Morningstar International Shares (Hedged) Fund

Quarterly Performance Update

Q32016

All data and information as of September 30, 2016

APIR Code (Class A)	INT0050AU
Inception	07 Jul 2000
Size $m	252.9
Unit Pricing	Daily
Distributions	Quarterly
Management Fee	Up to 0.56%
Buy/Sell Spread	0.12% / 0.12%
Minimum Investment	$20,000

Investment Objective

Aims to deliver a superior risk-return profile to the performance benchmark (MSCI All Country World exAustralia Index with Net Dividends Reinvested (A$ Hedged)) over rolling seven year periods by investing predominantly in listed international shares, supplemented by a passive currency overlay.

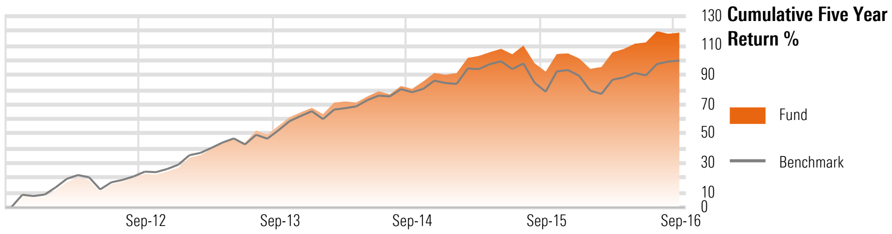
Investment Strategy

The Fund invests in listed international shares across developed and emerging markets and aims to deliver a superior risk-return profile to that of the performance benchmark. To achieve this aim, the Fund invests in an international equity strategy that is non-market cap weighted, incurs low turnover, and targets companies that exhibit desirable fundamental quality, value, and liquidity characteristics.

Key Features

Exposure to a diversified portfolio of international shares, provided at a low cost.

Performance [1]



Total Return %	3 Months	6 Months	1 Year	3 Years (pa)	5 Years (pa)
Fund (Net of Fees)	3.13	6.50	13.78	12.09	16.96
Benchmark	5.31	6.94	11.81	9.45	14.85
Active Return	-2.18	-0.44	+1.97	+2.64	+2.11

Portfolio Analysis [2]

Sector Allocations	%
Healthcare	18.3
Information Technology	17.5
Consumer Staples	15.1
Consumer Discretionary	15.0
Industrials	14.6
Telecommunication Services	5.2
Materials	5.1
Financials	4.4
Energy	2.4
Utilities	2.3
Cash	0.3

Regional Allocations	%
North America	58.2
Europe ex-UK	13.4
Japan	10.1
Emerging Markets	9.9
UK	5.6
Pacific ex-Japan	2.4
Cash	0.3

Top 10 Portfolio Holdings	%
Newmont Mining	1.3
NetEase	1.1
KDDI	1.1
NTT DoCoMo	1.1
Cisco Systems	1.1
General Dynamics	1.0
Quest Diagnostics	1.0
Raytheon	1.0
Microsoft	1.0
Dr Pepper Snapple	1.0

Notes

1. Performance measures are expressed after fees, costs and before taxes. Performance may not sum due to the rounding of individual components.
2. Allocations may not add up to 100% due to the rounding of individual components.
3. The Management fee is inclusive of GST (after taking into account Reduced Input Tax Credits) and can be negotiated for direct investors. Refer to the current disclosure document for more information on fees and costs.
4. Please refer to the Product Disclosure Statement on the Morningstar website for more information on how to apply.

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How the portfolio performed

Despite the extreme fear and panic that dominated markets at the start of 2016 and the more recent upheaval around Brexit, the fund generated 3.13% over the quarter. The previous quarter saw shares in riskier industries recover faster than those typically in more defensive industries (such as consumer staples, telecommunication services, and health care). The portfolio consists of higher quality shares that operate within more defensive industries. We were therefore relatively pleased with the portfolio's positive returns delivered over the quarter.

US technology shares were the primary drivers of performance. NetEase, a leading online game operator, was one of the stellar performers in this sector. Apart from developing some of the most popular online games, the company also provides email, e-commerce, and advertising services. The company has over 80 game titles in its mobile portfolio, including hits like "Fantasy Westward Journey Online." Recently reported results show that the firm continues to generate substantial cash flows and is easily able to cover outstanding debt using cash on hand. With a strong balance sheet and impressive ability to grow revenues and margins, NetEase is an ideal candidate for inclusion in the portfolio. NetEase's share price ended the quarter up 21.7%.

Linear Technology (Linear) was another great performer in the information technology sector. The company manufactures highly specialised integrated circuits, which require extreme precision and reliability. You may be using devices that have many of Linear's products within them, including mobile phones, computers, and automotive electronics. In late July, Analog Devices agreed to acquire Linear Technology at a 24% premium, offering US$60 per share in a mixture of cash and shares. Following the announcement, Linear's shares ended the quarter up 24.7%.

The investment strategy has been specifically designed to gain exposure to cheap, quality companies like Linear. We believe that the acquiring company holds the same view of Linear that we do, i.e. that it is a high-quality company, trading at reasonable valuation multiples.

Exposure to Campbell Soup weighed on performance over the quarter. Aside from being in one of the more defensive sectors, which underperformed over the quarter, the company suffered from self-inflicted execution errors. These errors included the recall of 3.8 million bottled protein shakes due to possible spoilage, weather, quality and customer service issues within its carrot business. The shares ended the quarter down 19.6%.

Despite these issues, the company still maintains its dominant position in the US soup industry. Investments to reinvigorate its product portfolio should see the company continue to generate strong cash flows. We also note the company's ability to meet capital expenditure and meet its dividend payments and share repurchases, while at the same time paying down borrowings. These are the characteristics that we seek to include in the portfolio. We believe that the company can correct its past mistakes and will continue to monitor progress in this regard.

Japanese fashion company Shimamura also hurt performance as the shares tanked, ending the quarter down 19.8%. The decline followed weaker than expected same-store sales growth. This knee-jerk reaction ended up costing investors, as the shares recovered following better than expected results in early October. In our view, Shimamura remains an attractive company operating in a challenging economy. Shimamura's financial position is strong, with no long-term liabilities and cash on hand to cover short-term debt. The company continues to generate strong cash flows, allowing for dividend payments and share repurchases.

We believe the portfolio's focus on quality and reasonable valuations, along with holistic diversification, will continue to deliver substantial reward for risk outcomes for investors over the long term.

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Morningstar's Investment Principles

We put investors first. We believe the firms that put investors first win in the long term because their investors win.

Since 1984, Morningstar, Inc. has been helping investors reach their financial goals. Our fiduciary duty to our principals is paramount.

We're independent-minded. To deliver results, we think it's necessary to invest with conviction, even when it means standing apart from the crowd.

Our research shows that making decisions based on fundamental analysis, rather than short-term factors and sentiment, delivers better long-term investment results.

We invest for the long term. Taking a patient, long-term view helps people ride out the market's ups and downs and take advantage of opportunities when they arise.

Investing with a multi decade horizon aligns with investors focus on increasing their purchasing power over their lifetimes.

The long term is the only period where fundamental, valuation driven investing works.

We're valuation-driven investors. Anchoring decisions to an investment's fair value—or what it's really worth—can lead to greater potential for returns.

Valuation-driven investing through a long-term focus on the difference between price and intrinsic value enables investors to get more than they're paying for.

We take a fundamental approach. Powerful research is behind each decision we hold, and we understand what drives each investment we analyse.

Fundamental investing incorporates a focus on the future earnings of an investment and not its prospective price change.

We strive to minimise costs. Controlling costs helps investors build wealth by keeping more of what they earn.

Investment returns are uncertain, but costs are not.

Lower costs allow investors to keep more of their returns.

We build portfolios holistically. To help manage risk and deliver better returns, truly diversified portfolios combine investments with different underlying drivers.

Portfolios should be more than the sum of their parts.

True diversification can have a powerful impact on a portfolio's risk-adjusted returns – but simply holding more investments isn't the same as true diversification.