Ausbil Australian Active Equity Fund

Monthly investment report

May 2018

Ausbil Investment
Management Limited
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ausbil

Australian equities

Performance review

Fund performance for May 2018 was 0.76% (gross of fees) versus the benchmark return of 1.19%, as measured by the S&P/ASX 300 Accumulation Index.

At a sector level, the Fund's overweight positions in the Materials, Consumer Discretionary and Information Technology sectors contributed to relative performance. The underweight positions in the Consumer Staples, Financials, Telecommunication Services and Utilities sectors also added value. Conversely, the overweight positions in the Energy sector detracted from relative performance. The underweight positions in the Industrials, Health Care and Real Estate sectors also detracted value.

At a stock level, the overweight positions in Aristocrat Leisure, BlueScope Steel, Challenger and BHP added to relative performance. The underweight positions in Commonwealth Bank and Telstra also added value. Conversely, the overweight positions in Treasury Wine Estates, Link Group and Santos detracted from relative performance. The underweight position in Wesfarmers also detracted value.

Equity Market Review

The Australian equity market had a reasonably positive month to return 1.2% driven by earnings upgrades in the Health Care and Consumer Discretionary sectors. Globally, there was significant divergence between Developed (+0.7%) and Emerging (-3.5%) equity markets as the effects of a stronger US dollar negatively affected EM currencies. Within Developed markets, US (S&P500: +2.4%) and UK (FTSE100: +2.8%) outperformed while Europe (EURO STOXX: -1.2%) underperformed.

Domestically, small-cap stocks (S&P/ASX Small Ordinaries Accumulation Index: +3.7%) outperformed. The large-cap stocks (S&P/ASX 20 Accumulation Index: +1.2%) performed in line with the overall benchmark whilst mid-cap stocks (S&P/ASX MidCap 50 Accumulation Index: +0.1%) underperformed.

Energy was generally higher (Thermal Coal: +17.8%, LNG: +16.8%, Metallurgical Coal: +6.1%, WTI Oil: -2.2%). Metals were mixed (Nickel: +11.5%, Lead: +5.4%, Manganese: +3.0%, Cobalt: +1.7%, Aluminium: +1.5%, Copper: +1.1%, Zinc: -0.9%, Iron Ore: -2.3%, Tin: -3.2%). Precious metals (Silver: +1.1%, Platinum: +0.5%, Gold: -1.2%).

Health Care (+5.5%) outperformed with strong earnings upgrades in the Pharmaceutical & Biotech (+9.0%) sector. Consumer Discretionary (+5.3%) was supported by strong fundamentals in Casinos & Gaming (+5.2%) and a re-rate in Retailing (+3.2%). Metals & Mining (+3.5%) outperformed due to supportive commodity prices but Construction Materials (-5.7%) and Chemicals (-6.9%) underperformed. Real Estate (+2.7%) and Industrials (+2.0%) also outperformed. The underperforming sectors included Telecommunication Services (-10.1%), Insurance (-1.4%) and Banks (-1.0%).

Economic review

Equity Market Outlook

June is the last month of trading updates and 'confessions' as companies review their 2018 fiscal year trading results prior to the June 30 balance date. We then move into the blackout period and await full-year results in the August reporting season. Better than expected commodity prices continue to underpin earnings growth for Resource (Energy and Metals & Mining) companies which have implemented cost rationalisation and deleveraging programmes. In addition, companies exposed to the Resources sector supplying labour, equipment and servicing are also expected to benefit from the thematic. Elsewhere, high quality companies in the Information Technology, Health Care, Consumer Staples and Consumer Discretionary sectors with strong offshore franchises are also expected to extend their outperformance.

Fund Strategy

During the month, the Fund increased positions in the Energy, Insurance and Chemicals sectors. Positions were trimmed in Consumer Discretionary. Overall positioning continues to favour a growth tilt with overweight positions in Materials and offshore earners, whilst maintaining underweight tilts to interest rate sensitive sectors such as Real Estate Investment Trusts and Utilities.

Consensus EPS estimates for the S&P/ASX 300 Index forecast earnings growth at +8.4% for FY18 and +8.9% for FY19.The market is now offering PE valuations of 16.2x and 14.8x for FY18 and FY19 respectively, with a dividend yield of 4.3%.

Economic Review

Brent oil touched US$80, political uncertainty whipsawed global bonds and the rebound in the US dollar has started to impact the peripheral Emerging Markets. President Trump re-confirmed the meeting with the North Korea for June 12th and China and the US agreed not to engage in a trade war for now. The US announced their withdrawal from the Iran nuclear deal and imposed tariffs on steel and aluminum imports from Canada, Mexico and the European Union. The Five Star Movement and Lega Nord parties formed a coalition government to the final satisfaction of the Italian President. The Spanish Prime Minister was forced out of office by a no-confidence vote.

The Federal Open Market Committee (FOMC) minutes confirmed the official policy of allowing a temporary period of inflation overshoot, expecting it to anchor "longer-run inflation expectations" at 2%. Eurozone Q1 GDP growth eased to a sustainable 2.5% pace and Japan's Q1 growth turned negative on softer private capital investment.

The Federal 2018/19 Budget announced tax cuts for low to middle income earners to offset ongoing fiscal drag. Budget forecasts are under-estimating the contribution from higher commodity prices in driving a faster and larger return to fiscal surpluses. APRA announced a lifting of the 10% speed limit on property investor loan growth from July 1st 2018.

Economic outlook

Economic Outlook

2018 will see ongoing synchronised global growth at a robust 3.9% plus pace compared to the post crisis period 3.3% average. The US economy accelerates to 2.7-3% as fiscal policy drives a capex investment boom. The Eurozone consolidates at 2.3%, Japan maintains a positive output gap growing at 1.4% and China remains focused on a 'high quality' growth in achieving their 6.5% target.

Cash rates and bond yields continue to rise at a modest and gradual pace. The US Federal Reserve will hike for a second time on June 14th and then be on hold for a possible third hike on December 20th. On auto pilot there is ongoing 'quantitative tightening' as US480bn bonds mature in 2018 and US600bn in 2019 and 2020 respectively. The European Central Bank extends QE to Q2 2019 from Q3 2018, with the volume reduced in quarterly stages from €30bn per month to zero. The Bank of Japan is expected to shift its target bond yield rate later this year and in 2019.

US dollar appreciation leads to a modest tightening in financial conditions and the Euro depreciates on ongoing QE. The currency and rate adjustments should see Developed equity markets outperform while the peripheral EM underperform. The risk of contagion flowing into the core EM seems limited, but is a risk requiring monitoring.

Australia's GDP is forecast at 2.7-3%, the unemployment rate lower to 5.1% and core inflation at 2% in 2018. Broadening growth, positive wage growth and inflation outcomes should see a tightening cycle, the timing of which has been pushed out to Q3 2019 from Q4 2018. Reflecting the themes echoed by RBA board members, noting that (1) the next move will be up, but not just yet; (2) the Reserve Bank should be a source of stability and confidence; and (3) the expected slowing in housing credit growth from tightening mortgage lending standards. Meanwhile the rates on hold policy should place downward pressure on the AUD as the interest rate differential moves further in favour of the US. The currency is forecast to test the lower range of 72-78 cents before closing at 75 cents by year end 2018 and the same for 2019.

Fund overview

Fund return

Period	Fund Return %		Bench-mark[1] %	Out/Under Performance %	
	Gross	Net		Gross	Net
1 month	0.76	0.69	1.19	-0.43	-0.50
3 months	1.46	1.25	1.10	0.35	0.15
6 months	5.85	5.42	2.93	2.92	2.49
FYTD	13.82	12.99	9.74	4.08	3.24
CYTD	2.52	2.17	1.05	1.47	1.12
1 year	13.59	12.68	9.99	3.61	2.70
3 years pa	8.11	7.24	6.06	2.05	1.18
5 years pa	10.79	9.89	8.78	2.02	1.12
7 years pa	9.97	9.08	8.18	1.80	0.90
10 years pa	6.99	6.11	5.12	1.87	0.99
15 years pa	12.12	11.17	9.36	2.76	1.80
Since inception pa Date: July 1997	11.29	10.30	8.21	3.07	2.09

Top Ten Stock Holdings

Name	Fund %	Index[1] %	Tilt %
BHP	8.84	6.34	2.50
Westpac Bank	6.66	5.71	0.95
CSL	6.21	5.07	1.14
Santos	5.22	0.62	4.60
ANZ Bank	4.95	4.79	0.16
Commonwealth Bank	4.75	7.35	-2.60
BlueScope Steel	4.67	0.59	4.08
QBE Insurance	3.78	0.78	3.00
National Australia Bank	3.48	4.39	-0.91
Aristocrat Leisure	3.45	1.15	2.30

Fund Sector Tilts

Name	Fund %	Index[1] %	Tilt %
Energy	7.20	5.47	1.73
Materials	31.31	18.65	12.66
Industrials	5.53	7.47	-1.94
Consumer Discretionary	5.67	4.97	0.70
Consumer Staples	5.49	7.87	-2.38
Health Care	6.21	8.43	-2.22
Financials	29.81	32.14	-2.33
Information Technology	5.14	2.40	2.74
Telecommunication Services	0.00	2.42	-2.42
Utilities	0.00	1.95	-1.95
Real Estate	2.88	8.24	-5.37
Cash	0.77	0.00	0.77
Total	**100.00**	**100.00**	**0.00**

1. The benchmark is S&P/ASX 300 Accumulation Index.

Fund activity

Fund activity

Major Purchases and Sales

Purchases	Sales
Nufarm	Nil

The Fund purchased a holding in Nufarm during May. No positions were sold during the period.

Nufarm Limited (NUF) is one of the world's leading crop protection and specialist seeds companies. The company produce products to help farmers protect their crops against damage caused by weeds, pests and disease. NUF have manufacturing and marketing operations based in Australia, New Zealand, Asia, Europe and the Americas. Recent acquisitions in Europe are improving the overall quality of the business and Omega-3 offers significant longer-term growth.

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