4.2
Pepsico Inc	4.1

Investment Option Commentary

The portfolio recorded a positive return for the quarter in absolute terms. The biggest contributors were the investments in Alphabet, Tencent Holdings and Microsoft. Alphabet rallied after its 23% surge in revenue for the fourth quarter that was driven by Search and YouTube advertising beat expectations. Tencent rose after it was among the Chinese stocks that the Trump administration spared from its ‘blacklist’ of Chinese stocks. Microsoft gained after fourth-quarter sales advanced a higher-than-expected 17% on pandemic-driven demand for video games and cloud resources.

The biggest detractors were the investments in Netflix, PepsiCo and SAP. Netflix declined as risk-taking investors rotated from streaming to legacy media companies. PepsiCo fell as further restrictions on out-of-home activity were implemented, especially in Europe. SAP declined as investors baulked at its shift to a cloud-based subscription model (rather than relying on selling licences).

In relative terms, the strategy underperformed over the quarter. While the portfolio performed strongly during the pandemic up to the end of October, it has lagged the benchmark since November for three main reasons.

The first was, to conform with portfolio risk controls (a combined risk-ratio cap of 0.8%), about half of the portfolio was invested in cash and defensive equities such as utilities, consumer staples and defensive healthcare. This portion of the portfolio has delivered lagging returns compared with the benchmark (but not noticeably against defensive stocks overall), highlighting the unusually strong preference among investors for riskier investments. The flipside is that these stocks are at their cheapest in many years, giving the fund comfort about future portfolio returns.

The second reason for the underperformance was the stock-specific issues faced by companies such as Alibaba. Despite their volatile stock prices, the fund remains comfortable with its investments and see a high likelihood of them delivering attractive returns over the horizon of three to five years. The third reason was the fund’s underweight exposure to cyclical equities. The fund is more attracted to defensive equity valuations compared with those of cyclicals.

Market Commentary

Global stocks reached record highs as they rose for the eighth quarter in nine for the three months to March after the vaccine rollout intensified, US President Joe Biden capitalised on the Democrat’s surprise control of Congress to launch massive fiscal stimulus, the Federal Reserve reiterated it would keep interest rates low, encouraging reports emerged on the US economy, and investors welcomed Italy’s new prime minister. Gains were capped as US bond yields rose on concerns that the fiscal stimulus could revive US inflation and a third wave of covid-19 infections swept through Europe. During the quarter, 10 of the 11 sectors rose in US dollars. Energy (+22%) climbed most while consumer staples fell (-0.6%). The Morgan Stanley Capital International World Index climbed 4.9% in US dollars and 6.3% in Australian currency over the quarter.

US stocks gained as the White House count showed 37% of Americans had received one vaccine dose by quarter end and Democrat control of Capitol Hill allowed Biden to force a US$1.9 trillion bill through Congress that, at 9% of GDP, will boost the budget shortfall for fiscal 2021 to 18% of output. The Democratic party gained control of the Senate after winning the two seats in Georgia that went to a special election (by-election) on January 6. The result tied the Senate 50-50 but new Vice President Kamala Harris’s tie-breaking vote gives the party control of the upper chamber to go with its control of the House of Representatives and the White House. In other political news, outgoing president Donald Trump was impeached and acquitted for a record second time. The House in January impeached Trump for helping to incite a mob that breached congress during a protest on January 6 against the election result. The Senate in February acting as an impeachment court acquitted Trump when it failed to gain the required two-thirds majority, though seven Republicans were among the 57 who voted for a guilty verdict while 43 senators voted not guilty. The Fed soothed concerns about bond yields rising on inflation concerns. Fed Chair Jay Powell testified to Congress that the US’s recovery is “far from complete” and that the central bank intends to keep interest rates at levels that support employment growth while concerns about inflation remain low. In economic news, the US economy grew at a (revised) annualised speed of 4.3% in the last three months of 2020. The March quarter was marked by individual investors on Reddit and Robinhood bidding up selected stocks that heightened concerns of a stock bubble and the liquidation of Archegos Capital Management’s leveraged bets that hurt selected stocks and its banking counterparties. The S&P 500 Index rose 5.8%.

European stocks rallied after the vaccine rollout gained enough pace, the European Central Bank loosened monetary policy even more and Mario Draghi won parliamentary backing to become Italy’s next prime minister. Draghi, the former president of the European Central Bank, accepted a mandate from the Italian President Sergio

Mattarella to lead the eurozone's third-largest economy after Italy's 66th post-war government collapsed. The European Central Bank officials spoke to calm investors about the risk from rising bond yields as it stepped up the pace of bond-buying to arrest the rise in borrowing costs. This offset the damage from a third wave of infections that forced fresh restrictions across Europe. An economic report showed the eurozone GDP fell a revised 0.7% for the fourth quarter. The Euro Stoxx 50 Index jumped 10.3%.

In other markets, Japan's Nikkei 225 Index rallied 6.3% after the Diet approved a record budget worth 106.6 trillion yen (US$976 billion) for the fiscal year starting on April 1 and a report showed the economy expanded a revised 2.8% in the fourth quarter. China's CSI 300 Index slid 3.1% as Chinese interest rates rose and the government set a modest growth rate of above 6% for 2021. The S&P/ASX 200 Accumulation Index added 4.3% as company earnings for the period ending December 31 exceeded expectations, the jobless rate fell below 6% and a report showed the economy expanded a higher-than-expected 3.1% in the December quarter. The MSCI Emerging Markets Index edged up 1.9% in US dollars on the better outlook for the world economy.

Index movements and stock contributors and detractors are based in local-currency terms unless stated otherwise.

Outlook

Investor risk appetite remained unusually high in the March quarter. In the US, Biden signed into law a massive stimulus and Democrats positioned for further fiscal stimulus via their infrastructure package. Despite increased concerns among investors of rising inflationary pressures, the Federal Reserve signalled that it did not expect to raise rates for another couple of years. Against this backdrop, the vaccine rollout supports upbeat economic growth.

The virus that causes the illness known as covid-19 further mutated over the quarter, highlighting the risk that current vaccines could be rendered ineffective. In this scenario, economic activity would be hindered for two to three quarters as replacement vaccines are sought. The fund believes there is more uncertainty around the timing of severe mutation, rather than whether this mutation occurs at all.

Equity returns over the next 18 months are challenging to predict and position for, as there are two different scenarios that the fund thinks are each equally likely.
The first scenario sees continued strong equity returns. This scenario would be underpinned by uninterrupted vaccine rollouts, economic reopening and no change to accommodative fiscal and monetary policy settings. In this scenario, cyclical equities and 'meme' stocks would perform well, despite rising bond yields.

The second scenario is a correction of at least 20%. This may be triggered by an escaped mutation, a perceived or actual shift in Fed policy due to rising inflation risks, a bursting of the meme stock bubble or perhaps another 'black swan' event. The fund observes many warning signs of an elevated risk of a market drawdown, including a 'fear of missing out' among many investors.

The portfolio reflects these contrasting scenarios. To benefit from the scenario of strong equity returns, the fund has reduced cash from 8% to 6% and increased the portfolio's combined risk ratio to 0.76. The fund's inbuilt defensive bias helps protect against the second scenario, but the fund has also limited its exposure to stocks that would be hampered most by a virus mutation or higher interest rates.

The portfolio is not exposed to meme stocks and prefers the power of compounded returns offered by long-term structural growth and attractively priced defensives over relatively fully valued cyclical stocks. The fund has high conviction that the relatively large amount of value apparent in defensive equities will be realised within the investment horizon of three to five years, but low conviction making this prediction over a shorter time frame. It's worth noting that the operational performance of the portfolio's companies has been strong.

Availability

Product Name	APIR Code
AMP Flexible Super - Super	AMP1844AU
AMP Flexible Super - Retirement	AMP1848AU
CustomSuper	AMP1828AU
Flexible Lifetime - Super	AMP1828AU
Flexible Lifetime - Allocated Pension	AMP1832AU
Flexible Lifetime - Investments (Series 2)	AMP2041AU
SignatureSuper	AMP1836AU
SignatureSuper - Allocated Pension	AMP1840AU

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