

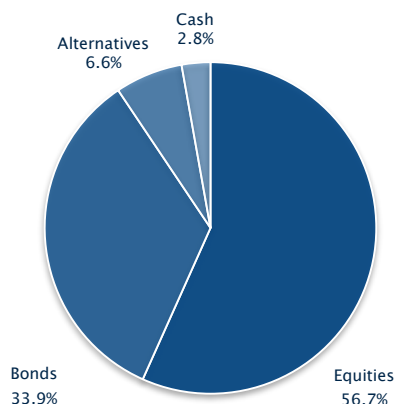
# OMI BENTLEY AUSTRALIAN DOLLAR BALANCED FUND

30<sup>TH</sup> SEPTEMBER 2018

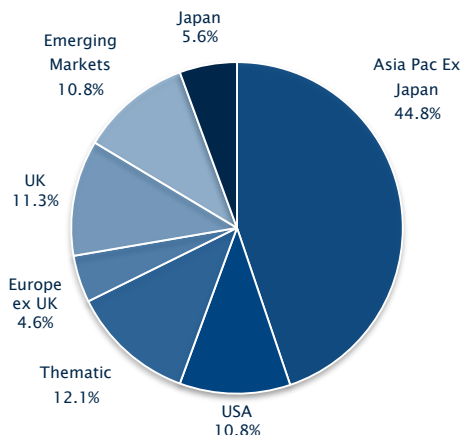
## INVESTMENT OBJECTIVE

The fund seeks to achieve an average annual return of CPI + 3% over any 5-year period, after all fees, with about half the risk of a pure equity exposure. Though the mandate favours equity investment, the investment manager has the latitude to actively allocate between different asset classes to protect values and reduce volatility. The fund aims to maximise returns in AUD terms.

### ASSET ALLOCATION



### EQUITY BREAKDOWN



## QUARTERLY INVESTMENT REPORT

US stocks have rebounded to all-time highs, but troubles are brewing elsewhere. UK and European indices are trading several percent below their 2018 peaks and many emerging markets experienced 20%+ losses over the summer. Global bond markets are drifting lower too, whilst commodity prices (bar oil) have seen renewed weakness.

There remains a risk that this is a temporary correction and not the material downturn we have been waiting for, but our bearish view now seems to be playing out. Protecting capital is our priority and the fund has not experienced anything like the double-digit drawdowns seen in many risk assets this year; the fund's price rose 0.1%, as a 2% fall in the Aussie dollar against the \$ aided the performance of the fund's overseas assets.

The fund price would have benefited further had some of its defensive positions performed better, but gold and the active managers that run short positions all struggled. We draw a degree of comfort from the fact that this basket of "protection" assets is yet to harvest the solid gains that typically come during "risk off" periods.

*continued overleaf*

## PERFORMANCE (NET OF FEES) \*

	3 MONTHS	YTD	1 YEAR	3 YEAR (ANN.)	5 YEAR (ANN.)
Fund	0.1%	0.4%	2.8%	1.1%	3.2%
Inflation (AUS CPI)**	n/a	n/a	2.1%	1.5%	1.7%

12 MONTHS TO	30 SEP 18	30 SEP 17	30 SEP 16	30 SEP 15	30 SEP 14
Fund	2.8%	2.0%	-1.5%	9.9%	3.0%

\* the fund's return is calculated net of the Insurance Bond Wrapper cost

\*\* the CPI figure is the actual inflation figure and is not adjusted to show the fund's target return. The 3 and 5-yr figures are annualised averages.



BENTLEY REID

### EQUITIES 56.7%

#### Asia Pac ex Japan 25.4%

Baring Australia	5.1%
Hermes Asia ex Japan	2.6%
iShares MSCI Australia ETF	10.8%
UBS Australia Equity	6.9%

#### Europe ex UK 2.6%

Invesco European Equity	2.6%
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#### United Kingdom 6.4%

City Financial Absolute Equity	2.3%
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Janus Henderson UK Absolute Return \$ Hedged	4.1%
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#### United States 6.1%

DB X-Trackers S&P Inverse ETF	4.0%
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iShares S&P 500 Financials	2.1%
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#### Japan 3.2%

Vanguard FTSE Japan ETF	3.2%
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#### Emerging Markets 6.1%

First State Stewart Latin America	1.9%
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iShares MSCI Emerging Markets ETF	1.9%
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Schroder EM Debt Absolute Return AUD Hedged	2.3%
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#### Thematic 6.9%

Fundsmith Equity	3.5%
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Kennox Strategic Value	3.4%
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#### ALTERNATIVES 6.6%

Pictet Physical Gold	6.6%
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#### BONDS 33.9%

Swisscanto AUD Bond Fund	16.4%
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UBS AUD Bond Fund	13.3%
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iShares Index Linked ETF	4.2%
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#### CASH 2.8%

We believe that gold and the various bond holdings should rally strongly if the US Federal Reserve signals an end to its tightening cycle; a scenario we expect to unfold in the coming months. Gold fell by 3% in Aussie dollar terms last quarter, but it is finding some buying support around U\$1,200/oz. We retain a 7% exposure to the physically-backed bullion ETF and plan to invest in cheap gold mining equities once the underlying gold price regains some positive momentum.

Similarly, we have been adding to longer-dated government bonds on the recent weakness. We completed the 4% allocation to the iShares UK index-linked ETF. The holding should produce a sizeable profit if UK real (inflation-adjusted) yields continue to fall. However, it was another tough quarter for City Financial, which tends to perform best when equity markets weaken; it declined by 12% with bets against US tech and healthcare stocks proving costly. City Financial is held in the portfolio as insurance and we are mindful that its 15% gain during the market sell-off earlier in the year was one of the reasons the overall fund held up so well.

There were wide-ranging returns across the equity positions last quarter. In hindsight the most profitable strategy would have again been to own expensive US equities and sell short most other assets. But with US stock valuations still at multi-decade highs, real returns are forecast to be negative over the coming years. As a result, the fund remains short the S&P 500 (but owns a US Financials tracker, which gained 6% last quarter) and long the much cheaper UK and emerging market (EM) listings. EM assets had a banner 2017 with the likes of Hermes Asia rallying by 35%, but this year has been a struggle with the stronger dollar causing widespread weakness. It is pleasing to see good stock-picking protecting the fund's dedicated EM positions last quarter; Hermes Asia and First State Latin America posted gains, whilst the Schroder EM Debt fund fell by only 2%.

With shades of panic-selling driving valuations to cheaper levels, we are keen to retain the modest EM allocation and may look to add if the sell-off intensifies. In the meantime, so that the fund can tolerate holding the more volatile EM positions we have slightly moderated its headline risk profile by redeeming FP Crux Europe and booking some profits on Fundsmith, which has averaged a 23% p.a. gain over the past 5 years.

We believe the fund's overall exposure is well balanced. It owns some cheap, albeit higher risk, EM and value equities that should generate solid returns over the coming years, whilst the bond and gold positions provide downside protection if risk assets continue to trend lower. It is reassuring that the 2018 market struggles are more consistent with our conservative stance and we are well aware of the need to curtail losses should a bear market take hold. This would reward our investors' patience as well as helping to protect the gains made in prior years. There remains a (slim) chance that we revert to a more "risk on" stance without a major market fracture, particularly if the Central Banks pro-actively resort to looser monetary policies, but for now stretched valuations, global growth concerns and less supportive liquidity conditions all argue for caution.

## PORTFOLIO ACTIVITY

INCREASE EQUITY EXPOSURE (55.5% to 56%):  
Buy City Financial UK Absolute (+0.5%)

INCREASE TARGET BOND EXPOSURE (31.4% to 34.2%):  
iShares Index-Linked Gilt ETF (+1.4%)

### FUND SWITCHES;

Buy Invesco European Equity (+2.5%)  
Sell Crux European Special Situations (-2.5%)

## KEY FACTS

Price	A\$1.876
Fund Size	A\$1.4m
Benchmark	AUS CPI + 3%
Launch Date	31/05/1998
Prices Published	<a href="http://www.bentleyreid.com">www.bentleyreid.com</a>

## CONTACTS

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