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Milford Unit Trust PIE Funds Monthly Review
February 2018

Market and Economic Review

January was a positive month for most of Milford's funds, with the notable exception of the Trans-Tasman Fund.

The Global Fund, with a 2.4% return for the month, was the standout performer followed by the Active Growth Fund, which appreciated 1.1%. The Balanced Fund was up 0.8%, the Conservative Fund 0.7%, and the Diversified Income Fund 0.1%. The Trans-Tasman Fund had a negative 0.1% return, mainly because the ASX 200 Accumulation Index was down 0.4% in AUD and 1.0% in NZD terms. Although the fund partially hedges the NZD against the AUD, the hedge was not sufficient to cover the sharp appreciation of the NZD in January.

Global share markets have had a remarkable run since the end of 2016, with the Wall Street's Dow Jones Industrial Average (DJIA) recording twelve up months out of thirteen, particularly in January 2018 when it gained 5.9%. This was its best month since October 2015, when it appreciated 8.6%. Since the end of 2016, the MSCI World Net Total Return Index has had thirteen positive months out of thirteen, the ASX 200 Accumulation Index eight out of thirteen, and the NZX 50 Gross Index has had thirteen positive months in a row. This has been driven by expanding global growth, the United States tax cuts, low interest rates and an encouraging outlook for company profitability.

Investors received a boost in January when US companies reported solid earnings increases for the December 2017 year and made positive predictions for 2018 and 2019. Investors also received a boost from an optimistic economic report from the International Monetary Fund (IMF). The IMF stated that "The pickup in growth has been broad based, with notable upside surprises in Europe and Asia" and "The U.S. tax policy changes are expected to stimulate activity".

These comments are encouraging but financial markets are due for a correction after their strong performance in recent years. Milford believes that a downturn will be a market correction, rather than a bear market, but we will continue to monitor developments on a daily basis.

Milford Unit Trust PIE Funds Monthly Review as at 31 January 2018

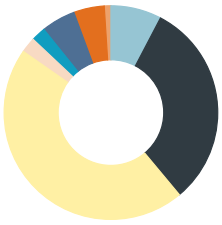
Conservative Fund **Portfolio Manager: Paul Morris**

The Fund returned 0.7% in January, bringing the one year return to 8.9%. January was notable for rising bond yields as markets anticipated potentially reduced monetary stimulus and the inflationary risks from synchronised global growth. However, this backdrop was supportive for global shares, albeit Australasian shares underperformed given a weighting towards bond-like income shares.

The Fund was reasonably well positioned for these market outcomes, even if a small foreign currency exposure was a headwind as the NZD appreciated. To protect from rising bond yields and benefit from improved global growth, we further reduced interest rate exposure and added to global shares. Against this, we retained an overweight to cash and fixed interest. Our fixed interest exposure is primarily to corporate bonds, which outperformed government bonds. We remained underweight Australasian shares, given their sensitivity to rising bond yields.

Looking forward, near term returns should remain reasonable through active management. We will look to take profit on some gains from the global share allocation and retain an overweight to cash and fixed interest, but with limited interest rate exposure. We will remain underweight Australasian shares but may contemplate cheaper income shares on further weakness.

Actual investment mix

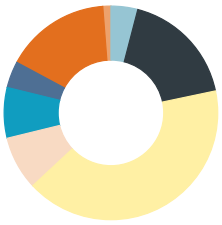


Cash and Cash Equivalents **7.68%**
Australian Equities **2.18%**
New Zealand Fixed Interest **31.26%**
International Equities **5.16%**
International Fixed Interest **45.76%**
Listed Property **4.64%**
New Zealand Equities **2.32%**
Other* **1.00%**

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

The Fund was slightly up in January and has returned 10.5% over the past year. It was a difficult month for income-oriented investment strategies, with weakness in global fixed income markets (global large cap corporate bonds fell 0.7%), as well as many higher dividend paying sectors of the share market (utilities and property companies in Australia fell 4.5% and 3.3% respectively). The key driver for this was increases in global interest rates, which led to lower investor demand for existing yield bearing assets. Against this backdrop, we were pleased with the modest positive return the Fund delivered.

The key positives for this month were interest rate markets (specifically bond futures in the US and Europe, where we had expected higher interest rates), and global shares (4.1% of the Fund, including listed property). At the company level, the Fund's small exposure to a2 Milk was a notable positive (+14.0%). Declines were dominated by Australian infrastructure and property companies including Macquarie Atlas Roads (-8.7%), Spark Infrastructure (-8.0%) and Mirvac (-6.4%). We believe several of these companies are now at attractive valuations and have been increasing exposure over the month, albeit we recognise that their short term performance is likely to remain volatile. Looking ahead, we retain a modestly cautious overall strategy.



Cash and Cash Equivalents **4.05%**
Australian Equities **7.65%**
New Zealand Fixed Interest **17.65%**
International Equities **4.01%**
International Fixed Interest **41.36%**
Listed Property **15.94%**
New Zealand Equities **8.12%**
Other* **1.22%**

Balanced Fund **Portfolio Manager: Mark Riggall**

The Fund returned 0.8% in January, bringing the one year return to 13.7%. Global markets started the year on a very strong note, led by US shares which surged higher on improved earnings. Other global share markets were also significantly higher, reflecting the accelerating global economic growth environment. The Fund's increased exposure to global shares delivered the bulk of the performance this month - the Milford Global Retail Fund was up 2.4%. Improving global growth is also being reflected in interest rate markets where increasing inflation expectations are causing bonds to be sold off. This process accelerated in January but is something we have been wary of and have taken precautions to protect against such falls. Given that, the bond portfolios delivered a positive performance for the month. Local share markets underperformed, partly due to their higher sensitivity to interest rates.

Looking forward, the Fund has reduced some share exposure given the strong run, but we still prefer global shares over NZ and are neutral on Australian shares. We remain negative on the NZD and have used recent strength to increase the Fund's offshore currency exposure. We expect markets to be more volatile this year, but we remain cautiously optimistic, using weakness in share markets to top up investments.

Cash and Cash Equivalents **11.35%**
Australian Equities **12.25%**
New Zealand Fixed Interest **9.08%**
International Equities **28.79%**
International Fixed Interest **21.50%**
Listed Property **7.21%**
New Zealand Equities† **8.61%**
Other* **1.21%**

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

The Fund rose 1.1% during January, benefiting from strong returns from global share markets which were up 3.8% in local currency. Returns from NZ and Australian shares were more subdued, at +0.5% and -0.4% respectively, as income producing shares fell in response to rising long-term interest rates.

Key company performers for the month were a2 Milk (+14.0%), Google (+11.8%) and Xero (+7.9%), as investors focused on high growth shares. The Fund also benefited from strategies to take advantage of rising long-term US interest rates. During the month, we added to our holdings in airlines Qantas and Air New Zealand as we believe they are attractively valued and oversold on concerns around rising oil prices. In January, we also reduced our exposure to shares and, in particular, the US market following its strong run during the month (+5.7%).

The outlook for share markets remains supported by good and robust economic growth, positive company earnings prospects, low interest rates and plenty of liquidity. The key risks for share markets are the prospect of further rate rises in the US, relatively high company valuations and in NZ, the housing market. On balance, we believe share markets will generate solid returns although we remain active within the portfolio to capture new opportunities and manage downside risks.

Cash and Cash Equivalents **8.93%**
Australian Equities **21.10%**
New Zealand Fixed Interest **3.30%**
International Equities **21.56%**
International Fixed Interest **11.69%**
Listed Property **5.04%**
New Zealand Equities‡ **27.40%**
Other* **0.98%**

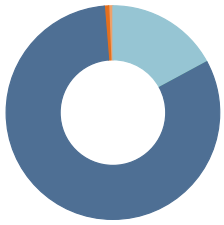
†Includes unlisted equity holdings of 0.23% ‡Includes unlisted equity holdings of 2.27% *Other may include swaps and currency contracts.

Milford Unit Trust PIE Funds Monthly Review as at 31 January 2018

Global Fund Portfolio Manager: Felix Fok

The Fund rose 2.4% in January in buoyant markets. The strength of the NZD was a sizeable headwind for the second month running. We were able to mitigate half of this impact through currency management. Direct stocks were strong and outperformed the market meaningfully. The top contributor was Amazon (+24.1%), the established US online shopping and computing services giant. Amazon is arguably the most interesting and hard to value company in the Fund because of how quickly it has evolved. It is rare for a company to strike gold twice (in e-commerce and cloud computing) but it may three-peat with its voice-based digital assistant, 'Alexa', which is increasingly embedded in smartphones, speakers and cars. A personalised assistant that listens and responds to commands promises convenience and utility to consumers and professionals. With widespread adoption, the digital assistant's influence over consumer preference could be a significant competitive advantage for Amazon over time.
In external managers, Wolf Creek (+6.8%), which invests in global financial companies, was the standout and is benefiting from strong economic activity. Negative contributors included Magellan Infrastructure (-2.5%) which was pressured by rising interest rates. Overall, the backdrop for shares remains supportive, with rising global economic growth, moderate interest rates and improving corporate earnings.

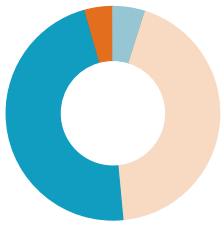
Actual investment mix



Cash and Cash Equivalents **17.12%**
International Equities **81.59%**
Listed Property **0.65%**
Other* **0.64%**

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

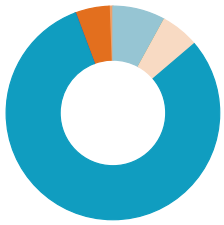
The Fund declined 0.1% in January, but it has returned 25.0% over the past 12 months. Our local markets were impacted by increases in key offshore interest rates, reducing the attractiveness of some of the high dividend paying companies. The NZX 50 Gross Index finished up 0.5% as new money continued to flow into the market, while the ASX 200 Accumulation Index fell 0.4% mostly due to the large amount of high dividend payers like banks, REITS and infrastructure stocks.
The Fund benefited from good stock selection. However, weakness in the AUD was again a headwind. Highlights included a2 Milk (+14.0%) and Treasury Wine Estates (+7.3%). a2 Milk was well supported following several positive broker updates and the implementation of regulation changes in the Chinese infant formula market reducing competition. Despite the rising AUD, Treasury Wine Estates topped out a good month with a good half year profit released at month end. Cash was deployed into the NZ electricity companies on interest rate related weakness, into South 32 and some key stocks like Qantas and Aristocrat. The Fund took profit on Xero and Newcrest Mining into strength. February will see many companies report financial results and we will work hard to identify new opportunities for the Fund.



Cash and Cash Equivalents **4.92%**
New Zealand Equities **43.59%**
Australian Equities **47.06%**
Listed Property **4.27%**
Other* **0.16%**

Dynamic Fund Portfolio Manager: William Curtayne

The Fund took a breather in January, finishing the month flat, having delivered +17.1% performance in the prior six-month period. The Fund's outperformance over the broader market, which finished down 0.4%, was driven by positive trading updates from several of our holdings.
Top performers included Pinnacle Investment Management (+24.5%) and fast growing consumer payments platform Afterpay (+23.3%). We also benefited from adding Xero to the portfolio in December, following uncertainty created on its removal from the NZX 50 Index. It has since rallied +20.7% from the lows and we remain optimistic about its prospects. Losers included wealth platform NetWealth (-14.8%) and the travel platform Serko (-14.2%), which both returned some outperformance from a stunning 2017 where they delivered +96.8% and +655.1% respectively.
We are optimistic about entering the February reporting season. Despite the obvious global macro-economic risks, the domestic economy remains more balanced with recent economic data having a more positive bias. Our portfolio is well balanced, with several reasonably priced companies having good growth prospects irrespective of the cycle. The inevitable volatility created with the February results season will be sure to provide some opportunities to deploy capital into oversold companies and reassess the investment theses of our core holdings.



Cash and Cash Equivalents **7.99%**
New Zealand Equities **5.78%**
Australian Equities **80.46%**
International Equities **0.09%**
Listed Property **5.11%**
Other* **0.57%**

*Other may include swaps and currency contracts.

Upcoming Distributions	Target	Payment Date
Conservative Fund	0.75 cents (Quarterly)	20/04/2018
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 31 January 2018

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*	0.68%	8.91%	—	—	7.45%	1.1127	172.4 M
Diversified Income Fund*	0.11%	10.45%	10.02%	11.71%	12.10%	1.6720	1796.3 M
Balanced Fund	0.82%	13.71%	9.48%	11.21%	10.51%	2.1177	503.5 M
Active Growth Fund	1.08%	16.17%	11.34%	13.29%	13.18%	3.3802	913.5 M
Global Fund	2.37%	20.03%	7.83%	—	9.03%	1.5059	409.7 M
Trans-Tasman Fund*	-0.13%	24.98%	14.10%	13.49%	11.36%	2.5572	319.5 M
Dynamic Fund	0.01%	22.34%	14.25%	—	14.22%	1.7652	197.0 M

For details of how investment performance is calculated, and returns at each PIR please see www.milfordasset.com/funds-performance/view-performance#tab-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 & Trans-Tasman Fund: 1 October 2007, Diversified Income Fund & Balanced Fund: 1 April 2010, Global Fund: 12 April 2013, Dynamic Fund: 1 October 2013, Conservative Fund: 1 September 2015.

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)	0.53%	21.26%	15.13%	16.15%	15.67%
S&P/ASX 200 Accumulation Index (AUD)	-0.45%	12.18%	7.31%	9.07%	8.23%
S&P/ASX 200 Accumulation Index (NZD)	-0.96%	18.54%	7.99%	6.35%	5.71%
MSCI World Index (local currency)*	3.77%	21.38%	11.21%	12.93%	11.00%
MSCI World Index (NZD)*	1.17%	24.65%	11.11%	14.55%	10.72%
S&P/NZX 90-Day Bank Bill Rate	0.16%	2.00%	2.59%	2.78%	2.78%

*With net dividends reinvested

Top Security 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 2.05%	Charter Hall Group 2.53%	iShares MSCI EAFE Index Fund 4.95%	Vanguard Intl Select Excl Index Fund 3.86%	Wellington Strategic Euro^ 5.51%	a2 Milk Company 4.92%	Xero 4.17%
Westpac 4.695% 2026 1.84%	ASB Bank 5.25% 2026 2.43%	Vanguard Intl Select Excl Index Fund 3.80%	iShares MSCI EAFE Min Vol ETF 3.71%	Antipodes Global Fund^ 4.52%	Commonwealth Bank of Australia 4.10%	Coporate Travel Mgmt 3.62%
ANZ Bank 5.28% 2049 1.76%	Westpac 4.695% 2026 1.89%	Wellington Strategic Euro^ 1.14%	Spark New Zealand 2.05%	Wellington Wolf Creek Shares^ 4.27%	BHP Billiton 3.97%	MNF Group 3.33%
ASB Bank 6.65% 2024 1.54%	Contact Energy 1.65%	Charter Hall Group 1.08%	Contact Energy 1.71%	GMO Systematic Global Macro^ 4.18%	National Australia Bank 3.97%	Bingo Industries 2.84%
NAB Float 2023 1.41%	Mirvac Group 1.61%	ASB Bank 5.25% 2026 1.06%	Air New Zealand 1.62%	Hawkes Bay Investors^ 3.98%	Westpac Banking Corp 3.84%	3P Learning 2.84%
Precinct Properties 4.42% 2024 1.29%	Argosy Property Trust 1.52%	Contact Energy 0.95%	CYBG 8% 2049 1.59%	Magellan Infrastructure^ 3.69%	Fisher & Paykel Healthcare 3.40%	Eclipx Group 2.73%
Genesis 5.7% 2022 1.24%	Kiwi Property Group 1.49%	Antipodes Global Fund^ 0.94%	iShares MSCI EAFE Index Fund 1.47%	Energy Select SPDR 3.59%	Spark New Zealand 2.99%	Australian Finance Group 2.67%
ANZ Term Deposit 3.08% 06/18 1.19%	Aventus Capital Float 2025 1.42%	Spark New Zealand 0.89%	Tourism Holdings 1.44%	SPDR DJIA ETF Trust 2.59%	Xero 2.63%	HUB24 2.47%
IAG 5.15% 2043 1.14%	Meridian Energy 1.38%	Wellington Wolf Creek Shares^ 0.89%	Delegat Group 1.36%	SPDR Euro Stoxx 50 ETF 2.58%	Contact Energy 2.58%	Pinnacle Investment Mgmt 2.34%
United Energy 3.85% 2024 1.08%	Aventus Retail Property Fund 1.36%	GMO Systematic Global Macro^ 0.87%	Chorus 1.33%	iShares Edge MSCI MV EM ETF 2.34%	Auckland Airport 2.44%	Collins Food 2.32%

^Externally managed fund.

Milford and Milford staff have approximately $33.3 million invested across our Unit Trust PIE Funds as at the end of January 2018.

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