

Lonsec Listed Managed Portfolio – Diversified

ISSUE DATE: 28-4-2017

Performance review

Model portfolios

RETURNS TO 31 MARCH 2017	SECURE	DEFENSIVE	CONSERVATIVE	BALANCED	GROWTH	HIGH GROWTH
3 MONTHS (%)						
MODEL PORTFOLIO	0.4	1.2	1.9	2.1	2.7	3.4
PEER GROUP BENCHMARK	0.4	1.2	1.3	1.9	2.2	2.7
EXCESS RETURN	0.0	0.0	0.6	0.2	0.5	0.7
6 MONTHS (%)						
MODEL PORTFOLIO	0.9	0.9	2.1	3.3	4.8	6.5
PEER GROUP BENCHMARK	0.9	1.2	1.6	3.6	4.7	6.2
EXCESS RETURN	0.0	-0.4	0.5	-0.3	0.2	0.3
1 YEAR (%)						
MODEL PORTFOLIO	1.9	4.4	6.9	8.8	11.3	14.0
PEER GROUP BENCHMARK	1.9	4.1	4.7	7.9	9.4	12.1
EXCESS RETURN	0.0	0.3	2.2	0.9	1.9	1.9
3 YEARS (%)						
MODEL PORTFOLIO	2.3	5.4	6.8	7.6	8.3	9.2
PEER GROUP BENCHMARK	2.3	3.7	4.1	5.5	6.3	7.4
EXCESS RETURN	0.0	1.7	2.7	2.2	2.0	1.8
5 YEARS (%)						
MODEL PORTFOLIO	2.6	5.8	7.8	9.5	11.2	12.8
PEER GROUP BENCHMARK	2.6	4.4	5.1	7.1	8.4	9.3
EXCESS RETURN	0.0	1.4	2.7	2.4	2.9	3.5
SINCE INCEPTION (%) - DECEMBER 2010						
MODEL PORTFOLIO	3.1	5.6	6.9	7.6	8.6	9.3
PEER GROUP BENCHMARK	3.1	4.4	4.9	6.1	7.0	7.6
EXCESS RETURN	0.0	1.2	1.9	1.5	1.6	1.7

Past performance is not a reliable indicator of future performance. The Model Portfolios are notional portfolios. No real portfolios exist under Lonsec management. Model Portfolio performance is calculated after management fees and before taxes.

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Overview of the Quarter

The continuation of the Australian equity market rally was readily evident throughout the March Quarter with the S&P/ASX 300 TR Index up 4.71% as reflation trades drove the prices of equities domestically. Retrospectively, Q1 2017 can largely be seen as a risk-on quarter driven by solid performance from Financials (and especially the 'Big 4'). Despite concerns over housing affordability and levels of household debt, the cash rate remained constant at 1.50%, with core inflation a focus of the RBA.

In the US, the Trump rally continued in Q1, with the S&P 500 rising 5.53% on the back of the 'reflation' trade. However, this rally seems to be showing signs of stalling, with market sentiment appearing to decline due to the policy roadblock facing President Trump in Washington. Within Europe, political uncertainty continued to dominate headlines over the quarter with a number of elections, including France and Germany, along with a progressing Brexit having the potential to alter the landscape significantly. Nonetheless, despite the uncertainty and some 'doom and gloom' towards the close of the quarter, the Eurostoxx 50 gained a robust 6.80% in Q1 2017. The Emerging Markets benchmark also rallied during the quarter (+5.78%) with most of the gains coming during the month of March (+3.33%) in Australian dollar terms. Asia ex-Japan contributed strongly to aggregate Emerging Market gains with the respective benchmark up 7.63% for the quarter and 4.08% for the month of March alone.

The A-REIT sector was flat (-0.1% total return) during the first three months of 2017, underperforming the broader Australian equities market with most of the large retail stocks (Westfield, Scentre and Vicinity all down 4-5%) holding the A-REIT index back. G-REITs continue to underperform broader markets due to expectations for higher interest rates, especially in the US where investors remain focused on whether the Trump administration can deliver on promised changes to tax rates, de-regulation in banking and energy, as well as boost infrastructure spending. The G-REIT benchmark rose 1.2% over the March quarter.

Both domestic and global fixed income markets rose during the quarter, up 1.2% and 0.7% respectively. Domestically, Australian bonds offer an attractive yield compared to similarly rated countries and this has seen their popularity remain high among investors. Australian corporate bond spreads have continued to narrow since January. Issuance remained strong in Q1 with \$59 billion worth of local bond issuance into the primary market (\$24 billion in March alone),

while Kangaroo issuance has totaled approximately \$12 billion. The 10 year US treasury yield finished the quarter at 2.40% following the Fed's decision to raise rates by 25 basis points in March whilst indicating any further rate hikes would be 'gradual' and projecting two further hikes in 2017. Domestically, the RBA kept rates on hold over the quarter at 1.50% and 10 year bonds finished Q1 2017 hovering around 2.38%.

Relative return at the model portfolio level was positive for the quarter, as all models either outperformed or performed in line with the peer group benchmark. Strong absolute and relative returns were recorded by the majority of Australian and global equities managers used within the model portfolios.

Overview of the Year

The Australian equity market finished the 12 months to March 2017 in positive territory, returning 20.2%, outperforming global equities which returned 15.9% (in Australian dollar terms). A recovery in commodity prices, post-election optimism and the rotation from 'bond proxy' and defensive equity sectors such as healthcare, infrastructure and property have all been key drivers of equity market returns over the previous 12 months. Domestically, small caps underperformed the broader market, returning 13.7% for the 12 months to March 2017.

Australian and global REIT markets continued to produce positive 12 month absolute returns (6.3% and 3.9% respectively), despite the Q1 selloff which carried over from late 2016. Despite solid fundamentals, particularly in Australia (low vacancy, effective rental growth in major markets), bond-proxy stock prices, including REITs, were significantly driven by global bond and cash rates in 2016. This is expected to continue as we move further into 2017 with markets keeping a close eye on Trump's pro-growth agenda and expecting multiple moves by the Fed.

Domestic fixed interest markets returned 2.1% for the year. In Australia, inflation remains well below the RBA target, adding to some downward pressure in rates. Stronger than expected growth at the end of 2016 was supportive of Australian yields throughout early 2017. Australian Government bonds continued to be popular with investors, given higher relative yields compared to similarly rated countries. In global markets (+2.2%), the key themes dominating the past 12 months continued to be diverging monetary policy, macroeconomic uncertainty and implementation of negative interest rates being employed by various central banks.

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Relative return at the model portfolio level was positive for the year, as all models either outperformed or performed in line with the peer group benchmark. Strong absolute returns were recorded by the Australian and global equities managers used within the model portfolios.

Australian Equities - fund contributions

RETURNS TO 31 MARCH 2017	3 MTHS	6 MTHS	1 YR	3 YRS*
LONGSEC AUSTRALIAN EQUITY CORE MODEL PORTFOLIO	6.2	8.1	18.2	7.3
S&P/ASX 300 TR INDEX AUD	4.7	9.9	20.2	7.5

* annualised

Note: Current portfolio funds shown above. Not all funds have been in the structure since inception.

Australian equities returned 4.7% for the March quarter on the back of a rally in the Resources sector as commodity and energy prices pressed higher. Financials also provided solid returns over the quarter, driven by significant returns from the 'big 4'. Small caps underperformed the large cap sector, returning 1.5% for the quarter.

Lonsec Australian Equity Core Model Portfolio

The Lonsec Australian Equity Core Model Portfolio outperformed the benchmark over the March quarter despite the strong rally in Financials and Resources. Key contributors to performance included CSL Limited, Computershare Limited and Challenger Financial Ltd. Stocks that detracted the most from performance over the quarter included Brambles Limited, BHP Billiton and Ansell Limited. The main overweight positions within the portfolio are Health Care, Industrials, Information Technology and Consumer Staples while the main underweight exposures are Resources, A-REIT's, Financials, Consumer Discretionary and Telecommunications.

The Manager's investment themes are: inflation and interest rate environment to persist, global growth outlook to gradually increase led by the US, Asian growth in transition, global population ageing, middle class growing and becoming more mobile and competition increasing from globalisation and technology. Recent portfolio changes seek to reduce defensive exposure and increase exposure to growth and/or higher interest rates.

Global Equities - fund contributions

RETURNS TO 31 MARCH 2017	3 MTHS	6 MTHS	1 YR	3 YRS*
MAGELLAN GLOBAL EQUITIES FUND	1.4	7.5	10.4	-
VANGUARD ALL-WORLD EX-US SHARES INDEX ETF	2.9	6.9	14.9	7.9
MSCI AC WORLD EX AUSTRALIA NR INDEX AUD	1.4	8.4	15.9	12.3

* annualised

Note: Current portfolio funds shown above. Not all funds have been in the structure since inception.

Despite an uncertain macroeconomic and political backdrop, global equities gained 1.4% over the March quarter on the back of the Trump 'reflation' trade. Emerging markets outperformed the broader benchmark, returning 5.8% for the quarter.

Magellan Global Equities Fund

The Magellan Global Fund performed broadly in line with the benchmark during the March quarter. The largest positive contributors to the performance came from investments in Apple, Facebook and Lowe's. Apple rose significantly on a better-than-expected first-quarter update that showed iPhone popularity remains high as the installed base is growing at double-digit rates and the company is seeing record numbers of people switching from Android devices. Engagement with the IOS ecosystem is increasing as App store sales grew 43% in the quarter to an all-time high. Facebook also rose after fourth-quarter revenue exceeded expectations with 51% growth. Facebook's users and engagement is growing and this is being successfully monetised via advertising revenue, particularly via mobile. Lowe's climbed after fourth-quarter results saw strong comparable store growth of 5%, driven by buoyant housing and home-improvement spending.

Over the quarter, the stocks that detracted from returns included investments in Target, Tesco and Qualcomm. Target declined following the release of the company's fourth-quarter earnings that showed comparative sales were negative over the holiday period and the company's management announced significant downgrades to earnings expectations. This was due to implementation of a strategic initiatives that will entail resetting profitability to contend with a more competitive retail environment. Tesco fell after the release of mixed trading statements from the company and the announcement of its intention to acquire UK-based food wholesaler Booker added to business complexity compared with the increased simplicity of recent years. Qualcomm slid after Apple joined those launching legal action against the

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company based on claims of unfair royalty practices regarding its baseband chips.

The manager believes macroeconomic developments are likely to remain at the forefront of concerns for equity markets, indicating the future influence of central bank policy actions will periodically dominate sentiment. Specifically, the manager believes the key risks to the global economy are balanced between an uncertain slowdown trajectory for China and Emerging Markets, stabilising Europe and a growing U.S. and as such remains cautious in terms of where to prudently place capital.

Vanguard All-World Ex-US Shares Index ETF

Based on the 31 March 2017 closing price in Australia the Vanguard All-World ex US Shares Index ETF outperformed the benchmark for the quarter. This discrepancy in performance is due to the various closing times of global exchanges on which the ETF invests. When taken from a NAV calculation the fund performed broadly in line with the benchmark.

Property and Infrastructure - fund contributions

RETURNS TO 31 MARCH 2017	3 MTHS	6 MTHS	1 YR	3 YRS*
SPDR DOW JONES GLOBAL REAL ESTATE ETF	-4.2	-3.4	-0.2	12.3
VANGUARD AUSTRALIAN PROPERTY SECURITIES INDEX ETF	0.1	-0.6	6.4	16.6
FTSE EPRA/NAREIT DEVELOPED NR INDEX (AUD HEDGED)	1.2	-1.2	3.9	9.7
S&P/ASX 300 A-REIT TR INDEX AUD	-0.1	-0.8	6.3	16.8

* annualised

Note: Current portfolio funds shown above. Not all funds have been in the structure since inception.

Both domestic (-0.1%) and global listed (1.2%) property stocks underperformed their broader equity counterparts, largely attributable to profit taking after a strong performance over the last 4-5 years, but also to the expectation of higher interest rates moving forward.

SPDR Dow Jones Global Real Estate ETF

The SPDR Dow Jones Global Real Estate ETF underperformed the FTSE global listed property benchmark over the quarter but performed broadly in line with its internal benchmark (the Dow Jones Global Select Real Estate Securities Index).

Vanguard Australian Property Securities Index ETF

The Vanguard Australian Property Securities Index ETF performed broadly in line with the benchmark over the March quarter (based on its closing price).

Fixed Interest - fund contributions

RETURNS TO 31 MARCH 2017	3 MTHS	6 MTHS	1 YR	3 YRS*
ISHARES COMPOSITE BOND ETF	1.2	-1.7	1.9	4.8
VANGUARD INTERNATIONAL FIXED INTEREST INDEX ETF (HEDGED)	0.3	-2.2	0.9	-
ANZ SUBORDINATED NOTES	0.7	1.8	4.0	4.1
AMP SUBORDINATED NOTES II	0.4	1.4	4.9	5.1
BLOOMBERG AUSBOND COMPOSITE 0+ YEAR INDEX AUD	1.2	-1.7	2.1	5.0
BLOOMBERG AUSBOND CREDIT FRN 0+ YEAR INDEX AUD	1.2	1.7	3.7	3.3
BLOOMBERG BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)	0.7	-1.5	2.2	5.6

* annualised

Note: Current portfolio funds shown above. Not all funds have been in the structure since inception.

The Fixed Interest and Income assets component of the portfolios provided positive performance over the March quarter, with the domestic market returning 1.2% and global fixed interest returning 0.7%.

AMP Subordinated Notes II

The AMP Subordinated Notes II (AMPHA) underperformed the cash benchmark over the March quarter, as its distribution yield was partially offset by a slight decline in market value.

ANZ Subordinated Notes

ANZ Subordinated Notes (ANZHA) outperformed the cash benchmark over the March quarter with a low level of volatility ahead of its upcoming maturity. ANZ have advised of its intention to redeem the Notes on 20 June 2017, at which time holders will receive \$101.15/security, being the \$100 face value plus the final interest payment of \$1.15/security. Redemption of ANZHA will provide an opportunity to extend the maturity profile of the portfolio, with a replacement security for the portfolio to be announced in due course.

iShares Composite Bond ETF

The iShares UBS Composite Bond Index Fund (IAF) performed in line with the Bloomberg AusBond Composite Index over the March quarter (based on close price).

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Vanguard International Fixed Interest Index ETF (Hedged)

Based on the 31st March 2017 closing price, the Vanguard International Fixed Interest Index (Hedged) ETF underperformed the relevant benchmark. When taken from a NAV calculation the fund performed broadly in line with the benchmark.

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3 MONTHS (%)						
MODEL PORTFOLIO	0.4	1.2	1.9	2.1	2.7	3.4
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	0.4	1.2	1.6	1.9	2.3	2.7
EXCESS RETURN	0.0	0.0	0.3	0.2	0.4	0.7
6 MONTHS (%)						
MODEL PORTFOLIO	0.9	0.9	2.1	3.3	4.8	6.5
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	0.9	1.2	2.7	4.1	5.9	7.9
EXCESS RETURN	0.0	-0.4	-0.6	-0.8	-1.1	-1.4
1 YEAR (%)						
MODEL PORTFOLIO	1.9	4.4	6.9	8.8	11.3	14.0
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	1.9	5.0	7.9	10.3	13.3	16.5
EXCESS RETURN	0.0	-0.6	-1.0	-1.5	-1.9	-2.5
3 YEARS (%)						
MODEL PORTFOLIO	2.3	5.4	6.8	7.6	8.3	9.2
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	2.3	5.7	7.2	8.6	9.7	10.7
EXCESS RETURN	0.0	-0.3	-0.4	-0.9	-1.3	-1.5
5 YEARS (%)						
MODEL PORTFOLIO	2.6	5.8	7.8	9.5	11.2	12.8
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	2.6	6.3	8.4	10.4	12.3	14.1
EXCESS RETURN	0.0	-0.5	-0.6	-0.9	-1.1	-1.3
SINCE INCEPTION (%) - DECEMBER 2010						
MODEL PORTFOLIO	3.1	5.6	6.9	7.6	8.6	9.3
LONSEC (DIVERSIFIED DIRECT) BENCHMARK	3.1	6.4	7.9	9.2	10.3	11.4
EXCESS RETURN	0.0	-0.9	-1.1	-1.6	-1.8	-2.0

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Indices used for performance comparisons and for benchmark construction:

AUSTRALIAN EQUITIES	S&P/ASX 300 TR INDEX AUD
GLOBAL EQUITIES	MSCI AC WORLD EX AUSTRALIA NR INDEX AUD
PROPERTY AND INFRASTRUCTURE	FTSE EPRA/NAREIT DEVELOPED NR INDEX (AUD HEDGED)
PROPERTY AND INFRASTRUCTURE	S&P/ASX 300 A-REIT TR INDEX AUD
FIXED INTEREST	BLOOMBERG AUSBOND COMPOSITE 0+ YEAR INDEX AUD
FIXED INTEREST	BLOOMBERG AUSBOND CREDIT FRN 0+ YEAR INDEX AUD
FIXED INTEREST	BLOOMBERG BARCLAYS GLOBAL AGGREGATE TR INDEX (AUD HEDGED)
CASH	BLOOMBERG AUSBOND BANK BILL INDEX AUD

The model portfolios change over time therefore performance is not calculated on a static mix of funds.

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