

# Quarterly Review

Bottoms Up – celebrating stock selection

March 2018

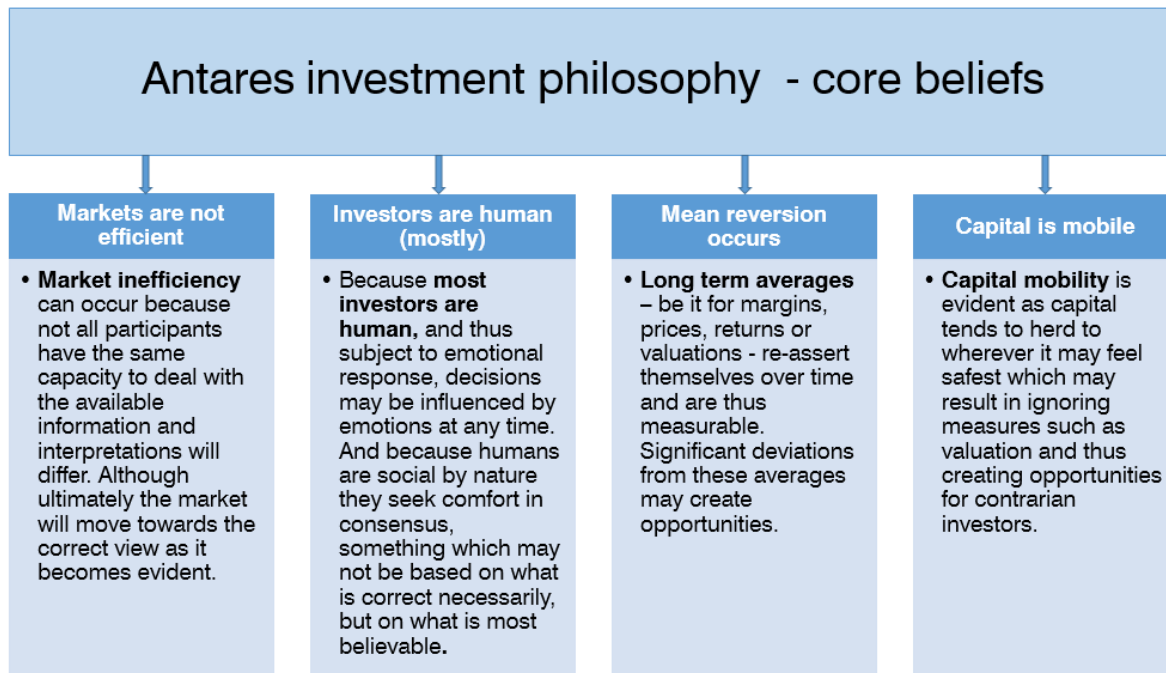


Typically over 100% of alpha in Antares’ portfolios is from stock selection. Our approach is, and always has been, bottom-up stock picking. A consistent process and detailed, quality research executed by a highly experienced team underpin this process.

Generating alpha from stock selection is where we believe our portfolios provide both a contrast and complement to portfolios derived from index or from style investing.

We believe that markets misprice stocks and our proven research process can identify them.

This paper seeks to explain how we do this and why we believe bottom-up delivers alpha.



## How does Antares identify mispricing opportunities?

This is a result of the quality of the Antares research team and the application of our proprietary research process which entails fundamental, bottom-up stock analysis. Our team of eight analysts spend about 70% of their time researching stocks.

We believe a strong, diverse and experienced investment team is important. Our investors must be courageous enough to go against the crowd and have the strength of conviction in what they are doing. Diversity of thought and background prompt us to question the status quo.

Experience assists in understanding the market’s likely response to company announcements and earnings updates, which we are then able to exploit. Co-heads Glenn Hart and Nick Pashias have worked together for nearly 20 years and all five portfolio managers have been with the team for over 10 years. The average tenure of the nine person investment team is more than 13 years.

By undertaking our own, independent valuation work we systematically identify contrarian opportunities by examining deviations from long term observable averages – be they returns, prices or valuations.

## Research inputs

Subject matter expertise is developed by arranging the investment team by industry.

Analysts use information sourced from but not limited to:

<b>Company financials</b>	<b>Industry data</b>
Company presentations	Industry contacts
Company sustainability reports	Regulatory environment and outlook
Company meetings (last year Antares analysts made over 600 meetings with companies)	Broker research
General reading and research	

## Using our research to build company models

Analysts build company models using the information they have sourced. Their models address the following key factors about each company:

- its business model and the ability of its executives and directors to execute it;
- its capital structure;
- its future cash flows and the costs associated with generating those cash flows (capital intensity);
- the returns the business may generate and compare these to its history;
- the risks associated with these future cash flows and how they can be mitigated.

Our modelling is proprietary, and utilises a common valuation model template with certain standardised valuation parameters - equity risk premium; stock beta; risk free rate and terminal growth rate.

Each model needs to be constructed from first principles by the stock's analyst. This ensures that the analyst for each company has a solid understanding of the key drivers in a business' valuation.

Stock research is consolidated in our information system that integrates all aspects of the equities investment process. All team members have full access to the system, meaning that knowledge is easily and proactively shared.

### Company valuations and stock ratings

After modelling the company, analysts are then required to set a target price. The target price represents an analyst's best estimate of the share price of the stock in 12 months' time. It is derived from the stock research process previously described.

Analysts may use the valuation, or, if they think it appropriate, they may use another methodology, such as based on multiples or sum of the parts.

As a risk control in setting target prices, both target price and valuation are published on our information system, hence any variation is easily scrutinised by our team and needs to be justified by the analyst.

Every time an analyst posts a new target price, our system requires that discussions take place about any Environmental, Sustainability and Governance issues and our ESG "traffic lights" are refreshed for that company.

Each new target price is presented to the equities team in the next morning meeting for peer review and communication. This includes presentation of modelling assumptions and output as well as differences between our estimates and market consensus.

When a new target price is set, a Stock Rating is automatically assigned which reflects the stock's expected absolute return over the next 12 months, based on the difference between the current share price and the analyst's target price. The rating reflects our belief that stocks move towards their underlying valuations over the longer term, and that stocks with the greatest discount to valuation are therefore likely to deliver the highest returns. Each stock is rated from A (highest) to E (lowest) based on its expected 12 month return.

**Table 1: Antares stock ratings**

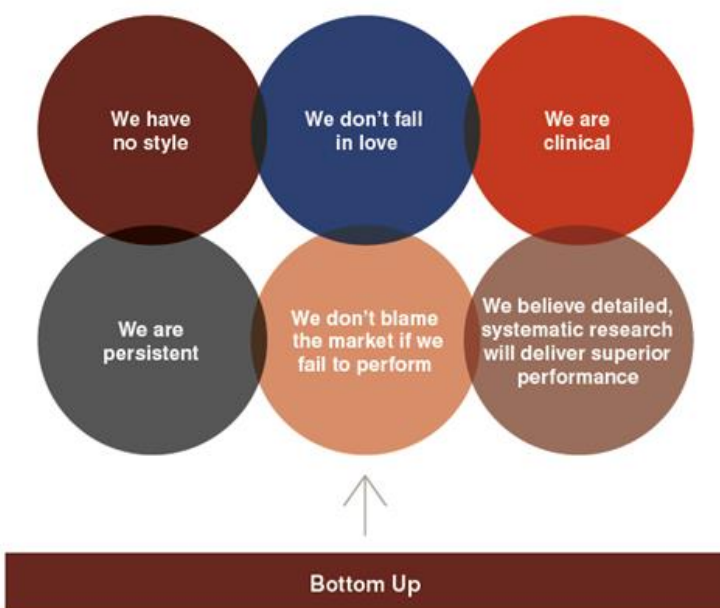
Antares stock rating	
A	Expected return greater than 25%
B	Expected return between 15% and 25%
C	Expected return between 5% and 15%
D	Expected return between -5% and 5%
E	Expected return below -5%

### Team approach and peer review

All our stock research work is peer reviewed. Peer review is ongoing but formally occurs when new target prices are set and at quarterly research meetings which include the entire investment team as well as representatives from our performance and risk teams.

Analysts are expected to attend a minimum number of meetings with the companies they cover and provide formal valuations plus "mark to market" updates each year.

# The Antares research rules



## Selecting stocks for our portfolios

Portfolio managers will look to be invested into a diversified portfolio of highest rating stocks subject to each strategy's guidelines and risk appetite. Portfolio construction processes differ according to the strategy.

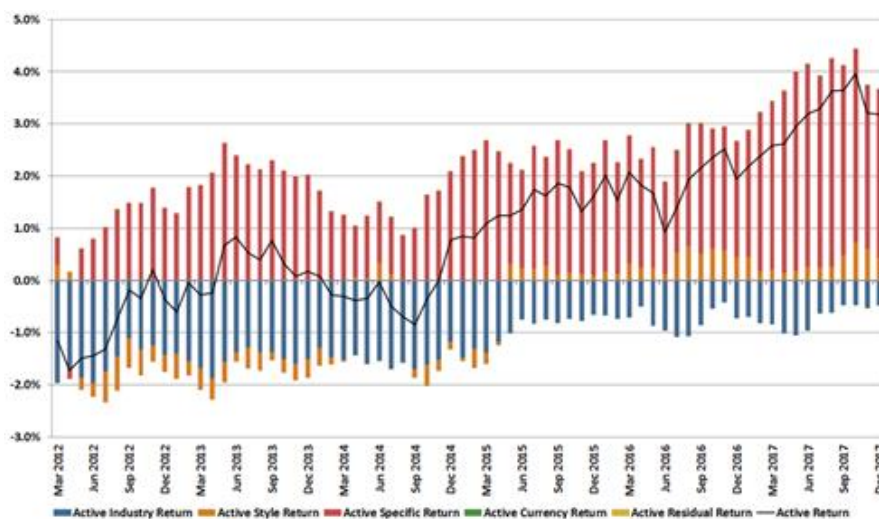
Stock selection is a direct outcome of our research effort and our process. Portfolio Managers will generally target investments in our highest rated stocks and generally avoid (or have below-index exposure to) stocks rated D & E. This strategy is implemented subject to appropriate portfolio diversification, portfolio risk constraints and guidelines.

This is a broad guide to the approach taken to portfolio construction at Antares. Any size, style or sector bias is an outcome of bottom-up research and valuation.

## Does it work?

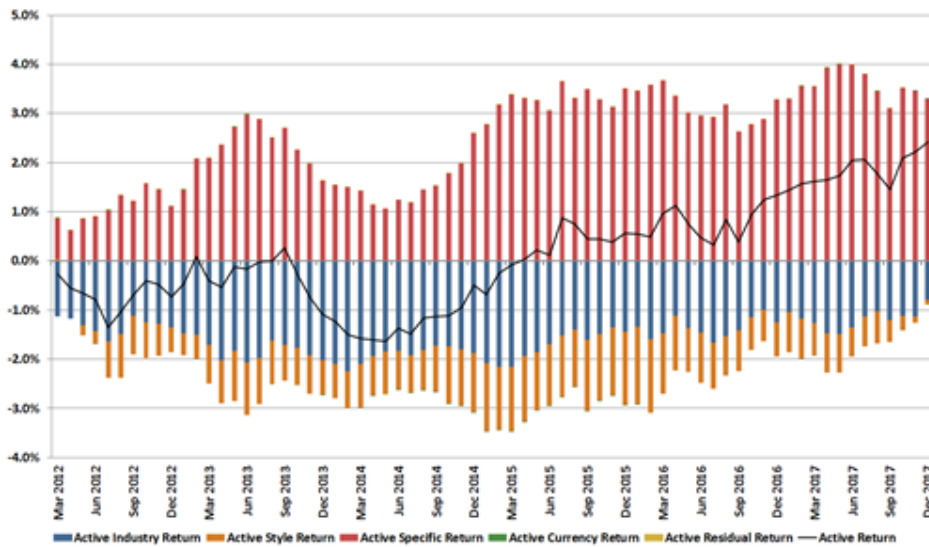
The attribution charts show that bottom up stock selection that results in stock specific alpha, labelled "Active Specific Return", is the key performance driver across our range of Australian Equities strategies. And in markets with elevated PE dispersion and a return to volatility, as we are currently experiencing, we believe that retaining a focus on bottom-up stock selection and implementing a disciplined, consistent, style agnostic strategy is even more important.

Chart 1: Antares High Growth – Rolling 3 year active return attribution



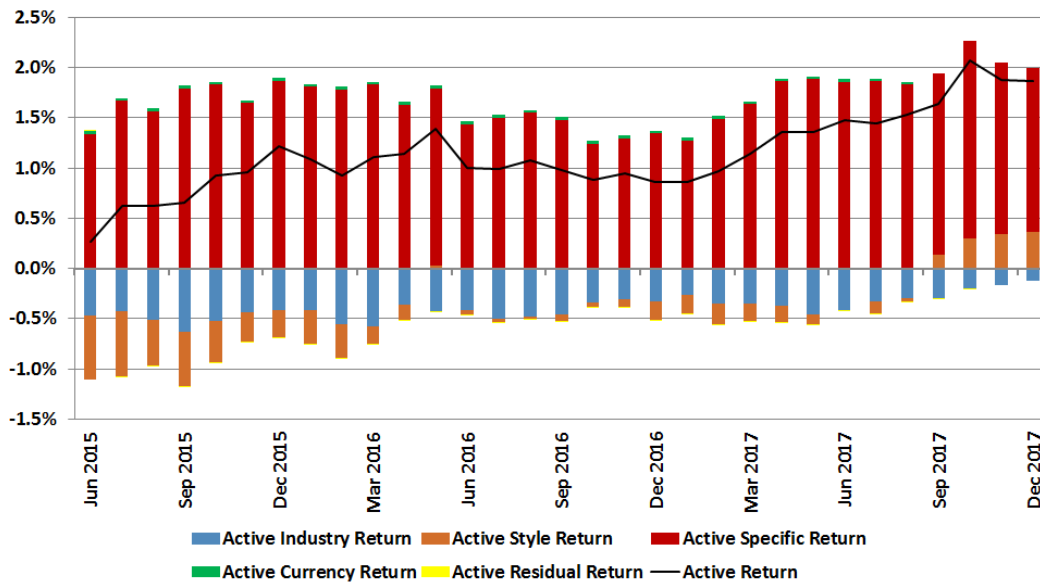
Source: MSCI Barra, Antares Equities

Chart 2: Antares Elite – Rolling 3 year active return attribution



Source: MSCI Barra, Antares Equities

Chart 3: Antares 50 Leaders – Rolling 3 year active return attribution



Source: MSCI Barra, Antares Equities

## Antares market & fund updates

Below is a brief review of how the Australian share market performed during the quarter as well as short commentaries on each Antares Fund, outlining their net performance and the main contributors to performance.<sup>#</sup>

### Australia share market review

A volatile March quarter saw major global markets post negative returns. Australia was no exception. After a positive start to the year on the back of encouraging economic and business conditions, the US market fell sharply in early February on fears that the recovery in wage growth could fuel inflation. The jitters were contagious and the Australian market experienced some wild intra-month swings despite a generally positive reporting season.

But despite the solid economic outlook and confirmation that Australia was to be exempted from new US tariffs on steel and aluminium, the Australian market (S&P / ASX 200 Accumulation Index) finished March down by 3.8% and by 3.9% for the quarter. Fallout from the global trade tensions between the US and China, together with negative sentiment toward banks arising from the Royal Commission on misconduct within the financial system contributed to the decline.

Not surprisingly the financial sector performed poorly over the quarter (-6.9%). Telcos were weakest on increased competitive pressures (-12.83%) followed by utilities (-8.3%) and REITs (-6.4%) which suffered as investors rotated out of income sectors. Energy (-7.7%) also declined. The strongest performer was Healthcare (+6.1%) which was buoyed by strong results from CSL and ResMed as well as a takeover offer for Sirtex.

### Australian Equities Fund

The Antares Australian Equities Fund returned -5.4% (net of fees) for the March quarter, underperforming its benchmark S&P/ASX 200 Accumulation Index return of -3.9% by 1.5%. The main contributors to quarterly performance relative to the benchmark were overweight positions in Rio Tinto, Ansell and cash. The main detractors from relative performance were an overweight position in Tabcorp, an underweight position in CSL and the decision not to hold a position in A2 Milk, of which both the latter performed well.

### Dividend Builder

Antares Dividend Builder delivered a return of -6.4% (net of fees) for the March quarter, underperforming the benchmark S&P/ASX 200 Industrials Accumulation Index return of -3.8% by 2.6%. The main contributors to quarterly performance relative to the benchmark was an overweight position in cash and underweight positions in CBA and Amcor. The main detractors from relative performance were overweight positions in Tabcorp and Fletcher Building and the decision not to hold a position in CSL.

### Elite Opportunities Fund

The Antares Elite Opportunities Fund delivered a return of -4.4% (net of fees) for the March quarter, underperforming the benchmark S&P/ASX 200 Accumulation Index return of -3.9% by 0.5%. The main contributors to quarterly performance relative to the benchmark were the decision not to own CBA and overweight positions in Qantas and Computershare. Detracting from relative performance was the decision not to hold a position in CSL along with overweight positions in Vocus and Tabcorp.

### High Growth Shares Fund

The Antares High Growth Shares Fund returned -2.3% (net of fees) for the March quarter, outperforming its benchmark S&P/ASX 200 Accumulation Index return of -3.9% by 1.6%. Contributing positively to quarterly performance relative to the benchmark were overweight positions in Computershare, Qantas, CSL and ResMed. The main detractors from relative performance were being underweight A2 Milk and overweight positions in Tabcorp and Janus Henderson.

### Australian Shares Fund\*

The Antares Australian Shares Fund delivered a return of -5.3% (net of fees) for the March quarter, underperforming the benchmark S&P/ASX 200 Accumulation Index return of -3.9% by 1.4%. The main contributors to quarterly performance relative to the benchmark were overweight positions in Rio Tinto, Ansell and cash. The main detractors from relative performance were an underweight position in CSL and the decision not to hold a position in a2 Milk, both of which performed well, and an overweight position in Tabcorp.

### Listed Property Fund

The Antares Listed Property Fund delivered a return of -6.9% (net of fees) for the March quarter, underperforming its benchmark S&P/ASX 200 A-REIT Accumulation Index return of -6.4% by 0.5%. Positively contributing to quarterly performance relative to the benchmark were overweight positions in cash and Peet and an underweight position in Mirvac. The Fund's relative performance was negatively impacted by an underweight positions in Goodman Group, a decision not to own Cromwell Property and an overweight position in Iron Mountain.

<sup>#</sup>All returns are net of fees. Please refer to page 6 for a summary of returns which are gross of fees.

\*Closed to new investments

# Antares Investments Returns

Performance to 31 March 2018<sup>1</sup>

		3 mths %	1 yr %	3 yrs % pa	5 yrs % pa	10 yrs % pa	Since inception % pa
<b>Australian Equities</b>							
	Net return <sup>2</sup> %	-5.4	0.6	3.4	6.9	5.8	9.4
<b>Australian Equities Fund</b>	Gross return <sup>3</sup> %	-5.2	1.4	4.3	7.8	6.8	10.3
Inception Date: 03/07/1995	Benchmark return %	-3.9	2.5	3.8	7.7	5.4	9.2
	<b>Net excess return %</b>	-1.5	-1.9	-0.4	-0.8	0.4	0.2
	<b>Gross excess return</b>	-1.3	-1.1	0.5	0.1	1.4	1.1
	Net return <sup>3</sup> %	-6.4	-5.5	0.5	7.0	7.4	7.3
<b>Dividend Builder</b>	Gross return <sup>4</sup> %	-6.3	-4.9	1.1	7.7	8.0	7.9
Inception date: 06/09/2005	Benchmark return %	-3.8	-0.4	2.9	8.8	7.3	7.4
	<b>Net excess return %</b>	-2.6	-5.1	-2.4	-1.8	0.1	-0.1
	<b>Gross excess return</b>	-2.5	-4.5	-1.8	-1.1	0.7	0.5
	Net return <sup>3</sup> %	-4.4	3.6	5.3	8.4	7.1	10.8
<b>Elite Opportunities Fund</b>	Gross return <sup>4</sup> %	-4.2	4.3	6.0	9.1	7.9	11.6
Inception date: 18/11/2002	Benchmark return %	-3.9	2.5	3.8	7.7	5.4	9.0
	<b>Net excess return %</b>	-0.5	1.1	1.5	0.7	1.7	1.8
	<b>Gross excess return</b>	-0.3	1.8	2.2	1.4	2.5	2.6
	Net return <sup>3</sup> %	-2.3	7.8	6.1	9.4	7.2	10.9
<b>High Growth Shares Fund</b>	Gross return <sup>4</sup> %	-1.9	9.0	7.3	10.6	8.4	12.5
Inception date: 07/12/1999	Benchmark return %	-3.9	2.5	3.8	7.7	5.4	7.9
	<b>Net excess return %</b>	1.6	5.3	2.3	1.7	1.8	3.0
	<b>Gross excess return</b>	2.0	6.5	3.5	2.9	3.0	4.6
	Net return <sup>3</sup> %	-2.8	12.4	-	-	-	12.4
<b>Ex-20 Equities Strategy</b>	Gross return <sup>4</sup> %	-2.6	13.3	-	-	-	13.3
Inception date: 27/05/2015	Benchmark return %	-3.6	9.6	-	-	-	10.2
	<b>Net excess return %</b>	0.8	2.8	-	-	-	2.2
	<b>Gross excess return</b>	1.0	3.7	-	-	-	3.1
	Net return <sup>3</sup> %	-5.3	0.5	3.2	6.7	5.8	8.2
<b>Australian Shares Fund*</b>	Gross return <sup>4</sup> %	-5.1	1.4	4.1	7.7	6.7	9.1
Inception date: 25/01/2000	Benchmark return %	-3.9	2.5	3.8	7.7	5.4	8.0
*Closed to new investments	<b>Net excess return %</b>	-1.4	-2.0	-0.6	-1.0	0.4	0.2
	<b>Gross excess return</b>	-1.2	-1.1	0.3	0.0	1.3	1.1
<b>Listed Property</b>							
	Net return <sup>3</sup> %	-6.9	-0.5	4.8	9.8	4.2	7.9
<b>Listed Property Fund</b>	Gross return <sup>4</sup> %	-6.7	0.2	5.6	10.6	4.9	8.7
Inception date: 28/02/1994	Benchmark return %	-6.4	-0.8	5.4	10.6	3.2	7.4
	<b>Net excess return %</b>	-0.5	0.3	-0.6	-0.8	1.0	0.5
	<b>Gross excess return</b>	-0.3	1.0	0.2	0.0	1.7	1.3

Disclaimer:<sup>1</sup> Past performance is not a reliable indicator of future performance. Returns are not guaranteed and actual returns may vary from any target returns described in this document.<sup>2</sup> Investment returns are based on exit prices, and are net of management fees and assume reinvestment of all distributions.<sup>3</sup>

Gross returns are provided to show performance against the investment objective.

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