SGH Australia Plus Fund

SG HISCOCK & COMPANY

31 January 2018

Fact Sheet

Investment objective	To outperform the S&P/ASX300 Accumulation Index by 5% on a rolling 3 year basis		
Investments held	Generally within the largest 300 companies listed on the ASX, plus companies listed in Asia with a focus on Asian domestic consumption.		
Investment Manager	SG Hiscock & Company		
APIR	ETL0383AU	**Buy spread**	+ 0.25%
Commencement	8 October 2013	**Sell spread**	- 0.25%
Management costs[1]	0.70% p.a.	**Performance Fee[2]**	20% capped at 1.25% in any calendar year, subject to a highwater mark
Minimum initial investment	$20,000	**Fund size**	$9.39 million

Unit Prices as at 31 January 2018	**Purchase**	**Net Asset Value**	**Withdrawal**
	1.5614	1.5575	1.5536

Performance as at 31 January 2018[3]	**1 mth %**	**3 mths %**	**6 mths %**	**1 yr %**	**2 yrs % p.a.**	**3 yrs % p.a.**	**Incept' % p.a.**
Distribution Return	0.00	1.35	1.48	7.06	6.38	10.07	8.78
Growth Return	0.45	3.20	13.36	18.47	15.30	8.50	10.83
Total Net Return	0.45	4.55	14.84	25.53	21.68	18.56	19.61
S&P/ASX 300 Accumulation Index	-0.39	3.18	8.16	12.37	14.82	7.47	8.34
Total Net Return vs. the Index	0.84	1.37	6.68	13.16	6.86	11.09	11.27

Top 5 holdings as at 31 January 2018
National Australia Bank Limited
Macquarie Group Limited
Australia & New Zealand Banking Group Limited
CSL Limited
James Hardie Industries SE

Top 5 holdings represent 26.50% of the total Fund.

Why Australia Plus?

1. We want access to the best quality companies in Asia, at the right price. It is the choice, but not the obligation to invest in emerging companies with strong local franchises
2. The strong rise in both the sheer number of Asians entering the middle class and the growth in disposable income, suggests that this is a multi year trend that is very hard to access by restricting the investible universe to Australian listed stocks.
3. Investors appropriately diversify their portfolio by enhancing returns with a focus on the domestic demand thematic within Asia.
4. It offers Australian investors a wider opportunity set without the requirement to have money invested in Asia through a pooled vehicle.
5. By focussing purely on the domestic demand thematic in Asia, our investible universe grows by 40-50 stocks outside the ASX300. This is a very narrow subset of Asian stocks that meet our basic quality filters and would consider owning at the right price.

1. Includes estimated GST payable, after taking into account reduced input tax credits (RITC).
2. A performance fee of 20% (net GST and an estimate of RITC) of any investment return above the fund's benchmark may also be payable as expense of the fund, capped at 1.25% in any year, subject to a highwater mark
3. Performance: Total Net Return is the Fund return after the deduction of ongoing fees and expenses assuming the reinvestment of all distributions.

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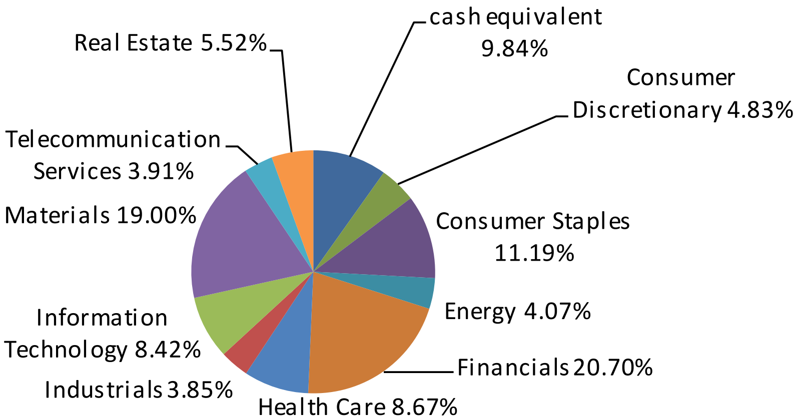
Asset allocation as at 31 January 2018



Commentary

In our December Quarterly Commentary we commented that "it is hard to think volatility will not increase from here" and that "we see the potential for a correction (say 10% down) .." Little did we think it would happen days after going to print with the VIX Index recording its sharpest one day rise in its history, and the S&P500 giving back literally all of its January gains (+5.7% and the strongest start to the year in 30 years) in the first few days of February.

The risk of a drawdown has been increasing with valuations becoming stretched, protracted extreme low volatility and extreme positioning, but identifying the trigger is not always clear, and sometimes there doesn't need to be one (as Robert Shiller reminds us). This time it seems to have been driven more by technical factors relating to the rebalancing of exchange traded volatility products rather than fundamentals. There is risk that heightened volatility leads to more short term deleveraging from other systematic trend following strategies. The tightening in financial conditions will also see an increase in risk aversion back to more normalised levels, with the result we may have seen the top in equity markets in the near term.

History shows that quarterly drawdowns of 10% or more in bull markets are not uncommon, and in fact the lack of a correction of greater than 5% in the S&P500 for such a long period of time as we have recently seen, is more the outlier. In this context some mean reversion is not unexpected, and arguably represents a return to a more normal pattern of market behaviour. Whilst unpleasant at the time, it is not something necessarily to fear. It provides an opportunity to capitalise on short term dislocations, and for active stock pickers like ourselves the potential to upgrade the portfolio with stocks we have had our eye on at lower prices.

Our base case continues to be that evidence of strong synchronised global growth and increasing earnings expectations should be positive for equities. In January global growth remained solid with the US ISM and European PMI's easing slightly and Japan strong. US equities saw upgrades as companies revised up guidance on the back of the Trump Tax Reform package announcement in December.

Australian equities underperformed global markets in January, falling 0.4%. The risk is this relative underperformance continues through 2018 given the more muted domestic earnings outlook compared to offshore. The strong commodities rally means there is still considerable upside to resource sector estimates based on spot prices, but outside this we expect the reporting season will confirm a mostly benign but constrained domestic earnings backdrop.

A rise in inflation expectations that pushes up bond yields remains the biggest risk to equities (and arguably all asset classes) given where valuations are trading relative to history. The sell off in bonds and rise in Government bond yields in January saw the US 10-year treasury yield hit 2.7%, its highest level since April 2014. The risk is when rates rise too quickly, they can weigh on growth expectations and equity valuations. This has the greatest impact on long duration assets and bond proxies. In January this was evident as the infrastructure, utility and REITs laggard the broader ASX300.

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Our working assumption is central banks increase rates gradually. But the risk is as we move through 2018 that inflation surprises to the upside versus expectations. Higher wage growth is certainly possible if growth remains strong. Couple this with higher commodity prices a scenario of rising inflationary pressures cannot be dismissed.

Portfolio Performance & positioning

The portfolio continues to be overweight companies with offshore earnings, reflective of their better relative growth prospects, and materially underweight the Major Australian banks. We made no changes to the portfolio outside existing positions during the month. The portfolio returned 0.45% in the month outperforming the ASX300 Accumulation Index by +0.84%. The fund held 11.7% in Asian equities and had 9.8% in cash at the end of January.