

Morningstar Australian Shares Fund **Q3 2018**

All data and information as of September 30, 2018

Quarterly Performance Update

Inception	07 Jul 2000
Size \$m	289.8
Unit Pricing	Daily
Distributions	Quarterly
Management Costs	Up to 0.41%
Buy/Sell Spread	0.07% / 0.07%
Minimum Investment	\$10,000

Investment Objective

To achieve meaningful capital growth over the medium to long term, while minimising the risk of permanent capital loss, by investing predominantly in listed Australian shares

Investment Strategy

The Fund invests predominantly in listed Australian shares with the aim of producing superior long-term total returns relative to the benchmark. To achieve this aim, Morningstar constructs a well-diversified portfolio of companies that exhibit desirable fundamental quality and/or value characteristics.

Available to wholesale investors, and indirectly to retail investors via select retail platforms.

Tax-effective strategies are used to increase the after-tax alpha to investors:

- × Centralised Portfolio Management (CPM) techniques are included (where investment decisions for a number of the managers are aggregated at a centralised dealing desk) saving transaction costs and potential capital gains tax realisations; and
- × A portion of the portfolio is allocated directly to tax-effective, value-orientated mandates.

Performance¹



Total Return %	3 Months	6 Months	1 Year	3 Years (pa)	5 Years (pa)
Fund (Net of Fees)	1.07	5.84	11.26	11.10	7.96
Benchmark	1.50	9.99	14.03	12.16	8.19
Active Return	-0.43	-4.15	-2.77	-1.06	-0.22

Portfolio Analysis²

Market Capitalisation	Fund %	Bmark %	Top/Bottom 5 Divergent Stock Positions	+/- Bmark %
50 Leaders	19.7	75.9	Kathmandu Holdings	+3.2
51 - 100 Leaders	16.7	12.4	Trade Me Group	+3.2
Ex - 100 Leaders	63.4	11.7	ResMed	+3.0
Cash	0.2	0.0	Contact Energy	+2.9
			Super Retail Group	+2.9

Active Sector Positions	+/- Bmark %
Consumer Discretionary	+24.8
Industrials	+6.7
Information Technology	+4.4
Utilities	+0.9
Healthcare	+0.4
Telecommunication Services	+0.4
Consumer Staples	-0.3
Materials	-3.6
Energy	-4.0
Property Trusts	-6.3
Financial ex-Property Trusts	-23.6
Cash	+0.2

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. The Fund also has exposure to underlying investment managers which charge performance fees and these are an additional cost to you and impact the return.

4. Please refer to the Product Disclosure Statement on the Morningstar website for more information on how to apply.

How the portfolio performed

The Morningstar Australian Shares Fund generated 1.07% over the quarter. The fund continues to invest in companies that are high quality and trading at discounts to their intrinsic value, with us believing that high quality companies will generate wealth for shareholders over the longer term and companies that are now undervalued, will revalue to their true worth over time. On this basis, the fund has performed relatively well and most importantly, has stayed true to label. And while this approach may not be flavour of the month (or even year) as growth stocks continue their recent outperformance over value peers, we trust that investors will see relative outperformance from this strategy, particularly during times of market uncertainty.

Spark New Zealand is one of the best performing value stocks in the portfolio and has been a holding for the past two years. The company has a strong market position in the New Zealand telecom market, aided by infrastructure. This allows Spark New Zealand to offer a superior mobile network, attracting high-end subscribers seeking premium wireless services. There were a number of issues contributing to the market undervaluing the company. These include growing concerns over the company's declining market share in broadband subscribers, the New Zealand's government's ultrafast broadband launch (with the objective of connecting 80% of homes to a new fibre to premises network by 2022), and the increasing competition in the telecom-media space.

As the market became increasingly concerned with the abovementioned factors, we found comfort in the company's low levels of debt, with no major refinancing commitments in the future. We were also pleased with the market's undervaluation of the reliable free cash flow generation. In addition, Spark's significant infrastructure underpins its mobile operations in a country with a relatively small population, providing a natural barrier to increasing competition. With this, we were comfortable to build a position in a stock that was undervalued, and our clients have received impressive levels of compensation (+21% in the past six months). We will continue seeking out companies like Spark New Zealand. The philosophy of buying companies trading at levels less than their fair value and selling them when they re-rate and become expensive is logical and repeatable and is key to delivering long term returns, in our view.

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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.