Portfolio Profile

Antares Ex-20 Australian Equities Model Portfolio
October 2018

Model description and investment return objective

The Antares Ex-20 Australian Equities Model Portfolio is an actively managed, highly concentrated portfolio of Australian equities. It invests in shares from outside of the largest 20 companies by market capitalisation that Antares identifies as having the potential to offer significant long term capital growth.

The investment objective is to outperform the Benchmark (before fees) over a rolling five year period.

Manager's commentary

It was a volatile month for nearly all financial markets in October, and equities certainly did not escape the change in sentiment that swept across the markets. The ongoing strength in the US economy is now a more tangible problem to other markets, as increasing rates of growth in the US attract liquidity, supported by increasing interest rates. Further, the impact of the trade dispute between the US and China now seems visible in the weakening of economic data from China. Finally, with the prospect of US mid term elections in early November 2018, political uncertainty also weighed, as investors sought safe havens such as gold and US treasuries. The Model Portfolio did not perform as well as we would like in the month, declining 8.9% (net of fees)[1] which was more than the decline in our benchmark of 7.1%.

Our best performer for the month was the packaging company Orora (ORA). While there was little company specific news, ORA benefitted from the defensive nature of its business – supplying packaging to consumer goods companies.

Further, there was a mild fall in some of the commodities that ORA uses to produce its packaging products, especially pulp and energy. Goodman Group (GMG) also performed well. Again, there was little specific news, however, GMG appeared to benefit from the defensive stance in the market due to its industrial property derived earnings, coupled with its very solid balance sheet, which were seen as a haven in the sell-off.

Finally, QBE Insurance Group (QBE) enjoyed a reasonable month. QBE has around 40% of its assets in the US, and so its valuation was boosted by the decline in the Australian dollar over the month. Further, increasing interest rate expectations in the US also helped sentiment towards QBE, as investors started to price in a rise in the yield on its capital base.

Our major detractor for the month was AfterPay Touch Group (APT). There were several possible reasons for its decline including the negative sentiment towards technology companies generally. Another factor was the lingering negative sentiment towards APT over regulatory questions. This was heightened by the announcement from the opposition Labor Party it would hold a Senate inquiry into the unregulated lending segment of the financial industry, including "buy now, pay later" firms such as APT. We have looked closely at the regulatory situation in our investment thesis on APT, and while we can never be certain, we believe its model to be benign. Its model doesn't currently appear to be punitive, with fees clearly disclosed, debts not enforced at law, and no impact on a customer's credit rating in the event of default. Nevertheless, there is a political aspect in this inquiry and so we are cognisant of unexpected outcomes such things can produce. We continue to believe that the long-term viability of the model is under appreciated by the market, and the opportunity available in the considerably more liberal economy of the US offers a potential far greater upside than near term regulatory risk in Australia. We note APT already has signed up over 1,000 retailers in the US in just four months of operating there, compared to 20,000 retailers in Australia in four years.

Fairfax Media (FXJ) also suffered during the month. We are slightly puzzled, given that FXJ is not expensive on a relative basis, so rising rates should have a minor effect on its valuation. We note that FXJ's real estate subsidiary Domain (DHG) produced a weak trading update, but given the FXJ share price is underpinned by the bid from Channel Nine (NEC) this does not, to us, explain the magnitude of the fall. We can only conclude that some mildly weak ratings data from NEC was the drag, coupled with a more negative view of the Australian consumer due to falling house prices, which could possibly lead to lower advertising revenues in FY 19/20.

Finally, CYBG (CYB) bank also suffered a poor month. While company specific news flow was limited, there was a general fall in European banks, given the looming budget issues in Italy. We do not currently see CYB as overly exposed to this risk as it is nearly entirely deposit funded. Also the Brexit process seems to be struggling, impacting sentiment towards British banks and property prices. But we note that CYB has very little exposure to the centre of this problem, being London and South Eastern England as its asset base is predominately located in northern England. Finally, CYB is seen as expensive to other English banks. and unlike its larger peers, has little exposure to the risks facing those same institutions. Further, it has gains to come from synergies after the successful conclusion of its merger with Virgin Money.

Portfolio facts

Inception date:	27 May 2015
Strategy size at 31 October 2018:	$65.9m
Benchmark:	S&P/ASX 200 Accumulation Index excluding the S&P/ASX 20 Accumulation Index.
Investment timeframe:	At least 5 years
No. of shares:	15 to 30

Investment returns as at 31 October 2018[1]

Period	1 month	3 months	1 year	3 years pa	5 years pa	7 years pa	Since inception pa
Net return[2] %	-8.9	-8.5	2.6	11.9	-	-	10.1
Gross return[3] %	-8.8	-8.4	3.4	12.8	-	-	11.0
Benchmark return %	-7.1	-6.6	2.0	11.5	-	-	8.8
Net excess return %	**-1.8**	**-1.9**	**0.6**	**0.4**	**-**	**-**	**1.3**
Gross excess return %	**-1.7**	**-1.8**	**1.4**	**1.3**	**-**	**-**	**2.2**

[1] 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.
[2] Performance is based on the income and market value of the Model Portfolio and is net of fees. The performance of individual portfolios may differ to the performance of the Model Portfolio due to cash flows, portfolio reweighting and timing issues.
[3] Gross returns are provided to show performance against the investment objective.

Investor profile

The Ex-20 Australian Equities SMA is designed for investors seeking an actively managed, highly concentrated portfolio of Australian securities that excludes the top 20 stocks by market capitalisation. The SMA aims to provide investors with long term capital growth.

Investment details

Minimum investment:	$20,000
Minimum additional investment:	$2,000
Income treatment:	Monthly distribution or re-investment
Administration fee:	Nil
Entry fee:	Nil
Exit fee:	Nil
Management fee:	0.75% (incl. net effect of GST) per annum

Investment guidelines and ranges

	Minimum	Benchmark Allocation	Maximum	As at 31 Oct 18
Australian shares	90%	100%	99%	97%
Cash and cash equivalents	1%	0%	10%	3%

Top 10 share holdings

as at 31 October 2018 (alphabetical order)

- Caltex Australia
- DuluxGroup
- Goodman Group
- James Hardie Industries
- Medibank Private
- Orora
- Qantas Airways
- QBE Insurance Group
- Star Entertainment Group
- Tabcorp Holdings

Stock Activity

Buys / Additions

Aristocrat Leisure (ALL) - We added a small position in Aristocrat Leisure during the month. ALL had been a stalwart in the Model Portfolio, but we sold the stock last year given concerns about its strategy to invest heavily into the digital part of its business and a belief that earnings in its core land-based business were peaking. The latter was an incorrect conclusion, and we have come to view the digital investment in a more positive light given recent research. With the share price having been weak for reasons that are unclear to us, we have added a small position back. We await ALL's full year result later in November 2018 before making any further commitment.

WorleyParsons (WOR) - We took a small position in Worley Parsons (WOR) opportunistically following its acquisition of Jacobs petrochemical business. This required a large equity raising, in which we participated. We like the acquisition, as we think it expands WOR's offering by providing further "downstream" capability. With the potential ability to provide a full suite of consulting services to the petroleum industry becoming more important to reduce costs and complexity, we see this currently as a strategically sound acquisition.

Sales / Reductions

Orica (ORI) - We sold our position in Orica (ORI) as further information came to light about the underperformance of its Western Australian joint venture, Burrup. With the WA market facing oversupply in the near term, we feel it may be hard for ORI to make the plant profitable, even after production comes on-line as planned, due to pricing pressure. We have also lost patience with ORI's management, given that the business seems to face recurring issues in its production facilities. We wonder if ORI may have been underspending on essential capital expenditure, thus potentially requiring a catch-up sometime soon.

About Antares

Antares is a dedicated asset management business managing more than $36.1bn on behalf of Australian investors, with $6.4bn in Australian equities and more than $29.7bn in fixed income (as at 30 September 2018).

At Antares we are wholly focused on delivering performance for investors through an investment approach underpinned by dedication, experience and discipline. We recognise and are ready for market uncertainty, and believe great performance is achieved through a focus on both risk and return. Antares consists of two divisions – Antares Equities (formerly Portfolio Partners and Aviva Investors) and Antares Fixed Income (formerly National Specialist Investment Management).

For further information please contact our Client Services Team - Toll Free: 1800 671 849

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