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Milford Unit Trust PIE Funds Monthly Review
December 2017

# Market and Economic Review

November was another good month for Milford's funds, with all seven PIE funds producing positive returns. The one year returns varied from a high of 24.6% for the Trans-Tasman Fund to a low of 9.2% for the Conservative Fund. Our two largest funds, the Active Growth and Diversified Income funds, reported returns of 15.3% and 12.2% respectively for the twelve months ended 30 November.

The majority of the funds have beat their performance benchmark (where applicable), partly because of the strong performance of several large holdings over the past twelve months. These include a2 Milk, Fisher & Paykel Healthcare, Serko and Tourism Holdings. Milford's Australian investment team has also identified several companies that performed exceptionally well.

Share markets are responding to strong economic growth throughout most of the world, with major forecasters indicating that this growth will continue into the 2018 year. The major predictions are as follows;

- The OECD is forecasting global growth of 3.7% in 2018 compared with an estimated 3.6% for 2017
- The International Monetary Fund (IMF) is also projecting world output growth of 3.7% in 2018
- The World Bank is a bit more cautious and is projecting world GDP growth of 2.9% next year, slightly above its projection of 2.7% for the current year
- Year-end broker reports are also forecasting higher levels of global growth in 2018

These forecasts, albeit they are not from the same base, are consistently optimistic. The 2019 forecasts are also optimistic.

The IMF World Economic Outlook, which was published in October, had this to say: "The global cyclical upswing that began midway through 2016 continues to gather strength. Only a year and a half ago, the world economy faced stalling growth and financial market turbulence. The picture now is very different, with accelerating growth in Europe, Japan, China and the United States".

These positive economic conditions have boosted business confidence, capital investment and company profitability. We continue to closely monitor global economic conditions and are prepared to adopt a more defensive investment strategy if there are any signs that global growth is easing.

# Milford Unit Trust PIE Funds Monthly Review as at 30 November 2017

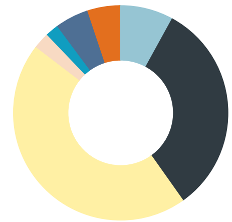
## Conservative Fund **Portfolio Manager: Paul Morris**

The Fund returned 0.8% in November, bringing the one year return to 9.2%. The broad asset classes into which the Fund is invested contributed positively again in November.

Australasian corporate bonds had a reasonable month, outperforming global peers, supported by expectations official cash rates will remain on hold for an extended period. This expectation also benefited the Fund's Australasian income shares, including notable returns of above 8% from both Charter Hall Group (Australian property) and Stride (NZ property). Global shares extended their gains but the contribution from global corporate bonds was more muted due to weakness in high yield. That served as a reminder that the extra yield from high yield bonds has contracted to less attractive levels. We have been trimming more expensive holdings and will look to further increase average Fund credit rating. The Fund's foreign currency exposure was reduced but contributed to returns on NZD weakness.

Looking forward, near term returns should remain reasonable, albeit likely lower than the last year. We remain underweight shares due to valuations but note low inflation, economic growth and slow monetary policy normalization are supportive. The biggest risk is that higher inflation precipitates faster policy tightening. To protect against this, we have limited interest rate exposure.

### Actual investment mix

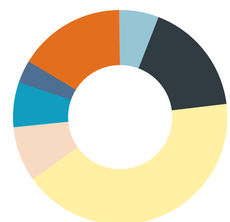



## Diversified Income Fund **Portfolio Manager: David Lewis**

November was a good month for the Fund returning 1.1%, taking the one year return to 12.2%. Performance this month was generally robust across key asset classes, with gains across both bond and shareholdings both internationally and in NZ.

The Fund's holdings in property companies performed particularly well, with the sector gaining 5.3% in Australia and 3.6% in NZ. These gains reflect continued attractive dividend yields compared to cash, as well as good operational performance for many property companies, driven by strong tenant demand for space. Key performers at the company level were Charter Hall Group (+8.8%), Stride (+8.6%), Westfield (+7.9%) and Folkestone Education (+7.1%). Contact Energy was among our weaker holdings this month, falling by 6.1% following selling from international passive funds. The Fund added modestly to its share exposure (now approximately 35%) while reducing high yield bonds (now 22%), where we continue to take profits following good performance.

Looking ahead, we still think return prospects remain reasonable especially compared to low interest rates. However, given prospects for less supportive central bank policy next year, our strategy has become more cautious, and we expect this shift to gradually continue if market valuations increase further.




## Balanced Fund **Portfolio Manager: Mark Riggall**

The Fund returned 0.9% in November, bringing the one year return to 14.4%. After strong gains in October, the pace slowed in November but markets remained broadly positive.

Global growth continues to improve but market interest rates are subdued, providing a strong backdrop for the Diversified Income Fund. The Balanced Fund's core investment into this Fund delivered the bulk of this month's performance. Global shares continue to perform well, particularly in the US on hopes that Trump will deliver tax reform. Local NZ and Australian shares were largely unchanged. Exposure to offshore currencies continues to provide a tailwind to performance as the NZD underperformed the Yen and Euro last month. The bond portfolios delivered solid returns from security selection, despite weaker corporate credit conditions and weaker government bonds.

Going forward, we are cautiously optimistic on risk assets because although global economic growth looks good, asset valuations are reasonably elevated and it is unlikely that interest rates can continue to be this low in the face of increased global growth. We remain overexposed to global shares and have reduced our holdings in NZ shares as the relative outlooks continue to diverge. Volatility is likely to pick up going forward after a benign 12 months. We have moved NZD exposure back to neutral in light of typical December strength.


## Active Growth Fund **Portfolio Manager: Jonathan Windust**

The Fund rose 0.9% during November, benefiting from rising share markets, which had good economic momentum, positive company earnings, low interest rates and in the US, the prospect of tax cuts.

Key positive company investments were Serko (+74.5%), Summerset Group (+8.4%), Origin Energy (+12.5%) and Charter Hall Group (+8.8%). Serko benefited from a positive result that demonstrated positive cash flow, strong revenue growth and a significant northern hemisphere market opportunity. Origin Energy benefited from rising oil prices and a positive investor day. The major detractor was Living Cell Technologies (-85.5%) which fell after disappointing results from trials for its Parkinson's treatment. During the month, we took advantage of weakness to increase holdings in select New Zealand shares; Fletcher Building, Contact Energy, Chorus and Spark. We also added to our Australian shares as we identified attractive opportunities.

At month end, the Fund had approximately 76% invested in shares with a higher than average weight in global shares and lower than average weight towards NZ. The outlook for shares remains supported by good economic growth, earnings and low interest rates with full valuations being the key headwind. On balance, we believe share markets will generate solid returns albeit strong gains require good company selection.


† Includes unlisted equity holdings of 0.23% ‡ Includes unlisted equity holdings of 2.36% * Other may include swaps and currency contracts.

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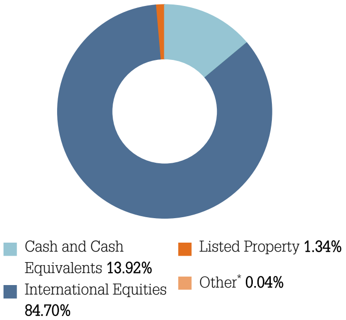
## Global Fund Portfolio Manager: Felix Fok

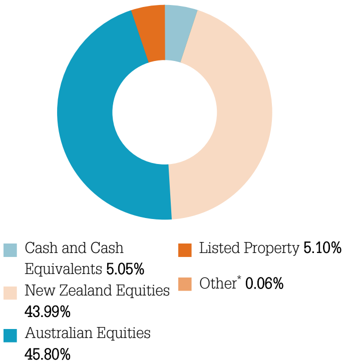
Actual investment mix




The Fund gained 1.2% in November and is up 21% in the past year. Global share markets gained 1.6% in local currency terms. Direct stocks had another positive month. Shares of Chinese internet powerhouse Tencent (+13.8%) made a new high after releasing earnings and breached the US$500bn market value milestone. Tencent's messaging application, WeChat, has become a daily necessity for Chinese residents and now hosts an ever-increasing suite of consumer services, further cementing its lead. Global exchange company CME Group (+9.0%) has been benefiting from a shift in trading from private venues to exchanges. This trend was epitomised by the announcement to launch Bitcoin contracts in December. As a marketplace, CME will benefit from money flows and trading in its contracts (a standard unit of an asset), without direct exposure to price changes. We are watching with keen interest.

In external managers, Magellan Infrastructure was ahead of the market and has been a steady outperformer year to date. Otherwise, it was a tougher month for our managers. The team assesses new and existing managers constantly and will make changes if we expect it to improve the risk-return profile. Overall, the backdrop for shares remains supportive, with rising global economic growth, low interest rates and improving corporate earnings.

## Trans-Tasman Fund Portfolio Manager: Sam Trethewey & Wayne Gentle

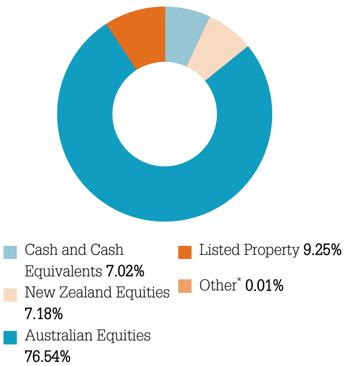



The Fund made a small gain of 0.1% in November and has now returned 24.6% over the past year. Our local markets remain well supported; the ASX 200 Accumulation Index rallied 1.6% as property trusts and energy stocks rose, while the NZX 50 Gross Index was up 0.5% following a recovery in the aged care stocks led by Ryman Healthcare (+13.8%). The most disappointing aspect of the month was the announcement by Xero (a great NZ growth story) of its intention to delist from the NZX and concentrate its liquidity on the ASX.

The Fund benefited from good stock selection, however the weakness in the AUD was a small headwind to returns this month. Highlights included Origin Energy (+12.5%) and Serko (+74.5%). Origin rallied as the oil price continues to strengthen. Serko, a travel management software developer, reported a positive financial result that demonstrated positive cash flow, strong revenue growth and a significant US opportunity. Cash was deployed into Ryman after its result and AGL Energy. The Fund took profit on Fisher & Paykel Healthcare and Technology One on share price strength.

Looking ahead, we remain optimistic on the local equity markets and will work hard to identify new opportunities for the Fund.

## Dynamic Fund Portfolio Manager: William Curtayne




Following a six-month period of relatively flat returns to begin the calendar year, the Australian equity market has continued its strong trajectory of the past few months. The Fund returned 2.1% for the month, bringing the six month return to a healthy 14.5%.

Some of our key contributors were Virgin Australia (+56.8%) following a rebound in operating performance and the potential of a privatisation, Experience Co (+18.6%) after management reiterated guidance at the AGM and Pinnacle Investments (+13.8%) on impressive fund flows and the signing of a new affiliate high conviction fund. The major detractor for the Fund was Living Cell Technologies (-85.5%) which disappointed following the results of the company's Parkinson's trial. Given the strong rally leading into the release, we took steps to mitigate our exposure to a potential negative outcome.

Two positions we added to the portfolio over the month were debt collector Credit Corp (+14.9%) and wealth management platform provider Netwealth (+44.1%). Credit Corp is Australia's largest provider of financial services to the credit impaired consumer segment. The group has a strong track record of revenue and earnings growth, having grown organically by more than 20% p.a. over the past five years. Netwealth operates a platform which has $14.3bn of FUM and is considered best-in-class across functionality and features.

*Other may include swaps and currency contracts.

| Upcoming Distributions | Target | Payment Date |
|---|---|---|
| Conservative Fund | 0.75 cents (Quarterly) | 18/01/2018 |
| Diversified Income Fund | 1.6 cents (Quarterly) | 21/02/2018 |
| Trans-Tasman Fund | 1.5 cents (Biannually) | 21/03/2018 |

# Milford Unit Trust PIE Funds Monthly Review as at 30 November 2017

## Fund Performance

| | Past month | 1 year | 3 years (p.a.) | 5 years (p.a.) | Since Fund inception (p.a.) | Unit price $ | Fund size $ |
|---|---|---|---|---|---|---|---|
| Conservative Fund* | 0.76% | 9.24% | — | — | 7.60% | 1.1103 | 162.6 M |
| Diversified Income Fund* | 1.07% | 12.17% | 10.83% | 12.26% | 12.29% | 1.6617 | 1731.0 M |
| Balanced Fund | 0.92% | 14.37% | 9.99% | 11.83% | 10.56% | 2.0897 | 467.1 M |
| Active Growth Fund | 0.87% | 15.28% | 11.41% | 13.80% | 13.10% | 3.2891 | 830.7 M |
| Global Fund | 1.20% | 20.99% | 8.23% | — | 9.01% | 1.4835 | 383.6 M |
| Trans-Tasman Fund* | 0.14% | 24.63% | 14.11% | 14.16% | 11.28% | 2.4947 | 296.2 M |
| Dynamic Fund | 2.08% | 17.53% | 13.35% | — | 13.92% | 1.7078 | 191.9 M |

For details of how investment performance is calculated, and returns at each PIR please see www.milfordasset.com/fund-performance
Performance figures are after total Fund charges have been deducted and at 0% PIR. Please note past performance is not a guarantee of future returns. *Performance figures include the reinvestment of the Funds' distribution. Inception dates for the Funds: Active Growth Fund: 1 October 2007, Balanced Fund: 1 April 2010, Conservative Fund: 1 September 2015, Diversified Income Fund: 1 April 2010, Dynamic Fund: 1 October 2013, Global Fund: 12 April 2013, Trans-Tasman Fund: 1 October 2007.

## Key Market Indices

| | Past month | 1 year | 3 years (p.a.) | 5 years (p.a.) | 7 years (p.a.) |
|---|---|---|---|---|---|
| S&P/NZX 50 Gross Index (with imputation credits) | 0.56% | 20.22% | 16.14% | 16.58% | 15.54% |
| S&P/ASX 200 Accumulation Index (AUD) | 1.64% | 14.60% | 8.72% | 10.56% | 8.60% |
| S&P/ASX 200 Accumulation Index (NZD) | 0.50% | 21.64% | 9.34% | 7.53% | 6.26% |
| MSCI World Index (local currency)* | 1.57% | 20.44% | 8.96% | 13.46% | 11.42% |
| MSCI World Index (NZD)* | 1.99% | 27.72% | 13.15% | 15.82% | 11.77% |
| S&P/NZX 90-Day Bank Bill Rate | 0.17% | 2.03% | 2.70% | 2.80% | 2.81% |

*With net dividends reinvested

## Top Securities Holdings (as a percentage of the Fund's Net Asset Value)

| Conservative | Diversified Income | Balanced | Active Growth | Global | Trans-Tasman | Dynamic |
|---|---|---|---|---|---|---|
| ASB Bank 5.25% 2026 2.18% | ASB Bank 5.25% 2026 2.55% | iShares MSCI EAFE Index Fund 5.81% | iShares MSCI EAFE Min Vol ETF 4.16% | Wellington Strategic Euro^ 5.87% | a2 Milk Company 4.92% | MNF Group 3.24% |
| KPGNZ 4% 2023 2.16% | Charter Hall Group 2.05% | Vanguard Intl Select Excl Index Fund 4.12% | Vanguard Intl Select Excl Index Fund 3.89% | Antipodes Global Fund^ 4.79% | Commonwealth Bank of Australia 4.55% | Bapcor 2.77% |
| Westpac 4.695% 2026 1.91% | Westpac 4.695% 2026 1.96% | Wellington Strategic Euro^ 1.25% | Spark New Zealand 2.26% | Hawkes Bay Investors^ 4.56% | BHP Billiton 3.95% | Eclipx Group 2.69% |
| ANZ Bank 5.28% 2049 1.82% | Aventus Retail Property Fund 1.84% | ASB Bank 5.25% 2026 1.12% | CYBG 8% 2049 1.75% | GMO Systematic Global Macro^ 4.35% | Fisher & Paykel Healthcare 3.89% | Amcor 2.68% |
| QBE 6.115% 2042 1.78% | Argosy Property Trust 1.56% | Antipodes Global Fund^ 1.02% | Air New Zealand 1.64% | Magellan Infrastructure^ 4.25% | National Australia Bank 3.81% | HUB24 2.68% |
| ASB Bank 6.65% 2024 1.61% | Contact Energy 1.53% | Hawkes Bay Investors^ 0.97% | iShares MSCI EAFE Index Fund 1.62% | Wellington Wolf Creek Shares^ 3.80% | Westpac Banking Corp 3.53% | Australian Finance Group 2.61% |
| Precinct Properties 4.42% 2024 1.60% | Kiwi Property Group 1.51% | GMO Systematic Global Macro^ 0.93% | Contact Energy 1.41% | Vanguard Info Tech ETF 3.01% | Spark New Zealand 3.51% | Bingo Industries 2.51% |
| NAB Float 2023 1.47% | Meridian Energy 1.49% | Spark New Zealand 0.91% | Tourism Holdings 1.38% | SPDR Dow Jones Industrial Average ETF 2.86% | Auckland Airport 2.72% | 3P Learning 2.39% |
| Genesis 5.7% 2022 1.17% | JPMorgan 5.15% 2023 1.43% | Charter Hall Group 0.91% | JPMorgan 5.15% 2023 1.38% | Energy Select SPDR 2.60% | Fletcher Building 2.47% | Collins Food 2.38% |
| Sydney Airport 3.76% 2020 1.09% | QBE 6.115% 2042 1.32% | Magellan Infrastructure^ 0.90% | Delegat Group 1.37% | SPDR Euro Stoxx 50 ETF 2.51% | Contact Energy 2.33% | iSelect 2.29% |

^Externally managed fund.

**Milford and Milford staff have approximately $32.7 million invested across our Unit Trust PIE Funds as at the end of November 2017.**

Level 17, 41 Shortland Street, Auckland
PO Box 960, Shortland Street, Auckland 1140
Free phone **0800 662 345**
milfordasset.com

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