

Touchstone Index Unaware Fund

Performance update

As at 30 September 2017

Performance

September 2017	1 month	3 months	6 months	1 year	Since Inception** p.a.
Fund	+0.39%	-0.11%	-1.17%	+9.63%	+12.17%
Benchmark*	+0.04%	+0.80%	-0.78%	+9.02%	+13.86%
Value added	+0.35%	-0.90%	-0.39%	+0.61%	-1.69%

Performance figures are net of fees and expenses. *S&P/ASX 300 Accumulation Index. **Inception date is 4 April 2016.

Market Review

The Australian equity market, as measured by the S&P/ASX 300 Accumulation Index, ended the month of September 2017 largely flat, despite volatile intra-month trading. Weakness in commodity prices saw a pullback in the Resources sector. In addition, the Telcos and Utilities sectors fell as rising bond yields saw weakness across most bond proxy sectors. In contrast, Financials posted gains as expectations of higher rates resulted in the yield curve steepening in the month. The Healthcare sector was also a solid performer, aided by a weaker Australian dollar (AUD).

The performance of the market over the quarter was disappointing, rising modestly by 0.8% and underperforming major international equity markets. The main influence over the quarter was the lacklustre reporting season, which led to a reduction in earnings forecasts for FY18 for the market in general. Declines in the Financial sector—following CBA's money laundering allegations together with general weakness in insurance companies over the period—also impacted. The Telco sector was also soft after Telstra management outlined a new dividend/capital allocation policy at their full year result release, which disappointed the market. The higher AUD versus the US dollar (USD) over the quarter impacted those firms with large US denominated earnings, such as Healthcare and Industrials. Conversely, the Energy and Resources sectors were strong in the quarter, with the latter trimming some of its gains at period end following a pullback in commodity prices.

In contrast, global sharemarkets were generally firmer in the month and the quarter. In the US, the Dow Jones Industrial Average (+2.1% mom, +5.0% qoq), S&P500 (+1.9%, +4.0%) and Nasdaq Composite (+1.1%, +5.8%) traded at new record highs, with the market shrugging off higher interest rate expectations. Firmer economic data, together with solid US corporate earnings, aided sentiment.

Domestic economic data was mixed in September, with business conditions once again showing upside, but the consumer remained weak. The RBA made no change to the cash rate of 1.5% for the twelfth month in a row. In its statement the Board expressed confidence that "stronger conditions in the labour market should see some lift in wages growth over time". The AUD was up +2.0% over the quarter, but retraced some of its recent strength against the USD, falling -1.4% to \$0.784 over the month.

Top 5 Shareholdings

Company
National Australia Bank
Westpac Banking Corporation
Wesfarmers Limited
QBE Insurance Group
Insurance Australia Group



Touchstone Index Unaware Fund

Monthly performance update

As at 30 September 2017

Performance Review

The portfolio outperformed the market over the month, advancing by +0.4% after fees versus a flat benchmark return. Pleasingly, the Fund has advanced by +9.6% over the year and outperformed its benchmark by +0.6%.

A number of key positions contributed to performance for both the month and quarter. Mantra (+8.9% mom, +6.7% qoq) benefited from the release of ABS data, which showed that inbound tourism continued to grow at high single-digit rates with arrivals from mainland China growing at closer to 20%. At the time of writing, Mantra has confirmed media speculation that it has received an indicative and non-binding proposal from Accor SA at \$3.96 per share.

Bingo Industries (+4.8% mom, +18.9% qoq) was also a strong contributor over the month and quarter, as the company continues to gain market support following the release of its maiden profit result which was circa 3% above prospectus. The company also upgraded its FY18 guidance over 10%. The highlight was the expansion into Victoria, which is expected to generate in excess of 20% earnings growth over the next three years.

Conversely, Treasury Wine Estates (-5.5% mom, +5.0% qoq) detracted in the month. The company reversed some of its strong gains from August, but was a strong contributor over the quarter.

QBE detracted in both the month and quarter (-4.1% mom, -13.5% qoq), as the insurer was impacted by a number of catastrophe events that will cost an additional US\$600m. We believe the drivers for an earnings uplift are in place, with signs that the insurance pricing cycle has turned up. Post month-end the company rallied as the market has become more optimistic regarding the outlook for firmer insurance pricing, as 2017 is now the worst insured catastrophe year on record.

Market Outlook

The Australian equity market has been range-bound for the past six months and has posted disappointing performance compared to global sharemarkets. Weakness in consumer spending, rising input costs and increased competition will continue to weigh on the outlook for earnings growth. For the Banking sector, we see the growth outlook for FY18 as challenging given modest volume growth, limited potential for further loan book repricing, diminishing tailwinds from credit writebacks and a difficult political environment. For Resources, we continue to anticipate that commodity prices will decline from current levels, tempering their profit outlook.

Against this backdrop of weakness across our major market sectors, we believe that bottom up stock selection is paramount in driving portfolio returns. Opportunities remain for individual companies to post strong returns, despite the broader market environment.

We also believe that risks remain elevated globally. International financial markets have continued to rally, some to ever increasing highs, yet uncertainty in terms of policy settings, interest rates and geopolitical risk generally remains high.

Our thesis remains unchanged that given the heightened uncertainty, the market remains very vulnerable to an exogenous shock. As such we remain cautious and have reflected this in our portfolio positioning.

Touchstone's takeaways:

- Revenue growth remains difficult – tight cost management takes on added significance
- Highly-g geared capital structures are riskier in this environment, even with low interest rates
- Heightened geopolitical uncertainty

Downside protection remains at the fore of our investment decisions.

Contact details

For more information, call 1800 895 388 (AU) or 0800 442 304 (NZ) or visit touchstoneam.com.

The Fund is managed by Touchstone Asset Management, a Bennelong Funds Management boutique.

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