



## Milford Unit Trust PIE Funds Monthly Review

### July 2018

## Market and Economic Review

June was another positive month as Milford's six equity-oriented Funds appreciated between 1.0% and 3.5% while our four bond focused Funds had returns between slightly positive and 0.8% for the month. Bond funds have faced headwinds in a rising interest rate environment while equity funds benefited from the relatively strong performances of the New Zealand and Australian share markets.

The big question is whether these favourable share market conditions will continue. The outlook for global economic growth remains solid, although there are signs that growth has become more mixed on a region by region basis. The US economy continues to perform well, mainly because of tax cuts, deregulation and business investment. Meanwhile, growth seems to have peaked in other regions, notably Europe, Japan and New Zealand but economic activity in these areas has eased, rather than fallen dramatically.

The Reserve Bank of NZ reported domestic GDP growth of 2.6% for the March 2018 year compared with 3.1% for the same period in Australia (reported by the Reserve Bank of Australia). We expect New Zealand's growth to moderate further but to remain above 2.0% for the March 2019 year. We remain marginally positive on share markets but expect further volatility. Milford continues to prefer US markets because of the country's strong economic growth but acknowledge that company valuations are high, particularly for technology companies. We have become slightly more positive on European stocks, mainly on a valuation basis, while there continues to be more attractive opportunities in Australia than New Zealand.

Milford expect interest rates to continue to drift higher, mainly in the United States because of its accelerating growth and increasing inflationary pressures. Meanwhile, official interest rates are expected to remain on hold in New Zealand and Australia until mid-2019. The NZD is expected to remain softer over the medium-term, particularly against the USD, as interest rates in the world's largest economy are expected to rise more rapidly than in other countries. It is important to remember that Milford is an active investment manager, with our 23-person investment team monitoring economic and market conditions on a day-by-day basis. Our aim is to respond quickly to any deterioration in economic and market conditions.



## Trans-Tasman Bond Fund

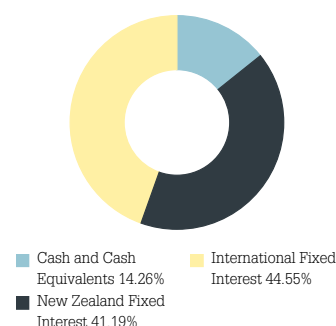
**Portfolio Manager: Paul Morris**

The Fund returned 0.4% in June, in line with its benchmark. Australasian corporate bond prices were mixed over the month, but continue to outperform offshore peers. They have been supported by expectations for unchanged central bank cash rates into 2019.

NZD corporate bonds continued to outperform those in AUD, helped in June by the Reserve Bank of New Zealand reiterating the next cash rate move may be up or down. Australasian corporate bonds may look expensive relative to offshore, and we believe they could remain so for some time. The Fund's small exposure to offshore bonds of Australasian companies generally offers better yields to maturity, but in June contributed negatively to returns as offshore corporate bonds were weaker. We continue to reduce expensive Fund holdings, concurrent with reducing exposure to lower rated and longer dated bonds. Instead, we added several new holdings, including new issues from Housing NZ, Auckland Council, Vector Limited and Barclays (the UK bank).

Looking forward, we remain wary that Australasian government and corporate bond valuations are stretched. Although Australasian cash rates may be on hold, longer dated bonds will be influenced by offshore. This may be a headwind for returns. Therefore, after recent falls in yields we have reduced interest rate exposure to help protect capital over time.

### Actual investment mix<sup>1</sup>



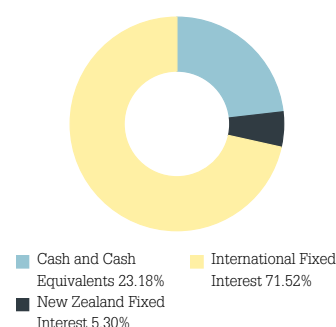
## Global Bond Fund

**Portfolio Manager: Paul Morris**

The Fund's exposure is primarily to corporate bonds. In 2018 global corporate bond prices have been under pressure, weighing on Fund returns. This can be attributed to higher government bond yields and one of the worst starts to a year for credit spreads (the extra yield of corporate over government bonds).

In June, global government bond yields were generally close to unchanged, but large new bond issuance volume and an escalation in the tariff war, drove corporate bond yields generally higher. This limited the Fund to a flat return in June, 0.2% less than its benchmark (which has a lower corporate bond exposure). The Fund has been active in navigating these challenging market conditions, further improving the credit quality of its corporate bond holdings and reducing their time to maturity. We remain wary of ongoing elevated geopolitical risks (especially trade) and therefore increased interest rate exposure, considering also the increase in long dated yields already in place.

Near-term, improved corporate bond valuations and likely slower issuance should improve corporate bond returns. Looking further out, Fund returns may face headwinds from weaker monetary policy support, as inflation recovers. Therefore, we will continue to limit interest rate exposure below the long-run neutral and will look to reduce further exposure to credit spreads.



<sup>1</sup>The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

## Conservative Fund

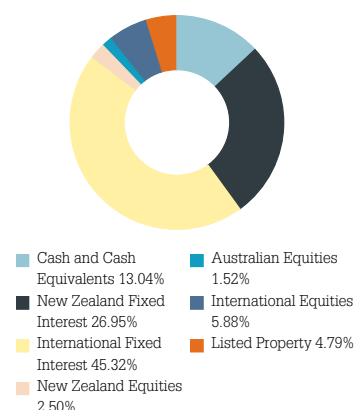
**Portfolio Manager: Paul Morris**

The Fund returned 0.6% in June and has returned 6.0% over the past year. Fixed interest posted a moderate return in the month, albeit primarily from its Australasian corporate bonds as global corporate bond returns were close to zero.

Globally, 2018 has been challenging for fixed interest but Australasian bonds have benefited from expectations that cash rates will remain on hold deep into 2019. This has also supported the Fund's Australasian shares, given a focus on income shares. In June, these shares contributed strongly to Fund returns, although they underperformed growth shares. Irrespective of some notable headwinds, including an escalation of tariff wars, the Fund's global shares enjoyed a reasonable month. It also benefited from a small foreign currency exposure as the NZD was weaker.

Looking forward, we remain cautiously positive for moderate returns. Nevertheless, considering the Fund's conservative profile, arguably elevated valuations and near-term known risks (including the tariff war and less certainty on global growth outlook) we remain underweight in shares compared to the long-run neutral. This is against an overweight in cash and fixed interest. Within fixed interest we are limiting interest rate exposure, cognisant of the ongoing risks to returns from rising global interest rates, even though Australasian cash rates may remain on hold well into 2019.

### Actual investment mix<sup>1</sup>



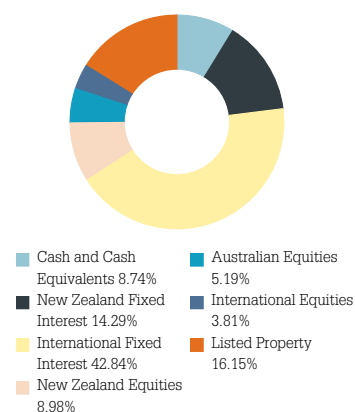
## Diversified Income Fund

**Portfolio Manager: David Lewis**

The Fund had a solid month, up 0.8% and has returned 7.6% over the past year. Returns this month came largely from the Fund's share exposures, especially in Australasia, although market gains for income-oriented shares were lower than for higher growth companies. Bond markets were mixed in June, with small gains in NZ and Australia offset by modest declines in international bonds.

Among the Fund's shares, Suncorp (Australian bank and Australasian insurance company) rose 8.6% as market fears regarding the Australian Royal Commission on banks receded somewhat. In addition, several of the Fund's holdings in Australian property companies performed well, Goodman (+4.5%), Charter Hall (+5.3%) and Scentre (+5.0%), which was supported by strong commercial property prices in Sydney, as well as continued low interest rates from the Reserve Bank of Australia. We have begun to reduce some of these Australian property exposures in recent weeks - while the operating outlook remains positive, valuations for these companies are now less attractive.

In fixed income, the Fund has been adding to some international holdings, given much improved valuations over recent months. Looking ahead, the Fund retains a modestly cautious approach, as reflected in slightly lower holdings of shares (currently 34% of the Fund, including property) and high yield bonds (approx. 18%), relative to our expected long-run positions.



<sup>1</sup>The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

## Balanced Fund

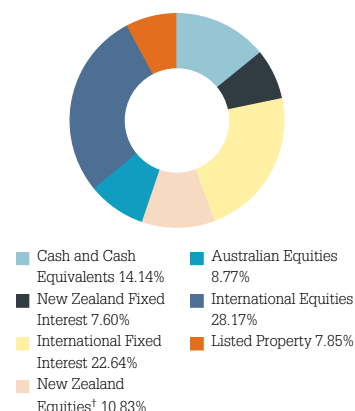
**Portfolio Manager: Mark Riggall**

The Fund returned 1.0% in June bringing the 1-year return to 10.7%. The key theme during the month was the escalation in the US centred trade war that has been building for months. Unlike previous episodes of rising market risks, this has been different as we are seeing markedly different reactions by various asset classes.

The NZD (and AUD) has weakened due to our economy's significant reliance on trade. This benefited the unhedged portion of global shares in the Fund. In addition, local NZ and Australian shares performed well as global investors valued their more defensive attributes compared to other Asian share markets. Government bonds were largely unchanged but company bonds underperformed due to an increase in supply.

Going forward, the risk of further escalation in the trade spat is increasing and accordingly the Fund is cautiously positioned. Global shares continue to look more attractive than local shares, due to improving US growth and fading NZ/Australian growth, coupled with high valuation levels for NZ/Australian shares. Corporate bonds now look more attractive after a period of underperformance. The Fund has a largely neutral currency position, having trimmed exposure following the recent falls in the NZD. Medium term, whilst our expectations are for increased volatility, we retain a positive outlook with shares likely to outperform bonds and cash.

### Actual investment mix<sup>1</sup>



## Active Growth Fund

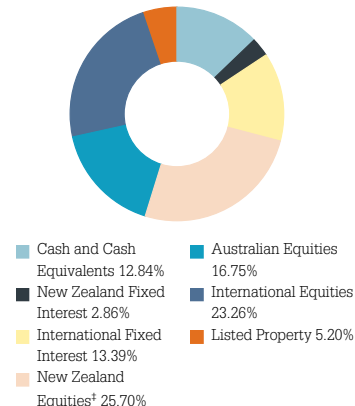
**Portfolio Manager: Jonathan Windust**

The Fund rose 1.6% during the month benefiting from strong returns in the NZX 50 Gross Index and ASX 200 Accumulation Index, both up 3.3%. These markets benefited from good investor demand, despite uncertainty and risk aversion in global markets caused by politics and trade wars. Global shares were relatively flat, up 0.3%, but rose strongly in NZD terms due to the fall in the value of the NZ currency. The NZD fell due to the strength in the US economy, where further rate rises are likely.

Key company performers during the month were Kathmandu (+21.8%) and oil companies Sundance Energy (+10.1%) and Woodside Petroleum (+9.4%). Kathmandu rose following a strong trading update where it increased its full year earnings guidance, which points to growth of over 30%. During the month, we took advantage of market strength to reduce exposure to Australian shares which reached our price targets, including Scentre Group and Corporate Travel Management.

The outlook for shares remains generally positive, supported by robust economic conditions and company earnings, with the key headwinds being rising valuations (particularly in New Zealand) and political/trade uncertainty. Reflecting this uncertainty, and rising valuations we have a lower weight in shares and property (approximately 70%) than average. We continue to remain active to isolate companies that are attractively valued relative to their risks.

*Please note this Fund is closed to new investors.*



<sup>†</sup>Includes unlisted equity holdings of 0.26% <sup>†</sup>Includes unlisted equity holdings of 2.27%

<sup>1</sup>The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

## Australian Absolute Growth Fund

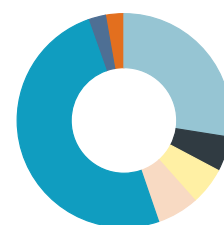
**Portfolio Manager: William Curtayne**

The Fund returned 1.6% in June and 5.0% for the last quarter. Over the month we reduced our position in Bingo ahead of the release of escrowed stock in August. This release includes the CEO's \$189 million shareholding, which was escrowed as part of the IPO process in May 2017. Given the 48.1% return over the last 12 months, we wouldn't begrudge some profit taking by the CEO. However, any selling by insiders can create short term uncertainty and share price volatility, so we believe it's prudent to reduce the size of our investment until this event has passed.

Growth stocks have continued to perform very strongly in the Australian market. This has pushed valuations on many of these companies to very expensive levels. Given the elevated risk from high valuations, we have reduced our exposure to growth companies. We have reinitiated a position in NAB and CBA after completely selling out of bank shares in April. The ongoing Royal Commission has seen their share prices continue to decline. We believe they may recover some of their recent losses over the next couple of months as the fallout from the Royal Commission may not be as bearish as current market expectations.

The Fund's total equity exposure (including property) is now approximately 62%. We will be looking for a market sell-off as an opportunity to purchase back some of the growth stocks we have recently sold.

### Actual investment mix<sup>1</sup>



Cash and Cash Equivalents 27.50%	Australian Equities 49.85%
New Zealand Fixed Interest 5.25%	International Equities 2.64%
International Fixed Interest 5.68%	Listed Property 2.78%
New Zealand Equities 6.30%	

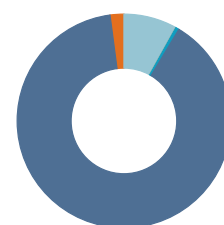
## Global Equity Fund

**Portfolio Manager: Felix Fok**

The Fund was up 1.5% in June, bringing the 1-year return to 13.3%. Returns were driven by the performance of direct stocks and a broadly weaker NZD. Biggest positive contributors during the month included global consumer companies Inditex (+8.3%) and Reckitt Benckiser (+8.3%). Inditex, the company behind fast-fashion chain Zara, reported solid results, despite concern over the health of the high street. The weaker EUR and GBP also helped lift sentiment for these Europe-based multi-national companies. Meanwhile, pet play Trupanion (+21.5%) continued its run.

The biggest detractor to performance was, for a second month, Chinese internet company 58.com (-14.6%). The Chinese marketplace is extremely competitive, but the prize is enormous. We continue to view founder-run 58.com favourably. Chip maker Intel (-10.0%) was dragged down by US-China trade tension, as well as a surprise resignation by its CEO on a breach of the company's non-fraternization code. Our research aims to find long-term winners based on business strength and industry dynamics, but fails to predict senior management indiscretion. Amongst our managers, Magellan Infrastructure (+3.9%) performed well as defensive assets were sought after. However, MTX (-4.2%) could not avoid a selloff in emerging market assets.

Overall, the backdrop for shares remains supportive, with steady global economic growth, moderate interest rates, and solid corporate earnings. However, concerns over inflation and protectionism are likely to lead to a bumpier road ahead.



Cash and Cash Equivalents 8.08%	International Equities 89.32%
Australian Equities 0.52%	Listed Property 2.08%

<sup>1</sup>The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

## Trans-Tasman Equity Fund

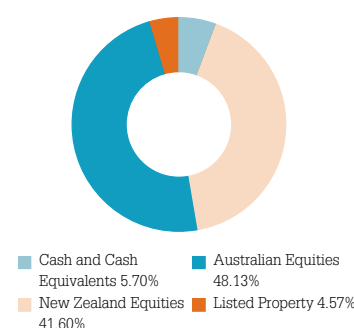
**Portfolio Manager: Sam Trethewey & Wayne Gentle**

The Fund had a very strong month in June, returning 3.5%, due to strong local equity markets and good stock selection. The Fund has now returned 21.5% over the past year.

Key highlights included Corporate Travel Management (+10.9%) and Vista Group (+9.4%). Both companies have sizable growth opportunities ahead and have demonstrated an impressive ability to win market share. On a relative basis, Fisher & Paykel Healthcare (+13.4%) was a key detractor due to the Fund underweighting the stock. The stock rallied strongly despite a weak result in May that indicated slowing earnings growth and upcoming margin pressure. However, we benefited from avoiding poor performers like Telstra (-6.4%) and CBL Corporation. CBL was placed on suspension in February pending numerous regulatory investigations and removed from the NZX 50 Index at \$0.00 mid-month.

During the month, the Fund participated in a placement in PushPay Holdings, a faith sector payments provider, and reduced its underweight position in the major Australian banks. We continued to trim Z Energy and waste management exposure - Bingo Industries, into strength. Looking ahead we will focus on stock selection. As the local markets head into 'confession season' ahead of the key August reporting period we will be watchful of companies where expectations become extended. Earnings momentum has been highly correlated to share price performance recently.

### Actual investment mix<sup>1</sup>



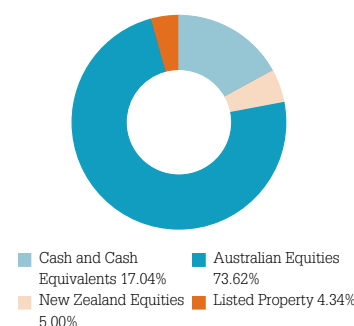
## Dynamic Fund

**Portfolio Manager: William Curtayne & Michael Higgins**

Following a 5.3% return in May, we were pleased to deliver a 1.5% return in June. Despite our defensive positioning, the Fund outperformed the benchmark return of 1.4%. Performance was led by growth companies such as IDP Education (+8.6%), Xero (+9.9%), Corporate Travel Management (+10.9%) and WiseTech (+6.5%) which continue their outstanding rally.

We have taken some profit on these growth companies as valuations have become elevated. One example is IDP Education, which has rallied over 175.9% since we first bought in January 2017. IDP's valuation now looks full at 50 times FY18 earnings. While we still like its exposure to emerging markets, like India, we have sold the lion's share of our original position. Over the month we also reduced our position in Bingo, ahead of the release of the CEO's escrowed stock in August. Given the 48.1% return over the last 12 months, we wouldn't begrudge some profit taking by the CEO. However, any selling by insiders can create short term uncertainty and share price volatility, so we believe it's prudent to reduce the size of our investment.

Detractors for the month included independent platform providers HUB24 (-16.2%) and Netwealth (-9.2%) which pared recent gains. The Fund's cash weighting leaves us well positioned to take advantage of any market volatility in what is an increasingly expensive market.



Upcoming Distributions	Target	Payment Date
Trans-Tasman Bond Fund	0.75 cents (Quarterly)	20/09/2018
Global Bond Fund	0.75 cents (Quarterly)	20/09/2018
Conservative Fund	0.75 cents (Quarterly)	19/07/2018
Diversified Income Fund	1.6 cents (Quarterly)	21/08/2018
Trans-Tasman Equity Fund	1.5 cents (Biannually)	20/09/2018

<sup>1</sup>The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

# Milford Unit Trust PIE Funds Monthly Review as at 30 June 2018

## Fund Performance

	Past month	1 year	3 years (p.a.)	5 years (p.a.)	Since Fund inception (p.a.)	Unit price \$	Fund size \$
Trans-Tasman Bond Fund**	0.38%	4.59%	4.57%	—	5.62%	1.1144	383.8 M
Global Bond Fund**	0.02%	2.42%	—	—	4.37%	1.0170	315.9 M
Conservative Fund*	0.55%	5.96%	—	—	6.73%	1.1166	188.2 M
Diversified Income Fund*	0.84%	7.61%	10.03%	11.23%	11.80%	1.6789	1845.5 M
Balanced Fund	1.00%	10.73%	9.04%	10.75%	10.34%	2.1772	552.8 M
Active Growth Fund#	1.57%	16.46%	12.21%	13.18%	13.16%	3.5453	971.3 M
Australian Absolute Growth Fund	1.60%	—	—	—	—	1.0405	69.0 M
Global Equity Fund	1.48%	13.34%	6.13%	8.80%	8.71%	1.5361	432.9 M
Trans-Tasman Equity Fund*	3.49%	21.49%	15.10%	14.02%	11.56%	2.7054	361.3 M
Dynamic Fund	1.46%	25.30%	13.93%	—	14.42%	1.8786	222.1 M

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, Trans-Tasman Equity Fund: 1 October 2007, Balanced Fund: 1 April 2010, Diversified Income Fund: 1 April 2010, Global Equity Fund: 12 April 2013, Dynamic Fund: 1 October 2013, Trans-Tasman Bond Fund: 3 December 2013, Conservative Fund: 1 September 2015, Global Bond Fund: 1 February 2017, Australian Absolute Growth Fund: 1 March 2018.

For details of how investment performance is calculated, and returns at each PIR, please see [www.milfordasset.com/funds-performance/view-performance#tab-performance](http://www.milfordasset.com/funds-performance/view-performance#tab-performance)

Performance figures are after total Fund charges have been deducted and at 0% PIR.

^Returns prior to 1 March 2018 are from when the Fund was previously offered to wholesale investors only and have been adjusted for current Fund charges.

#The Active Growth Fund is closed to new investors.

## 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)	3.37%	18.87%	17.42%	16.48%	16.08%
S&P/ASX 200 Accumulation Index (AUD)	3.27%	13.01%	9.04%	9.98%	9.12%
S&P/ASX 200 Accumulation Index (NZD)	4.48%	17.66%	7.57%	8.18%	6.47%
MSCI World Index (local currency)*	0.33%	10.86%	8.64%	11.09%	10.47%
MSCI World Index (NZD)*	3.58%	20.14%	8.44%	12.87%	11.98%
S&P/NZX 90-Day Bank Bill Rate	0.16%	1.96%	2.35%	2.72%	2.72%

\*With net dividends reinvested



# Milford Unit Trust PIE Funds Monthly Review as at 30 June 2018

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

Trans-Tasman Bond Fund	Global Bond Fund	Conservative Fund	Diversified Income Fund	Balanced Fund
NZLGFA 2.75% 2025 2.26%	Microsoft 2.875% 2024 2.55%	Westpac Float 2028 2.28%	ASB Bank 5.25% 2026 2.10%	iShares MSCI EAFE Index Fund 2.93%
Auckland Council 3.17% 2023 2.10%	Westpac Float 2028 1.97%	Investore Property 4.40% 2024 1.92%	Contact Energy 2.08%	Vanguard Intl Select Excl Index Fund 2.23%
ANZ Term Deposit 3.23% 12/18 1.96%	Citigroup 5.95% 2049 1.69%	ASB Bank 6.65% 2024 1.47%	Aventus Retail Property 2.07%	Contact Energy 1.37%
ASB Bank 6.65% 2024 1.94%	HSBC Float 2024 1.55%	QBE 6.75% 2044 1.31%	Spark New Zealand 1.79%	Spark New Zealand 1.32%
Vector 4.996% 2024 1.93%	Sprint Spectrum 4.738% 2025 1.47%	BNZ 3.375% 2021 1.20%	Westpac 4.695% 2026 1.76%	a2 Milk Company 1.18%
United Energy 3.85% 2024 1.90%	Bank of America 6.10% 2025 1.43%	Vector 4.996% 2024 1.13%	Argosy Property 1.70%	Wellington Strategic Euro^ 1.01%
Westpac 3.795% 2021 1.88%	JPMorgan 5.15% 2023 1.40%	NZLGFA 2.75% 2025 1.12%	Kiwi Property Group 1.65%	Energy Select SPDR 0.99%
Downer Group 5.75% 2018 1.84%	Aviva 3.875% 2044 1.35%	United Energy 3.85% 2024 1.07%	Charter Hall Group 1.61%	Aventus Retail Property 0.95%
BNZ 3.375% 2021 1.80%	Swiss Re 5.75% 2050 1.35%	Auckland Council 3.17% 2023 1.04%	Mirvac Group 1.57%	Regional Banking ETF SPDR 0.91%
Investore Property 4.40% 2024 1.79%	Nationwide Bldg Society 2% 2029 1.34%	Sydney Airport 3.76% 2020 1.04%	Meridian Energy 1.46%	ASB Bank 5.25% 2026 0.89%

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

Active Growth Fund	Australian Absolute Growth Fund	Global Equity Fund	Trans-Tasman Equity Fund	Dynamic Fund
iShares MSCI EAFE Min Vol ETF 3.53%	Orora 3.79%	Wellington Strategic Euro^ 5.20%	a2 Milk Company 6.14%	Coporate Travel Mgmt 3.94%
Contact Energy 2.50%	Origin Energy 3.28%	Energy Select SPDR 4.47%	BHP Billiton 4.24%	Smartgroup Corp 3.27%
a2 Milk Company 2.34%	Credit Corp Group 3.01%	Antipodes Global Fund^ 4.42%	Commonwealth Bank of Australia 4.14%	Credit Corp Group 3.21%
Spark New Zealand 2.22%	Boral 2.87%	Wellington Wolf Creek Shares^ 4.29%	Westpac Banking Corp 3.21%	Seven Group Holdings 3.06%
Vanguard Intl Select Excl Index Fund 1.70%	National Australia Bank 2.60%	Magellan Infrastructure^ 4.23%	National Australia Bank 3.19%	Collins Foods 2.98%
CYBG 8% 2049 1.38%	Commonwealth Bank of Australia 2.50%	Hawkes Bay Investors^ 4.16%	Fisher & Paykel Healthcare 3.18%	Pinnacle Investment Mgmt 2.73%
Delegat Group 1.37%	Collins Foods 2.39%	GMO Systematic Global Macro^ 4.05%	Spark New Zealand 3.12%	Boral 2.50%
Z Energy 1.24%	Transurban Group 2.34%	iShares Russell 2000 3.24%	Fletcher Building 2.56%	Origin Energy 2.35%
Westpac Float 2028 1.15%	Sydney Airport 2.28%	Vontobel Sust. EM Leaders^ 3.08%	Contact Energy 2.51%	Australian Finance Group 2.27%
JPMorgan 5.15% 2023 1.14%	Smartgroup Corp 2.21%	Euro Stoxx 50 ETF SPDR 2.81%	Summerset Group Holdings 2.51%	Wellcom Group 1.99%

<sup>\*</sup>Externally managed fund.

Milford and Milford staff have approximately \$32.5 million invested across our Unit Trust PIE Funds as at the end of June 2018.

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



Disclaimer: The Milford Monthly Review has been prepared by Milford Funds Limited. It is based on information believed to be accurate and reliable although no guarantee can be given that this is the case. No reproduction of any material either in part or in full is permitted without prior permission. For more information about the Funds please refer to the Product Disclosure Statement or the latest Quarterly Fund Update.