Fund Manager Commentary

January 2018

BT Investment Management

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Australian Shares

BT Wholesale Core Australian Share Fund

Market review

The domestic equity market started 2018 on a downbeat note, with the S&P/ASX 300 Accumulation Index finishing January down 0.39%. While **Resources (+0.8%)** recorded a small gain amid strong commodity prices, it was more than offset by the weak performance from **Industrials (-0.7%)**. The market also continued to lag global peers, with the S&P500 finishing the period 5.3% higher in USD terms.

The major macro themes over the month include a weakening US dollar, which has led to rising commodity prices; and rising global bond yields against the backdrop of synchronised global economic growth. As such, miners were generally supported in January with **Metals & Mining** edging 1.2% higher. The major miners finished the month in the black, supported by well-received market updates and iron ore remaining above US$70 per tonne. **BHP (BHP, +2.1%)** reported a record quarterly iron ore production at Pilbara; while dropping its FY18 production guidance for coking coal due to operational issues at Broadmeadow and Blackwater. **Rio Tinto (RIO, +1.4%)** also released its Q4 production update, hitting its production guidance at Pilbara following a record shipment of 357Mt. Copper volumes were also solid due to the production ramp-up at RIO's Escondida mine, and improved ore grade at Kennecott Utah Copper (KUC) division. Slightly weighing on an otherwise strong set of results was the realised coal price – the reported US$78/t for thermal coal and US$164/t for met coal were both below market prices. Partially helped by the miners, **Materials (+0.5)** was one of the few sectors which finished the month in the black.

Also residing within the winner's group, **Health Care (+3.1%)** was the largest contributor to the headline index performance. Sector heavyweight **CSL (CLS, +3.6%)** recorded a positive month in January. While there was no company-specific news attached, investor sentiment was helped by the two acquisition deals announced by French pharmaceutical giant Sanofi, totalling US$17 billion over the month. Also adding to the sector's positive performance was the strong return from **Resmed (RMD, +13.5%)** and **Sirtex Medical (SRX, +66.2%).** The former reported a good set of Q2 results across the board: sales growth of the flowgen machines did not decelerate as some had feared; while sales of the high-margin masks also grew at double digit rates globally. For Sirtex, an all-cash acquisition offer from Varian Medical, which represents a 19x multiple for SRX's FY1 EBITDA, was well received by the market.

On the other side of the ledger, **Utilities (-4.3%)** was the worst performing sector over the period. The pickup in bond yields continued on the back of synchronised global economic growth and was evident both overseas (US 10-year Treasuries added 31bps over the month to yield 2.72%) and back at home (the Australian counterpart added 16bps to yield 2.79%), which weighed on bond sensitive sectors. For similar reasons the **Real Estate (-3.2%)** sector got dragged into the red as did infrastructure companies including **Transurban (TCL, -3.3%), Sydney Airport (SYD, -3.4%)** as well as **Macquarie Atlas (MQA,**

-8.7%). Last but not least, all the Big Four banks slid moderately over the month, from -1.8% (CBA) to -0.6% (ANZ), driving the broader **Financials (-0.7%)** sector into negative territory. The banks are yet to provide trading updates in February.

Finally on the global macro front, global bond markets suffered in January, while risk assets enjoyed a strong start to the year. Sentiment was supported by the passage of US tax reform, a strong US corporate earnings season and an absence of major geopolitical disruptions. The Federal Reserve left rates unchanged at their January gathering, but offered a more upbeat outlook for inflation. Meanwhile, US economic data was mixed with weaker-than-expected payrolls and fourth quarter GDP. In contrast, leading indicators like the ISM manufacturing survey ticked higher as did the Conference Board gauge of consumer confidence. In Europe, the ECB left its policy settings unchanged and noted that while broader economic data continued to improve a stronger inflation pulse remained absent. President Draghi also added that a rate hike would be unlikely over 2018 and the Euro's recent appreciation could complicate the outlook. European economic data was stronger across the board with a 1.5% jump in retail sales, a 0.5 point increase in the Composite PMI, a 17 year high for sentiment and a 0.10% fall in the unemployment rate. Meanwhile in Asia, China recorded a healthy 6.8% GDP growth rate for 2017.

Portfolio performance

The BT Wholesale Core Australian Share Fund returned 0.27% (post-fee, pre-tax) in January 2018, outperforming its benchmark by 0.66%.

Contributors

Overweight JB Hi-Fi

Electronics retailer **JB Hi-Fi (JBH, +17.2%)** enjoyed a strong start to the year, bouncing back from weakness in H2 2017 as the skies did not fall in on the day that Amazon launched its expanded offering in Australia. Strong November retail sales figures, bolstered by the release of the iPhone X and 'Black Friday' have also supported the retailer's price. Going from here, there is little doubt that Amazon's proposal and effect on the market will expand, however we remain confident that JBH is among the best-placed companies in Australia to deal with increased competitive intensity. Even with its price spike this year, it remains towards the lower end of its long-term price/earnings band. We continue to like the brand.

Overweight Qantas

National airliner **Qantas (QAN, +4.6%)** remains our largest active position within the portfolio. Higher oil prices and some technical selling related to the index weighed on Qantas in the last half of 2017 however it regained some upward share price momentum over January. While the share price of Qantas has almost doubled since bottoming out in June 2016, the company remains attractive on share price valuation compared to its global peers. We believe the market has not yet priced in its ability to sustain its recent turnaround in earnings, based on the stable competitive environment that has emerged in domestic skies.

Overweight Resmed

Respiratory device manufacturer **Resmed (RMD, +13.5%)** is one of our long-term holdings. It reported good Q2 results during the month: sales growth of the flowgen machines hasn't decelerated, while sales of their high-margin masks have also been growing at double digit rates globally. In addition, the distributors of RMD's products, the DME (Durable Medical Equipment) suppliers, are under increasing regulatory and compliance pressure to do more granular reporting on their patients. This underpins the strong demand for Resmed's products, which help the DME suppliers meet these obligations. Being US domiciled, Resmed will also benefit from the latest tax reforms, albeit only shortly: the underlying tax rate is expected to drop to 15% (from 21%) for the second half of FY18, but will revert back to 21% following the passage of anti-hybrid tax legislation in Australia. We continue to hold RMD in our portfolio.

Overweight BHP

Amid a weakening US dollar, and continuing strong demand from China, commodity prices remained buoyant over the month and the iron ore price in particular stayed above US$70. This has benefited the domestic miners in general, and diversified miner **BHP** finished the month 2.1% higher. In January, the company reported a record quarterly iron ore production at Pilbara, while dropping its FY18 production guidance for coking coal due to operational issues at Broadmeadow and Blackwater. We continue to favour the diversified miner due to its strong business fundamentals and improved capital discipline. We also expect the upcoming sale of its US onshore business to lead to additional shareholders returns.

Detractors

Not holding South 32

It was another positive month for diversified miner **South 32 (S32, +9.5%)** after the company provided the market with its Q4 production results. Guidance was largely maintained apart from manganese production in South Africa, which was lifted by 8%. However, management reaffirmed that cost guidance is under pressure (first flagged at S32's investor day) Revised numbers will be provided with the company's upcoming trading update in February.

Overweight Macquarie Atlas

It was a tough month for toll road operator **Macquarie Atlas (MQA, -8.7%)**, as rising global bond yields weighed on bond sensitive stocks. The pick-up in bond yields continued in January on the back of synchronised global economic growth and was evident both overseas (US 10-year Treasuries added 31bps over the month to yield 2.72%) and back at home (the Australian counterpart added 16bps to yield 2.79%). We continue to hold MQA in our portfolio given its strong asset portfolio.

Overweight Santos

The share price of oil and gas producer **Santos (STO)** pulled back during January, finishing the month 6.4% lower. STO had a strong share price run over the second half of 2017, as oil prices remained elevated due to agreement achieved/extended by OPEC and Russia to curtail their production volumes. The revelation of a proposed acquisition offer from oversea oil company Harbour Energy in November also supported investor sentiment. There wasn't any new company specific news over the month and we suspect the slide was largely attributed to profit-taking.

Overweight Amcor

The share price of packaging company **Amcor (AMC)** slid by 5.6% in January ahead of reporting on what management had flagged will be a tough half. Rumours from last year around Amcor's potential takeover of its global peer, Bemis, failed to spark any further media coverage after management responded vaguely without much clarity, stating that Amcor regularly assesses a range of strategic options. We continue to hold AMC in the portfolio as a capital defensive/yield position, with strong consistent free cash flow and potential for capital management.

Strategy & outlook

The portfolio gained ground in January, in contrast to the broader market's decline. There was a wide range of drivers, with our positions in resources (BHP), growth stocks (ResMed), and our cohort of previously-unloved industrial cyclicals (Qantas and JB Hi-Fi) all making notable contributions. Bond sensitive stocks underperformed – including our position in Macquarie Atlas. However in an environment of rising bond yields and, in many cases, elevated valuations among these stocks, we are underweight this segment of the market as a whole, which was beneficial for performance.

Investor fears of a pullback in equities – following a relatively long period of unusually low volatility – came to fruition in early February. Stronger-than-expected wage inflation data in the US prompted speculation that the Federal Reserve would hike interest rates more aggressively than previously thought. This saw bond yields spike and equity market volatility surge.

There are several points to make about the outlook for Australian equities from here, on the back of this action. The first is that, at this point, we do not believe that this presages a sustained bear market. Market valuations are not extreme in Australia, which has not participated in the recent surge in global equities, due in part to the more defensive nature of the ASX, with a much lower proportion of health care and technology companies than, say the S&P 500. The aggregate price/earnings multiple for the S&P/ASX 200 is above its long-term average, but this is entirely consistent with the low level of domestic interest rates – and the RBA is giving little indication that it plans to hike aggressively this year. As a result, the Australian market retains an element of valuation support. This has been evident in the first week of February where the downward moves in the S&P/ASX have been less than its American counterpart.

The second point to note is that underlying economic conditions remain benign. The risk is, of course, that aggressive tightening by the Fed stymies the pace of growth in the US. However we believe they are sensitive to that risk and that the pace of tightening – both in the US and globally – will remain relatively moderate. Australia's growth remains muted but stable, with a pick-up in corporate capital expenditure and the pipeline of transport infrastructure projects providing some tailwinds for further growth. The Australian dollar's pull-back from recent highs against the USD will also help companies with overseas earnings. All in all, as we move into a reporting season with expectations of reasonable – if not exciting – earnings growth there appears to be few signs of the economic weakness which might prompt a bear market.

We remain mindful of the risks in the local market. We consider roughly 30% of the S&P/ASX 300 to be significantly sensitive to bond yields; we are underweight this segment, but a sustained pick up in yields could see these stocks drag on the market as a whole. There is also a significant cyclical exposure – particularly through resources – which may be vulnerable if US rates go up faster than anticipated. We will monitor yield-driven factors in the market, however our more immediate focus as we head into reporting season is that it feels like the market is already positioned for the more obvious results. The risk here is that many of the stocks expected to deliver good results have already outperformed and may actually underperform post report, in a case of "buy the rumour, sell the fact." This also leaves scope for the market's most recent unloved – including index heavyweights such as the banks and Telstra – to do better than has been the case in recent months.

BT Wholesale Smaller Companies Fund

Market review

The Australian small cap market gave back some of its previous gains in January, with the S&P/ASX Small Ordinaries Accumulation Index recording a loss of 0.5%, as both **Industrials (-0.4%)** and **Resources (-0.9%)** pulled back. For the first time since April 2017 the small cap index underperformed the broad market S&P/ASX 300 Accumulation Index (by 15bps).

Performance was positive for the majority of sectors, however all the Index heavyweight sectors, including **Materials (-3.6%)**, **Consumer Discretionary (-1.7%)** and **Real Estate (-4.6%)** finished January in the red. A meaningful pullback by lithium miners was the big contributor to the Materials sector's relatively poor performance, with notables including **Mineral Resources (MIN, -11.0%)**, **Pilbara Minerals (PLS, -15.2%)** and **Galaxy Resources (GXY, -13.3%)**. Lithium miners all rallied significantly in the second half of 2017 (with some of them doubling their market value within months), underpinned by expected demand for lithium-ion batteries from the flourishing EV industries in the EU and China. While that broader theme still runs hot, investors decided some profit-taking was in order over January, with some concern over an increase in supply providing the excuse. **Orocobre (ORE, +3.4%)** was the outlier amongst the lithium miners over the month, as the market supported management's decision to raise additional equity capital to more than double production capacity at its Argentina operation. Partially offsetting some of the negative impact from the lithium miners, **Independence Group (IGO, +5.7%)** and **Perseus (PRU, +13.3%)** benefited from a rising gold price amid a weakening dollar. The two miners also provided production updates where quarterly gold production volume increased by 11% and 19% respectively.

Consumer Discretionary also put a dent on the headline index performance. Solid performance came from **Nine Entertainment (NEC, +9.4%)**, as the latest TV data was seen supportive of TV ad spending, which is now back on the rise. However, this was more than offset by poor performance from the likes of **Navitas (NVT, -14.1%)** and **Village Roadshow (VRL, -9.8%)**. English language course provider, Navitas saw a drop in its net profits of more than 50%, as college closures as well as a weakening demand from migrants for English courses dragged on the company's financials. Theme park operator Village also warned investors that its 1H results would be "substantially below" the previous period as the challenging operating environment persists. Embattled domestic food retailer, **Retail Food Group (RFG, -20.9%)** also continued to underperform, extending its share price loss to 65% in just two months' time.

On the other side of the ledger, **Energy (+4.6%)**, **Information Technology (+2.9%)** and **Health Care (+2.9%)** had the best sector performance in absolute terms over the month. Standouts included oil and gas explorer **AWE (AWE, +10.9%)**, payment solution provider **Afterpay (APT, +23.3%)** and liver cancer treatment specialist **Sirtex (SRX, +66.2%)**. Acquisition offers from oversea bidders saw the share price of AWE and SRX surge – the former received its third rival bid from Mitsui, trumping offers from Mineral Resources and China Energy Reserve and Chemical Group; whereas the all-cash offer received by SRX from US bidder Variant Medical system represented a 19x multiple for SRX's FY1 EBITDA. Afterpay on the other hand flagged the strong trend of its sales growth, now heading beyond A$2 billion, and a possible move into the US market.

Finally on the global macro front, global bond markets suffered in January, while risk assets enjoyed a strong start to the year. Sentiment was supported by the passage of US tax reform, a strong US corporate earnings season and an absence of major geopolitical disruptions. The Federal Reserve left rates unchanged at their January gathering, but offered a more upbeat outlook for inflation. Meanwhile, US economic data was mixed with weaker-than-expected payrolls and fourth quarter GDP. In contrast, leading indicators like the ISM manufacturing survey ticked higher as did the Conference Board gauge of consumer confidence. In Europe, the ECB left its policy settings unchanged and noted that while broader economic data continued to improve a stronger inflation pulse remained absent. President Draghi also added that a rate hike would be unlikely over 2018 and that the Euro's recent appreciation could complicate the outlook. European economic data was stronger with a 1.5% jump in retail sales, a 0.5 point increase in the Composite PMI, a 17 year high for sentiment and a 0.10% fall in the unemployment rate. Meanwhile in Asia, China recorded a healthy 6.8% GDP growth rate for 2017.

Portfolio performance

The BT Wholesale Smaller Companies Fund returned -0.91% (post-fee, pre-tax) in January 2018, underperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.37%.

Contributors

Overweight The A2 Milk Company

A2M **(A2M, +12.5%)** announced it would begin to roll out its dairy products to vendors in the North-Eastern United States, including the states of New York, New Jersey, and Massachusetts, with first deliveries beginning immediately. This – in addition to its existing presence in California and the South Eastern states – will give the company exposure to 20% of the milk volume category in the US, according to management.

Overweight Bapcor

Bapcor **(BAP, +3.3%)** has underperformed over the last six months of 2017, failing to participate in the broader market's surge. This is likely to be at least partly due to its retail exposure, where investors have been nervous ahead of Amazon's arrival in Australia in December. There may be some impact from Amazon, over time, on auto accessories sales, however we believe that BAP's core business of trade and wholesale distribution of auto parts enjoys some protection from the effects of Amazon. This relatively defensive profile means BAP is among our preferred exposures to Australian consumers.

Detractors

Underweight Sirtex Medical

Sirtex **(SRX, +66.2%)**, which designs and manufactures drugs to treat liver cancer, has had a difficult period following setbacks in a key medical trial. However, it surged in January following an all-cash takeover bid from US-listed firm Varian Medical Systems.

Underweight Bellamys Australia

Dairy product company Bellamys (BAL, +42.1%) upgraded its revenue and profit target in January following a pick-up in Chinese consumption. This was a significant turnaround for BAL, which has endured a torrid time of late following a series of profit downgrades and a surge in excess inventory. At this point, A2 Milk remains our preferred exposure in this space.

Review and outlook

The small cap sector paused for breath following the surge of the last six months, and the portfolio gave back a little of its strong absolute gains from that period. Holdings in lithium-related miners provided a key drag, as some concerns about additional supply prompted a bout of weakness in the sector. This ultimately offset good performance from tech holding Altium and the A2 Milk company, among others. The portfolio was slightly behind its index in January. Some of the highest-conviction positions, such as Bapcor and Ryman Healthcare, made a good contribution. However, this was largely offset by the lack of a position in Sirtex Medical, which was up over 66% following a takeover bid.

Investor fears of a pullback in equities – following a relatively long period of unusually low volatility – came to fruition in early February. Stronger-than-expected wage inflation data in the US prompted speculation the Federal Reserve would hike interest rates more aggressively than previously thought. This saw bond yields spike and equity market volatility surge. There is evidence to suggest the rapid adjustment in low-volatility strategies exacerbated the market's ructions and saw a bout of technical selling.

There are several points to make about the outlook for Australian small cap equities from here, on the back of this action. The first is that, at this point, we do not believe that this presages a sustained bear market. Broad market valuations are not extreme in Australia, which has not participated in the recent surge in global equities, due in part to the more defensive nature of the ASX, with a much lower proportion of health care and technology companies than the S&P 500. The aggregate price/earnings multiple for the S&P/ASX 200 is above its long-term average, but this is entirely consistent with the low level of domestic interest rates – and the RBA is giving little indication that it plans to hike aggressively this year. As a result, the Australian market retains an element of valuation support. This has been evident in the first week of February where the downward moves in the both the broad S&P/ASX 200 and the S&P/ASX Small Ordinaries have been less than their American counterparts.

The second point to note is that underlying economic conditions remain benign. The risk is, of course, that aggressive tightening by the Fed stymies the pace of growth in the US. However, we believe they are sensitive to that risk and that the pace of tightening – both in the US and globally – will remain relatively moderate. Australia's growth remains muted but stable, with a pick-up in corporate capex and the pipeline of transport infrastructure projects providing some tailwinds for further growth. The AUD's pull-back from recent highs against the USD will also help companies with overseas earnings. All in all, as we move into a reporting season with expectations of reasonable – if not exciting – earnings growth there appears to be few signs of the economic weakness which might prompt a bear market.

International Shares

BT Concentrated Global Share Fund

Market review

Global equity markets commenced the year with strong returns in January, although further strength in the Australian dollar reduced the local currency gains, with the MSCI World ex Australia Total Return (A$) Index returning 1.8%. Markets were buoyed by reports of positive earnings momentum in US economies, strengthening indicators of economic growth in the major economies and the positive impact of tax cuts and concessions for US Corporations. Prices for key commodities were aligned with the pro-growth market sentiment, which saw oil break through the US$60/bbl level and iron ore remain above US$70/mt. Base metals were also generally higher. Bullish conditions in capital markets have pushed the MSCI World ex Australia (A$) Index to its sixth consecutive year of strong positive returns.

Stock prices in the US reflected the combined effect of good earnings growth, strong labour and consumer markets, and strong economic growth to register its strongest start to the year since 1987.

Investors looked passed the temporary Government shutdown that ensued following an impasse at Congress to approve budgetary measures. The greatest source of optimism seemed to come from Trump's corporate tax cuts which are expected to result in higher corporate earnings. At a sector level, Consumer, Technology and Health Care sector were among the best performers, while Utilities and Real Estate sectors were the weakest, given their quasi status as bond proxies. The S&P500 rallied strongly to record a 5.7% return while the Nasdaq was up 7.4%.

Most major European equity markets delivered healthy gains to commence the year, with the German DAX (+2.1%) and the French CAC (+3.2%) benefitting from growing optimism for the euro area. The region recorded further GDP expansion, with a 0.6% growth rate for the fourth quarter of 2017 marking 19 quarters straight of expansion. Private sector surveys across the region also supported the positive reading, although inflation indicators remain muted which is likely to limit progress for the European Central Bank in normalising monetary policy.

By contrast, the UK market weakened, losing value for the month in response to upward revisions to US interest rate expectations and a corresponding increase in government bond yields. Despite strong commodity prices, market sentiment was focused on the prospect of a hard Brexit scenario and signs of weakness in consumer-related sectors. The FTSE Index declined by 2.0% for the month.

The performance of Asian markets was more varied, with Hong Kong's Hang Seng rising by 9.9% and in significant contrast to Japan's Nikkei return of 1.5%. Chinese equities were beneficiaries of higher economic growth expectations and a weaker US dollar,

The Australian dollar had a mixed month on currency markets, finishing 3.5% stronger against the US dollar and 3.6% higher against the Hong Kong dollar, but weaker against the British pound (-1.5%) and euro (-0.2%). The local currency was a direct beneficiary of stronger commodity prices and stabilising demand from China.

Portfolio performance

The BT Concentrated Global Share Fund returned 2.55% (post fee, pre-tax) in January 2018, outperforming its benchmark by 0.80%.

We once again find ourselves in the midst of the US quarterly reporting season, with approximately 30% of S&P 500 companies having reported earnings in January. Of the companies that have reported, 80% have delivered earnings which have exceeded consensus estimates, with aggregate earnings growth being 12% .The passing of the US tax reform has allowed companies to announce the estimated financial impact, and in the most part is leading to consensus earnings upgrades for 2018 and beyond. Leading economic indicators also continue to suggest a continuing improvement in business conditions. With the strongest start to the year for the MSCI All Country World Index in two decades, markets are clearly taking note.

On the heels of the "scale matters" comments from Broadcom in December 2017 in relation to their proposed acquisition of Qualcomm, our holding in analogue semiconductor company, Maxim, was up 16% this month. The gain was in part due to press reports suggesting a possible takeover by Japanese semi-conductor company, Renesas. The company has subsequently denied that any discussions with Maxim has taken place. Whilst we have no insight into the validity or otherwise of the press reports, we prefer to focus on Maxim's fourth quarter 2017 report, which was announced this month. Second quarter net revenues were +13% over the year, gross margins increased to 67.6%, with management announcing that as a result of their confidence in the business outlook, 100% of free cash flow would be returned to shareholders (from 80% previously). The industrial and automotive sectors now account for 49% of Maxim's revenue, up from 37% three years ago. Management expects continued strong growth from both sectors, with factory automation and battery management systems for cars being prime drivers of what they consider to be secular growth. This same sentiment has been echoed by a number of semi-conductor companies over the past twelve months. The strategic benefit of having a strong suite of products across the industrial and automotive sectors is becoming increasingly evident.

The 9% rise in the Hong Kong Hang Seng Index this month, coupled with turnover data for the Q4-2017 was the driver behind the 17% gain for our holding of HK Exchange this month. Securities turnover rose 16% over the previous quarter, with derivatives turnover also up 5%. The virtual monopoly in the HK market across services including listing, trading, clearing and settlement, and also a dominant positon in the offshore China market has translated to a business model with significant pricing power and resultant margins above those of global peers. In 2018 we expect a number of initiatives to further boost volumes. Mainboard listing reforms are expected to be passed, which will pave the way for a pipeline of Chinese companies to be listed on the HK Exchange. In addition we expect the MSCI inclusion of A-shares to further promote volumes via the HK-China stock connect facility. Our view is that ultimately volumes will be the most significant driver of earnings, and that the strength of volumes in the fourth quarter of 2017 will be extended throughout 2018.

After redeploying funds from the sale of our holding in 21st Century Fox to increase our holding in Discovery Communications, we were pleased to see the share price of Discovery rise by around 10% this month. While we do not dismiss the structural concerns for cable network companies, we believe that share prices have not been adequately reflecting the pricing power and synergies sector consolidation brings to the acquirer. In the case of Discovery, we remain of the view that current multiples do not adequately reflect the benefits likely to flow from the Scripps Networks acquisition. Management's synergy target of US$350 million appears to be conservative, with marketing, production, and international content cost savings along with the capacity for a lift in US advertising revenue as a result of a wider audience reach likely to facilitate deleveraging and enhance shareholder returns. Recent insider buying of Discovery shares by Chairman and industry veteran, John Malone, gives us further confidence that value is being under-appreciated by the market.

Strategy & outlook

With the news headlines in January continuing to suggest a continuation of global political and policy uncertainty in 2018, we continue to focus on company fundamentals. We believe we have entered a period in equity markets where selective stock picking over broad market exposure is the best way to maximise returns. We have positioned our portfolio to the leading businesses in the sector that are trading below their intrinsic value. The companies we own have astute management teams and strong balance sheets are best placed in our view to navigate the challenging and ever-changing geopolitical outlook.

BT Wholesale Core Global Share Fund, managed by AQR

Market review

Global equity markets commenced the year with strong returns in January, although further strength in the Australian dollar reduced the local currency gains, with the MSCI World ex Australia Total Return (A$) Index returning 1.8%. Markets were buoyed by reports of positive earnings momentum in US economies, strengthening indicators of economic growth in the major economies and the positive impact of tax cuts and concessions for US Corporations. Prices for key commodities were aligned with the pro-growth market sentiment, which saw oil break through the US$60/bbl level and iron ore remain above US$70/mt. Base metals were also generally higher. Bullish conditions in capital markets have pushed the MSCI World ex Australia (A$) Index to its sixth consecutive year of strong positive returns.

Stock prices in the US reflected the combined effect of good earnings growth, strong labour and consumer markets, and strong economic growth to register its strongest start to the year since 1987. Investors looked passed the temporary Government shutdown that ensued following an impasse at Congress to approve budgetary measures. The greatest source of optimism seemed to come from Trump’s corporate tax cuts which are expected to result in higher corporate earnings. At a sector level, Consumer, Technology and Health Care sector were among the best performers, while Utilities and Real Estate sectors were the weakest, given their quasi status as bond proxies. The S&P500 rallied strongly to record a 5.7% return while the Nasdaq was up 7.4%.

Most major European equity markets delivered healthy gains to commence the year, with the German DAX (+2.1%) and the French CAC (+3.2%) benefitting from growing optimism for the euro area. The region recorded further GDP expansion, with a 0.6% growth rate for the fourth quarter of 2017 marking 19 quarters straight of expansion. Private sector surveys across the region also supported the positive reading, although inflation indicators remain muted which is likely to limit progress for the European Central Bank in normalising monetary policy.

By contrast, the UK market weakened, losing value for the month in response to upward revisions to US interest rate expectations and a corresponding increase in government bond yields. Despite strong commodity prices, market sentiment was focused on the prospect of a hard Brexit scenario and signs of weakness in consumer-related sectors. The FTSE Index declined by 2.0% for the month.

The performance of Asian markets was more varied, with Hong Kong’s Hang Seng rising by 9.9% and in significant contrast to Japan’s Nikkei return of 1.5%. Chinese equities were beneficiaries of higher economic growth expectations and a weaker US dollar, The Australian dollar had a mixed month on currency markets, finishing 3.5% stronger against the US dollar and 3.6% higher against the Hong Kong dollar, but weaker against the British pound (-1.5%) and euro (-0.2%). The local currency was a direct beneficiary of stronger commodity prices and stabilising demand from China.

Portfolio performance

The BT Wholesale Core Global Share Fund returned 1.78% (post-fee, pre-tax) in January 2018, outperforming its benchmark by 0.03%.

Outperformance was sourced from North America and Europe, while developed Asia underperformed its regional benchmark over the month.

Thematically, the outperformance in North America was driven by the strong performance of momentum signals, both direct and indirect, outweighing weakness in valuation signals. In Europe, the outperformance was also driven by momentum, through both direct and indirect measures. Developed Asia underperformance was attributable to positioning in Japan where weakness in both valuation and indirect momentum themes drove underperformance, outweighing positive contributions from management quality signals over the month.

From a stock and industry attribution perspective, active industry tilts were the source of outperformance, outweighing the mild underperformance of stock selection within industry groups. At a sector level, the underweights to Consumer Staples and Energy was the largest contributors and an overweight to Real Estate was the largest offsetting detractor to active returns over the month. Stock selection within industry groups was a net detractor, notably through unfavourable outcomes within the Consumer Discretionary and HealthCare sectors. The largest offsets were within Materials & Real Estate, where stock selection within industry groups added to overall outperformance over the month.

At a stock level, the strongest positive contributors came from overweight positions in The Boeing Company; an American multi-national aircraft manufacturer and defence contractor; Intesa Sanpaolo S.p.A., an Italian multi-national banking group; and Covestro AG, a German headquartered manufacturer and global supplier of polymers and high performance plastics. The largest detractors from active returns were an overweight position in Southwest Airlines Co., a major US discount airline; an underweight position in Amazon.com, Inc., an American headquartered electronic commerce company; and an underweight position in Netflix, Inc., an American entertainment company.

Strategy & outlook

Moving into February, the largest sector tilts are overweights in Industrials and Materials and underweights in Financials and Consumer Staples. Relative to long-term allocations, we remain mildly tilted towards higher quality companies with positive momentum and away from cheaper industry peers in the US and Europe and Japan.

Australian Fixed Income

BT Wholesale Fixed Interest Fund

Market review

Australian bonds suffered alongside a broader global sell-off in January. However, the local market was supported to some extent as expectations for an RBA rate hike were pushed back to early 2019. As the central bank did not meet during the month this was shaped in part by the fourth quarter CPI report released at the end of the month. The Board's preferred measure of inflation, the trimmed mean, rose a softer-than-expected 0.40% over the quarter. The headline rate increased 0.6% quarter-on-quarter with strong gains in fresh food, fuel and tobacco. Other economic releases like retail sales as well as consumer and business confidence were more constructive. Employment data was reasonable with 34.7K jobs added (mostly in part-time). Finally in terms of market movements, the Australian curve steepened with the 3 year yield increasing 2bps to 2.16%, while the 10 year yield rose 16bps to 2.81%. Meanwhile at the front-end, 90 day BBSW fell 2bps to 1.78%. At the same time, the Australian dollar strengthened by +3.7% against its US counterpart, which was due in part to broad US dollar weakness and a more upbeat Australian outlook.

Portfolio performance

The BT Wholesale Fixed Interest Fund returned 0.00% in January 2018 (post-fees, pre-tax), outperforming its benchmark by 0.27%.

In the alpha overlay, the Yield Curve, Duration and Relative Value strategies added to performance, while FX and Macro strategies detracted. The Government bond component outperformed its benchmark with the Cross-Market strategy being the main contributor. Finally, the Credit component outperformed its benchmark. This came from a long infrastructure and utilities exposure, which was partly offset by a short position in supranationals.

Strategy & outlook

The weaker than expected fourth quarter inflation data will see the Reserve Bank most likely leave the cash rate unchanged in the near term. Market pricing now implies one rate hike from the Reserve Bank within the next year. There are positive signs for the Australian economy despite the subdued inflationary environment. Business confidence and conditions remain above longer term averages. Consumer confidence had been weak for most of 2017, however more recent data reflects improving sentiment. Employment growth has been strong although the unemployment rate reflects a labour market with plenty of slack still remaining. Economic growth has been weighed down by the lack of recent mining investment but is likely that the drag has now passed. The external environment has also improved with economic growth forecasts being revised up. The Reserve Bank has left the cash rate unchanged since August 2016. The question for the Reserve Bank is whether monetary policy settings need to be as stimulatory now, despite the current lack of inflationary pressures. The market may be under-pricing how close the Reserve Bank is to tightening monetary policy. A rate hike mid to late this year would not surprise us.

International Fixed Income

BT Wholesale Global Fixed Interest Fund

Market review

Global bond markets suffered in January, while risk assets enjoyed a strong start to the year. Sentiment was supported by the passage of US tax reform, a strong US corporate earnings season and an absence of major geopolitical disruptions. The Federal Reserve left rates unchanged at their January gathering, but offered a more upbeat outlook for inflation. Meanwhile, US economic data was mixed with weaker-than-expected payrolls and fourth quarter GDP. In contrast, leading indicators like the ISM manufacturing survey ticked higher as did the Conference Board gauge of consumer confidence. In Europe, the ECB left its policy settings unchanged and noted that while broader economic data continued to improve, a stronger inflation pulse remained absent. President Draghi also added that a rate hike would be unlikely over 2018 and that the Euro's recent appreciation could complicate the outlook. Economic data was stronger across the board with a 1.5% jump in retail sales, 0.5 point increase in the Composite PMI, a 17 year high for sentiment and a 0.10% fall in the unemployment rate. Meanwhile in Asia, China recorded a healthy 6.8% GDP growth rate for 2017. Finally in terms of market movements, US yields experienced a significant increase with the 2 year adding 26bps to 2.14% and the 10 year by 30bps to 2.71%.

Portfolio performance

The BT Wholesale Global Fixed Interest Fund returned -0.58% in January 2018 (post-fees, pre-tax), outperforming its benchmark by 0.20%.

Over the month, the Yield Curve, Duration and Relative Value strategies added to performance, while Macro and FX strategies detracted. The portfolio began the month at 5 risk units and increased to 6 risk units before declining to 4 risk units at the end of the month.

The Duration strategy performed well over the month. The majority of the gains were from our long duration position in the New Zealand front-end, which performed well as a result of the weak PMI and inflation data. We added to the position prior to the weak data and then took profit just before month end. In European swaps, we opened a long duration position in the front-end and a short duration position in the long end of the real yield curve. The net performance from these two trades has been flat. During the month we initiated long duration positions in the Korean front-end with small gains to the portfolio. In Australia, minor losses were incurred in our short duration positions in the front end.

The FX strategy detracted marginally over the month. Most of the losses were from a short NZD position opened during the month. There were also losses from our short EUR position, partially offset by profits made from short USD and long JPY. In emerging market currencies, we closed our loss making long USD positions against INR and TWD. Our long IDR and KRW against USD were largely flat. Towards the end of the month we opened a small short USD against MYR. We continue to hold our call option on USDCNH expecting an upcoming slowdown of the Chinese economy. In the month FX volatility picked up significantly and we opened long volatility positions in USD-JPY, NZD-USD, EUR-USD and AUD-USD. These positions were largely flat into month-end.

The Yield Curve strategy was the dominant contributor of performance over the month. As we have mentioned in prior months, yield curves have flattened aggressively recently to over-stretched territory. This month our retained steepening positions performed well as the market corrected steeper. Our steepeners in New Zealand were the most profitable trade as the long-end of the curve sold off most aggressively. The micro-steepening positions along the US front-end and a newly added 6m-5y steepener all contributed significantly to performance. We also added steepening positions in the long end of the European curve with a strong performance for the month.

There were no trades in the Cross-Market strategy.

The Macro strategy was the largest detractor over the month. Credit continued to rally as the market sentiment remained optimistic. We increased our hedge ratio for the buy protection positions on CDX HY with iTraxx Europe Main and reduced our CDX EM positions earlier in the month. Later in the month we initiated a new decompression trade between a basket of high risk CDX EM sovereigns and the CDX EM Index.

The Relative Value strategy was positive to performance. Our US 2y invoice spread positions continued to make steady profits. In the middle of the month we added to this position. Towards the end of the month, we opened an Australian 3y EFP widener with flat performance.

Strategy & outlook

There is little doubt the global economic recovery is continuing. The question is rather, has the market gone too far? As the Fed signals it will stick to the plan to hike, the supporting economic data makes it all the more convincing. The equity market has accelerated to new highs with historically low volatility levels. The narrative underpinning market optimism is of a highly synchronised global upswing. However, we've highlighted the risks on the horizon in previous months and a faster pace of 'melt-up' only brings forward the prospects for a correction. Any number of market complacencies could upset the apple cart, but it is the layering of leverage and short volatility against a shrinking liquidity backdrop that can make for a particularly unkind unwind.

Credit

BT Wholesale Enhanced Credit Fund

Market review

The local credit market outperformed its government counterpart during the month. This was tied to several factors including its lower duration, strong accruals and a tightening in spreads. However, on an absolute basis the Non-Government Index was essentially flat due to a sharp rise in underlying swap rates. Rates increased globally as expectations for further Fed hikes firmed and positive investor sentiment saw a continued rotation into riskier assets. Trader optimism was aided by the passage of US tax reform, a strong US earnings season and an absence of major geopolitical upsets.

Turning to local credit market activity, issuance of A$8.3 billion for the month was considerably higher than December’s A$3.1 billion. Further, it was the largest January in terms of volume in nine years and the second largest start to the year on record. Financials accounted for the lion’s share of the issuance: CBA tapped the market for A$1.5 billion of 5.25y fixed and floating at 80bps over swap. ANZ issued twice that amount with a shorter tenor of 5 years split between fixed and floating at 77bps over swap. The regional banks (Bendigo & Bank of Queensland) also issued, as did foreign issuer Qatar Bank. Meanwhile, issuance from Corporates was much more subdued, as is generally the case for January. United Energy Distribution issued A$400 million of 5 and 6.75 year paper at 97bps and 112bps over swap respectively.

As has been the case over the past year, the new issuance was well-absorbed with spreads tightening during the month. The best performing sectors were utilities, infrastructure and real estate, which narrowed 8, 7 and 6bps respectively, while supranationals and domestic banks underperformed and only tightened 2 and 3bps respectively. Semi-government bond spreads performed in line with government bonds over the month. Finally, the Australian iTraxx Index (Series 28 contract) traded in a tight 6bps range finishing the month 1bp tighter to +57bps.

Portfolio performance

The BT Wholesale Enhanced Credit Fund returned 0.03% in January 2018 (post-fees, pre-tax) outperforming its benchmark by 0.06%.

Another tightening in credit spreads as well as strong accruals helped drive a positive return and more than offset a rise in underlying swap rates. Positive excess returns were again experienced from positions in infrastructure and utilities. Activity over the month involved participating in the primary issuance of ANZ.

Strategy & outlook

The weaker than expected fourth quarter inflation data will see the Reserve Bank most likely leave the cash rate unchanged in the near term. Market pricing now implies one rate hike from the Reserve Bank within the next year. There are positive signs for the Australian economy despite the subdued inflationary environment. Business confidence and conditions remain above longer term averages. Consumer confidence had been weak for most of 2017, however more recent data reflects improving sentiment. Employment growth has been strong although the unemployment rate reflects a labour market with plenty of slack still remaining. Economic growth has been weighed down by the lack of recent mining investment but is likely that the drag has now passed. The external environment has also improved with economic growth forecasts being revised up. The Reserve Bank has left the cash rate unchanged since August 2016. The question for the Reserve Bank is whether monetary policy settings need to be as stimulatory now, despite the current lack of inflationary pressures. The market may be under-pricing how close the Reserve Bank is to tightening monetary policy. A rate hike mid to late this year would not surprise us.

We remain constructive on the outlook for investment grade credit. From a macroeconomic standpoint, the backdrop remains supportive with expectations that monetary policy settings will remain accommodative in the near term. This was apparent in the ECB's communication during January where policymakers emphasised a need for rates to remain at current levels in light of a slow inflation pulse. Meanwhile in the US, the Federal Reserve continues to highlight that additional rate increases will be gradual. In turn, monetary policy normalisation should be slow and not disruptive for risk appetite. Further, the global growth picture continues to improve, as reflected in global economic surprise indices. Credit fundamentals are also encouraging with healthy balance sheets and earnings growth. Defaults for high yield issuers globally also remain low and demand for credit is strong given the low yield environment.

Risks to the outlook include if central bank communication turns overtly hawkish and yields increase sharply, which could cause increased market volatility and credit spreads to widen. We are also cognisant of more country-specific risks like a high degree of corporate leverage in China and slowing credit growth in the region.

Cash

BT Wholesale Managed Cash and BT Wholesale Enhanced Cash Funds

Market review

Australian bonds suffered alongside a broader global sell-off in January. However, the local market was supported to some extent as expectations for an RBA rate hike were pushed back to early 2019. As the central bank did not meet during the month this was shaped in part by the fourth quarter CPI report released at the end of the month. The Board's preferred measure of inflation, the trimmed mean, rose a softer-than-expected 0.40% over the quarter. The headline rate increased 0.6% quarter-on-quarter with the main contributors coming from fresh food, fuel and tobacco.

Other economic releases over the month were more constructive. This included the fastest monthly increase in retail sales for five years (+1.2%), which benefited from one-off factors including the new iPhone model release and the Black Friday shopping period. Other leading indicators also improved including business confidence (+7 to +11) and consumer confidence (103.3 to 105.1 – a four year high). Employment data was reasonable with 34.7K jobs added (mostly in part-time). An increase in the participation rate to a seven year high of 65.7% caused the unemployment rate to tick 0.10% higher to 5.50%.

Looking abroad, the Federal Reserve left rates unchanged at their January gathering, but offered a more upbeat outlook for inflation. Economic data for the US was mixed with weaker-than-expected payrolls and fourth quarter GDP. In contrast, leading indicators like the ISM manufacturing survey ticked higher as did the Conference Board gauge of consumer confidence.

In Europe, the ECB left its policy settings unchanged and noted that while broader economic data continued to improve a stronger inflation pulse remained absent. President Draghi also added that a rate hike would be unlikely over 2018 and that the Euro's recent appreciation could complicate the outlook. Economic data was stronger across the board with a 1.5% jump in retail sales, 0.5 point increase in the Composite PMI, a 17 year high for sentiment and a 0.10% fall in the unemployment rate.

Meanwhile in Asia, China recorded a healthy 6.8% GDP growth rate for 2017. However, other gauges of economic activity recorded slower paces of growth including industrial profits and retail sales. The pace of imports also slowed notably at only +4.5% with sharp declines in crude oil, coal and iron ore.

Finally in terms of market movements, the Australian curve steepened with the 3 year yield increasing 2bps to 2.16%, while the 10 year rose 16bps to 2.81%. Meanwhile at the front-end, the 90 day BBSW fell 2bps to 1.78%. US yields experienced a more significant increase with the 2 year adding 26bps to 2.14% and the 10 year by 30bps to 2.71%. This saw the AU-US 10 year spread fall to an 18 year low of 10bp. At the same time, the Australian dollar strengthened by +3.7% against its US counterpart, which was due in part to broad US dollar weakness and a more upbeat Australian outlook. Iron ore also gained with a 4.8% increase, as did WTI with an impressive 7.1% rally on expectations of OPEC supply cuts being maintained and stronger demand.

Portfolio performance

Managed Cash

The BT Wholesale Managed Cash Fund returned 0.15% in January 2018 (post-fee, pre-tax), underperforming the benchmark return by 0.01%.

With a higher running yield than the Index remains well positioned to outperform. Themes and credit exposure remain consistent with prior months, with excess spread from A-1 rated issuers and yield curve positioning likely to be the main driver of outperformance. The fund ended the month with a weighted average maturity of 55 days (maximum limit of 70 days). Yields further out the curve continue to offer better relative value and the weighted average maturity has consistently been longer than benchmark due to this. With longer dated yields offering better value and with Reserve Bank monetary policy tightening a distant prospect we will remain longer than benchmark. The Fund is well positioned to continue to outperform its benchmark.

Enhanced Cash

The BT Wholesale Enhanced Cash Fund returned 0.30% in January 2018 (post-fee, pre-tax), outperforming its benchmark by 0.14%.

The portfolio outperformed the benchmark by 17bps in January. Positive performance came from industrials, financials, infrastructure and utilities sectors. The portfolio has outperformed its benchmark by 1.74% over the past 12 months (pre fees).

Activity during the month included increasing exposure to domestic banks while reducing some exposure to industrials, infrastructure and utilities sectors.

As at the end of the month, the portfolio had a credit spread of 64bps over bank bills, interest rate duration of 0.10 years and credit spread duration of 2.0 years.

Strategy & outlook

The weaker than expected fourth quarter inflation data will see the Reserve Bank most likely leave the cash rate unchanged in the near term. Market pricing now implies one rate hike from the Reserve Bank within the next year. There are positive signs for the Australian economy despite the subdued inflationary environment. Business confidence and conditions remain above longer term averages. Consumer confidence had been weak for most of 2017 however more recent data reflects improving sentiment. Employment growth has been strong although the unemployment rate reflects a labour market with plenty of slack still remaining. Economic growth has been weighed down by the lack of recent mining investment but is likely that the drag has now passed. The external environment has also improved with economic growth forecasts being revised up. The Reserve Bank has left the cash rate unchanged since August 2016. The question for the Reserve Bank is whether monetary policy settings need to be as stimulatory now, despite the current lack of inflationary pressures. The market may be under-pricing how close the Reserve Bank is to tightening monetary policy. A rate hike mid to late this year would not surprise us.

Australian Property

BT Wholesale Property Securities Fund

Market review

The S&P/ASX 200 AREIT Index was down 3.3% in January, underperforming the broader market by 2.8%. AREITs were sold off on the back of a steepening yield curve with 10 year bonds +15bps to close at 2.8%. The US curve also steepened +4bp, with 10 year Treasuries +30bps to 2.71%. Year rolling, AREITs are +7.5%, but have underperformed the broader market by 4.7%. Global REITs were down

1.2% for the month, with Japan the best performing market (+12%) and the US the worst performing market (down 5.8%, both in USD terms).

It was a very quiet month for AREIT news. Vicinity Centres revalued its portfolio for the period which showed that Chadstone had been revalued on a cap rate of 3.75%, down 50bp, with the 100% value of the centre now at A$6 billion. The balance of the revaluations were mixed, with Outlet centres performing well with cap rates compressing 26bps to 6.03%, however Roselands (Sydney) and Galleria (Perth) were down 10.8% and 4.1% respectively. We are beginning to see a bifurcation in regional mall valuations, with the better positioned, stronger centres leaving the stagnating marginal regionals behind. This shows the importance of maintaining and remixing centres constantly. Notable underperformers for the month were Iron Mountain Inc (-12.6%) on the back of a debt and capital raise to fund Data Centres, Abacus Property Group (-10%) and Charter Hall Retail REIT (down 8%) on the back of a Moodys change in outlook from Baa1 stable to negative.

Global equity markets were buoyant in January with the MSCI All Country World Index returning 5.6%. US GDP growth for 4Q17 was slightly below forecast at 2.6%, however non-farm payrolls were solid +148k with the unemployment rate steady at 4.1%. US retail sales were +0.4% and consumer sentiment continued to be solid.

In Australia, the 4Q17 core CPI was weak, at +0.4% Q/Q, and private credit growth was soft with annual growth at 4.6% (the lowest since May 2014). However, Consumer confidence was very strong (+1.8%) to 105.1, the strongest reading since December 2013. Business confidence was also strong (+7 to a reading of +11). Job creation was very strong over 2017, with the economy producing over 400,000 new jobs.

Portfolio performance

The BT Wholesale Property Securities Fund returned -3.33% in January 2018 (post-fee, pre-tax), underperforming its benchmark by 0.08%.

The portfolio marginally underperformed over the month with positive attribution from underweight positions in Abacus Property Group and Charter Hall Retail REIT and overweight positions in Arena REIT, Charter Hall Group and Aveo Group. Overweight positions in Lifestyle Communities, Mirvac Group and Iron Mountain and underweight position in Vicinity centres detracted from performance.

Over the month we reduced our overweight position in Scentre Group to an underweight position, closed our underweight position in Dexus Property Group and reduced our overweight position in Aveo Group.

Strategy & outlook

The AREIT sector is now priced on an FY18 dividend yield of 5%, a PE ratio of 15.7 times and a 20% premium to NTA, slightly above its long-term average of 15%. Cap rates will likely compress further in the next reporting period (on the back of recent transaction evidence), but asset valuation uplift thereafter will depend on income growth and tenancy retention. Balance sheets are stable with sector gearing at 29%. The sector is trading at a 200bps dividend yield premium to 10 years bonds, in line with its 20 year average.

International Property

BT Wholesale Global Property Securities Fund, managed by AEW

Market Review (in USD)

Performance of the global property securities market (on an ex-Australia basis) as measured by the FTSE EPRA/NAREIT Developed Index was roughly flat in January. Asia Pacific (+7.9%) was the strongest performing region, followed by Europe (+2.6%), while North America (-3.9%) was in negative territory for the month. In Asia Pacific, results were positive across the region. Japan (+11.3%) posted the highest return, followed by Singapore (+5.7%), Hong Kong (+4.6%), and New Zealand (+2.2%). Results in Europe were largely positive. Spain (+7.8%) posted the largest gain, followed by Ireland (+5.3%) and Belgium (+4.7%). Israel (-2.4%) was the only negative performer within the region. In North America, the US and Canada returned -4.2% and 2.1%, respectively.

Portfolio performance

The BT Wholesale Global Property Securities Fund returned -1.17% in January 2018 (post-fee, pre-tax) outperforming the benchmark return by 0.03%.

North America

The North America portfolio returned -3.73% in January (before fees and taxes), outpacing the FTSE EPRA/NAREIT North America Index by 12 basis points. Outperformance relative to the benchmark was attributable to positive sector allocation results, which was partially offset by negative stock selection results. Regarding sector allocation, positive results were driven by the portfolio's underweight to the underperforming triple net lease and shopping centre sectors. Moreover, the portfolio's small cash position was contributor to relative performance in light of the regional benchmark's negative absolute performance for the month. In terms of stock selection, results were weakest in the diversified, regional mall, and apartment sectors, and were strongest in the hotel, triple net lease, and industrial sectors. Among the portfolio's holdings, top individual contributors to relative performance included overweight positions in outperforming Extended Stay America (STAY), Rexford Industrial Realty (REXR), and Host Hotels & Resorts (HST). Detractors most notably included overweight positions in underperforming Retail Properties of America (RPAI), American Assets Trust (AAT), and Acadia Realty Trust (AKR).

Europe

The European portfolio returned 2.96% in January (before fees and taxes), exceeding the regional EPRA benchmark by 29 basis points. Outperformance relative to the benchmark was driven by positive stock selection results, which were partially offset by negative country allocation results. In terms of stock selection, results were strongest in the United Kingdom, France, and Sweden and were weakest in Spain, Ireland, and Switzerland. Regarding country allocation, negative results were largely attributable to the portfolio's lack of exposure to the outperforming Belgium market and an underweight to Switzerland which outperformed. Among the portfolio's holdings, top contributors to relative performance included overweight positions in Gecina SA (France) and Workspace Group PLC (United Kingdom), and holding no exposure to Intu Properties PLC (United Kingdom). Detractors most notably included an overweight position in Vonovia SE (Germany) and a lack of exposure to Icade (France) and Inmobiliaria Colonial S.A. (Spain).

Asia

The Asia portfolio returned 7.49% in January (before fees and taxes), lagging the regional EPRA benchmark by 39 basis points. Underperformance relative to the benchmark was attributable to both negative country allocation and stock selection results. Regarding country allocation, negative results were attributable to the portfolio's underweight to the outperforming Japan market. Moreover, the portfolio's small cash position was a detractor from relative returns in light of the regional benchmark's strong positive absolute performance for the month. In terms of stock selection, results were negative across the region, most notably in Hong Kong. Among the portfolio's holdings, top contributors to relative performance included overweight positions in Sumitomo Realty & Development (Japan) and Mitsui Fudosan (Japan), and an underweight position in CapitaLand Commercial Trust (Singapore). Detractors most notably included an overweight position in HongKong Land Holdings (Hong Kong), a lack of exposure to outperforming Tokyo Tatemono (Japan), and an underweight position in CapitaLand (Singapore).

Active Balanced

BT Wholesale Active Balanced Fund

The domestic equity market started 2018 on a downbeat note, with the S&P/ASX 300 Accumulation Index finishing January down 0.39%. While Resources (+0.8%) recorded a small gain amid strong commodity prices, it was more than offset by the weak performance from Industrials (-0.7%).

The major macro themes over the month include a weakening US dollar, which has led to rising commodity prices; and rising global bond yields against the backdrop of synchronised global economic growth. As such, miners were generally supported in January with Metals & Mining edging 1.2% higher. The major miners finish the month in the black, supported by well-received market updates and iron ore remaining above US$70 per tonne. Partially helped by the miners, Materials (+0.5) was one of the few sectors which finished the month with a positive return.

Also residing within the winner's group, Health Care (+3.1%) was the largest contributor to index performance. Sector heavyweight CSL (CLS, +3.6%) recorded a positive month in January. While there was no company-specific news attached, investor sentiment was helped by the two acquisition deals announced by French pharmaceutical giant Sanofi, totalling US$17 billion over the month. Also adding to the sector's positive performance was strong return from Resmed (RMD, +13.5%) and Sirtex Medical

(SRX, +66.2%). The former reported a good set of Q2 results across the board: sales growth of the flowgen machines did not decelerate as some had feared; while sales of the high-margin masks also grew at double digit rates globally. For Sirtex, an all-cash acquisition offer from Varian Medical, which represents a 19x multiple for SRX's FY1 EBITDA, was well received by the market.

On the other side of the ledger, Utilities (-4.3%) was the worst performing sector over the period. The pickup in bond yields continued on the back of synchronised global economic growth and was evident both overseas (US 10-year Treasuries added 31bps over the month to yield 2.72%) and back at home (the Australian counterpart added 16bps to yield 2.79%), which weighed on bond sensitive sectors. For similar reasons the Real Estate (-3.2%) sector got dragged into the red as did infrastructure companies including Transurban (TCL, -3.3%), Sydney Airport (SYD, -3.4%) as well as Macquarie Atlas (MQA, -8.7%). Last but not least, all the Big Four banks slid moderately over the month, from -1.8% (CBA) to -0.6% (ANZ), driving the broader Financials (-0.7%) sector into negative territory. The banks are due to provide trading updates in February.

Global equity markets commenced the year with strong returns in January, although further strength in the Australian dollar reduced the local currency gains, with the MSCI World ex Australia Total Return (A$) Index returning 1.8%. Markets were buoyed by reports of positive earnings momentum in US economies, strengthening indicators of economic growth in the major economies and the positive impact of tax cuts and concessions for US Corporations. Prices for key commodities were aligned with the pro-growth market sentiment, which saw oil break through the US$60/bbl level and iron ore remain above US$70/mt. Base metals were also generally higher. Bullish conditions in capital markets have pushed the MSCI World ex Australia (A$) Index to its sixth consecutive year of strong positive returns.

Stock prices in the US reflected the combined effect of good earnings growth, strong labour and consumer markets, and strong economic growth to register its strongest start to the year since 1987. Investors looked passed the temporary Government shutdown that ensued following an impasse at Congress to approve budgetary measures. The greatest source of optimism seemed to come from Trump's corporate tax cuts which are expected to result in higher corporate earnings. At a sector level, Consumer, Technology and Health Care sector were among the best performers, while Utilities and Real Estate sectors were the weakest, given their quasi status as bond proxies. The S&P500 rallied strongly to record a 5.7% return while the Nasdaq was up 7.4%.

Most major European equity markets delivered healthy gains to commence the year, with the German DAX (+2.1%) and the French CAC (+3.2%) benefitting from growing optimism for the euro area. The region recorded further GDP expansion, with a 0.6% growth rate for the fourth quarter of 2017 marking 19 quarters straight of expansion. Private sector surveys across the region also supported the positive reading, although inflation indicators remain muted which is likely to limit progress for the European Central Bank in normalising monetary policy.

By contrast, the UK market weakened, losing value for the month in response to upward revisions to US interest rate expectations and a corresponding increase in government bond yields. Despite strong commodity prices, market sentiment was focused on the prospect of a hard Brexit scenario and signs of weakness in consumer-related sectors. The FTSE Index declined by 2.0% for the month.

The performance of Asian markets was more varied, with Hong Kong's Hang Seng rising by 9.9% and in significant contrast to Japan's Nikkei return of 1.5%. Chinese equities were beneficiaries of higher economic growth expectations and a weaker US dollar,

The Australian dollar had a mixed month on currency markets, finishing 3.5% stronger against the US dollar and 3.6% higher against the Hong Kong dollar, but weaker against the British pound (-1.5%) and euro (-0.2%). The local currency was a direct beneficiary of stronger commodity prices and stabilising demand from China.

Within the fixed interest sector, Global bond markets suffered in January, while risk assets enjoyed a strong start to the year. Sentiment was supported by the passage of US tax reform, a strong US corporate earnings season and an absence of major geopolitical disruptions. The US Federal Reserve left rates unchanged at their January gathering, but offered a more upbeat outlook for inflation. Meanwhile, US economic data was mixed with weaker-than-expected payrolls and fourth quarter GDP. In contrast, leading indicators like the ISM manufacturing survey ticked higher as did the Conference Board gauge of consumer confidence. In Europe, the ECB left its policy settings unchanged and noted that while broader economic data continued to improve a stronger inflation pulse remained absent. President Draghi also added that a rate hike would be unlikely over 2018 and that the Euro's recent appreciation could complicate the outlook. Economic data was stronger across the board with a 1.5% jump in retail sales, 0.5 point increase in the Composite PMI, a 17 year high for sentiment and a 0.10% fall in the unemployment rate. Meanwhile in Asia, China recorded a healthy 6.8% GDP growth rate for 2017. Finally in terms of market movements, US yields experienced a significant increase with the 2 year adding 26bps to 2.14% and the 10 year by 30bps to 2.71%.

Australian bonds suffered alongside a broader global sell-off in January. However, the local market was supported to some extent as expectations for an RBA rate hike were pushed back to early 2019. As the central bank did not meet during the month this was shaped in part by the fourth quarter CPI report released at the end of the month. The Board's preferred measure of inflation, the trimmed mean, rose a softer-than-expected 0.40% over the quarter. The headline rate increased 0.6% quarter-on-quarter with strong gains in fresh food, fuel and tobacco. Other economic releases like retail sales as well as consumer and business confidence were more constructive. Employment data was reasonable with 34.7K jobs added (mostly in part-time). Finally in terms of market movements, the Australian curve steepened with the 3 year yield increasing 2bps to 2.16%, while the 10 year yield rose 16bps to 2.81%. Meanwhile at the front-end, 90 day BBSW fell 2bps to 1.78%. At the same time, the Australian dollar strengthened by +3.7% against its US counterpart, which was due in part to broad US dollar weakness and a more upbeat Australian outlook.

Portfolio performance

The BT Wholesale Active Balanced Fund returned 0.65% (post-fee, pre-tax) for the month of January, outperforming its benchmark by 0.38%.

The Fund's performance in January was driven primarily by the strong performance of global equities, while some of these gains were offset by negative returns from fixed interest assets. Exposure to alternatives contributed to returns, as did the Fund's exposure to listed property which declined in value.

Tactical asset allocation contributions were driven by the Fund's overweight exposure to global equities and an underweight to Australian and international fixed income.

The key factors influencing our active management returns were strong stock selection outcomes within Australian equities and the concentrated global equity component. Within the Australian equity strategy, overweight positions in JB Hifi, Qantas, BHP and Resmed. Partially offsetting these contributions were overweight positions in Macquarie Atlas, Santos and Amcor.

Active returns from our global equities portfolio were sourced from stock selection by both our core and concentrated managers, however, a strengthening Australian dollar and underperformance of our emerging markets manager detracted returns within this asset class.

Our Alternatives portfolio delivered another positive return for January, with contributions from six of the eight underlying strategies within the core component of the sector. The Alternatives strategy delivered a total return (before fees) of 1.60% vs a cash return of 0.16%, with contributions from Managed Futures, with profitable trend following in all four asset classes over the month, most notably within equities and currencies; Long/Short Equity, driven by stock positioning within the US and European markets, while the Japanese portfolio detracted somewhat. The strategy also benefitted from its directionally long equity beta component over the month. The Global Macro strategy benefitted from contributions from Developed Equities Relative Value strategy and Equity and Bond Timing strategies. The sole detracting sub-strategy over the month was Dedicated Short Bias, which was impacted both by its directionally short equity tilt, and its stock positioning with the US and Japan. Offsetting losses somewhat was positive results to stock positioning within Japan.

Our tactical positioning within alternatives made a further contribution to returns. A long position in certain commodities together with the Fund's short volatility position contributed to returns, while long positions in equities more than offset detractions from long positions in Australian, US and German bonds.

Strategy and Outlook

Recent market volatility has illustrated the importance diversification. While equities are a critical component in delivering long term growth to a portfolio, this exposure needs to be balanced by assets that are diversifying – bonds, foreign exchange exposure, and alternatives can all help to stabilise returns. Looking forward, the Fund remain overweight equities as we believe that equities will continue to be attractive on a shorter to medium term horizon. However, we recognise the inherent uncertainty of financial markets and continue to hold a broad range of diversifying exposures to seek to smooth out the inevitable bumps in the road.

While the conditions for equities are positive, we remain mindful of valuation indicators and continue to see prudence in maintaining some exposure to defensive and alternatives assets to preserve capital and diversify the asset base.

Performance as at 31 January 2018

(%)	1 Month	3 Months	6 Months	FYTD	1 year (pa)	2 Years (pa)	3 Years (pa)	5 Years (pa)	Since Incp. (pa)
Australian Shares - All Cap									
BT Wholesale Core Australian Share Fund									APIR - RFA0818AU
Total Return (post-fee, pre-tax)	0.27	3.72	9.22	9.86	15.68	13.95	8.09	10.34	10.07
Total Return (pre-fee, pre-tax)	0.34	3.93	9.67	10.39	16.61	14.86	8.95	11.21	11.08
Benchmark	-0.39	3.18	8.16	8.18	12.37	14.82	7.47	8.99	10.00
BT Wholesale Imputation Fund									APIR - RFA0103AU
Total Return (post-fee, pre-tax)	0.21	2.53	7.50	7.70	13.04	12.33	5.96	8.32	9.58
Total Return (pre-fee, pre-tax)	0.29	2.76	7.98	8.27	14.06	13.34	6.92	9.29	10.60
Benchmark	-0.39	3.18	8.16	8.18	12.37	14.82	7.47	8.99	8.76
BT Wholesale Focus Australian Share Fund									APIR - RFA0059AU
Total Return (post-fee, pre-tax)	0.88	4.23	9.76	10.36	17.46	15.58	10.11	12.40	9.46
Total Return (pre-fee, pre-tax)	1.21	4.67	10.53	11.27	19.25	16.66	11.42	13.54	10.60
Benchmark	-0.39	3.18	8.16	8.18	12.37	14.82	7.47	8.99	7.55
BT Wholesale Ethical Share Fund									APIR - RFA0025AU
Total Return (post-fee, pre-tax)	0.39	3.98	9.26	10.04	15.73	13.89	8.24	10.45	8.71
Total Return (pre-fee, pre-tax)	0.47	4.23	9.78	10.66	16.84	14.98	9.27	11.50	9.77
Benchmark	-0.39	3.18	8.16	8.18	12.37	14.82	7.47	8.99	8.12
Australian Shares - Mid Cap									
BT Wholesale MidCap Fund									APIR - BTA0313AU
Total Return (post-fee, pre-tax)	0.66	6.68	16.44	16.84	26.62	20.51	15.93	15.65	11.07
Total Return (pre-fee, pre-tax)	1.09	7.31	17.56	18.05	28.41	21.62	17.38	17.46	13.36
Benchmark	-0.69	5.15	14.19	12.95	22.44	21.32	14.80	12.80	6.07
Australian Shares - Small Cap									
BT Wholesale Smaller Companies Fund									APIR - RFA0819AU
Total Return (post-fee, pre-tax)	-0.91	4.33	13.59	15.06	19.32	12.95	14.06	10.88	13.30
Total Return (pre-fee, pre-tax)	-0.80	4.66	14.30	15.91	20.81	14.36	15.49	12.26	14.59
Benchmark	-0.54	6.65	17.65	18.05	22.35	19.32	13.82	6.39	7.91
Australian Shares - Micro Cap									
BT Wholesale MicroCap Opportunities Fund									APIR - RFA0061AU
Total Return (post-fee, pre-tax)	0.43	7.37	17.26	19.27	23.37	21.33	22.82	19.83	19.21
Total Return (pre-fee, pre-tax)	0.81	7.98	17.86	20.46	25.26	23.39	26.57	24.81	24.60
Benchmark	-0.54	6.65	17.65	18.05	22.35	19.32	13.82	6.39	3.28
International Shares									
BT Wholesale Core Global Share Fund									APIR - RFA0821AU
Total Return (post-fee, pre-tax)	1.78	3.22	12.30	11.07	19.01	12.69	9.64	17.61	5.91
Total Return (pre-fee, pre-tax)	1.87	3.47	12.84	11.70	20.14	13.76	10.69	18.74	7.08
Benchmark	1.75	3.24	12.27	10.39	18.15	13.42	10.49	17.77	7.34
BT Global Emerging Markets Opportunities Fund - Wholesale									APIR - BTA0419AU
Total Return (post-fee, pre-tax)	0.57	0.41	12.18	13.03	27.97	20.56	7.95	12.33	12.44
Total Return (pre-fee, pre-tax)	0.70	0.76	12.95	13.94	29.76	22.23	9.46	14.05	14.67
Benchmark	4.64	6.48	16.85	18.96	32.20	24.29	10.38	11.24	12.61
BT Concentrated Global Share Fund									APIR - BTA0503AU
Total Return (post-fee, pre-tax)	2.55	5.39	13.47	12.18	20.70	N/A	N/A	N/A	18.20
Total Return (pre-fee, pre-tax)	2.66	5.72	14.18	13.01	22.21	N/A	N/A	N/A	19.68
Benchmark	1.75	3.24	12.27	10.39	18.15	N/A	N/A	N/A	15.55
Property									
BT Wholesale Property Securities Fund									APIR - BTA0061AU
Total Return (post-fee, pre-tax)	-3.33	2.13	6.47	5.85	8.39	7.36	7.11	11.20	7.43
Total Return (pre-fee, pre-tax)	-3.28	2.30	6.81	6.26	9.10	8.06	7.80	11.92	8.25
Benchmark	-3.25	2.00	6.47	6.31	8.08	7.45	7.46	11.67	7.30
BT Wholesale Global Property Securities Fund									APIR - RFA0051AU
Total Return (post-fee, pre-tax)	-1.17	1.92	2.51	3.58	7.83	8.43	2.89	8.76	9.31
Total Return (pre-fee, pre-tax)	-1.10	2.16	2.99	4.15	8.84	9.43	3.84	9.77	10.31
Benchmark	-1.20	2.11	2.26	3.21	7.40	8.52	2.95	9.05	9.03
Fixed Interest									
BT Wholesale Fixed Interest Fund									APIR - RFA0813AU
Total Return (post-fee, pre-tax)	0.00	0.01	0.68	0.93	2.48	1.42	1.32	3.67	6.41
Total Return (pre-fee, pre-tax)	0.04	0.13	0.93	1.23	3.00	1.93	1.83	4.19	6.97
Benchmark	-0.27	0.08	0.85	1.10	2.75	2.52	2.41	4.14	6.64
BT Wholesale Global Fixed Interest Fund									APIR - RFA0032AU
Total Return (post-fee, pre-tax)	-0.58	-0.47	0.08	0.34	1.96	1.08	1.30	4.05	6.04
Total Return (pre-fee, pre-tax)	-0.53	-0.34	0.35	0.66	2.50	1.62	1.84	4.60	6.63
Benchmark	-0.78	-0.39	0.48	0.71	2.66	2.31	2.66	4.79	6.95
BT Wholesale Enhanced Credit Fund									APIR - RFA0100AU
Total Return (post-fee, pre-tax)	0.03	0.40	1.43	1.93	3.79	3.36	3.12	4.51	5.77
Total Return (pre-fee, pre-tax)	0.07	0.51	1.66	2.20	4.26	3.83	3.58	4.98	6.29
Benchmark	-0.03	0.37	1.32	1.81	3.66	3.37	3.13	4.47	5.87
Cash & Income									
BT Wholesale Enhanced Cash Fund									APIR - WFS0377AU
Total Return (post-fee, pre-tax)	0.30	0.76	1.56	1.89	3.22	2.98	2.74	3.03	4.97
Total Return (pre-fee, pre-tax)	0.32	0.82	1.69	2.04	3.48	3.24	3.00	3.29	5.31
Benchmark	0.16	0.43	0.87	1.01	1.75	1.89	2.02	2.32	4.91
BT Wholesale Managed Cash Fund									APIR - WFS0245AU
Total Return (post-fee, pre-tax)	0.15	0.44	0.89	1.04	1.78	1.93	2.03	2.30	6.48
Total Return (pre-fee, pre-tax)	0.17	0.50	1.00	1.17	2.01	2.15	2.26	2.53	6.79
Benchmark	0.16	0.43	0.87	1.01	1.75	1.89	2.02	2.32	6.56
BT Wholesale Monthly Income Plus Fund									APIR - BTA0318AU
Total Return (post-fee, pre-tax)	0.13	1.24	3.35	3.93	6.00	4.59	3.80	5.00	5.64
Total Return (pre-fee, pre-tax)	0.19	1.40	3.69	4.33	6.69	5.27	4.47	5.69	6.30
Benchmark	0.13	0.38	0.76	0.89	1.51	1.61	1.77	2.11	2.97
Diversified									
BT Wholesale Active Balanced Fund									APIR - RFA0815AU
Total Return (post-fee, pre-tax)	0.65	2.86	8.09	8.32	13.26	9.84	6.36	9.53	7.77
Total Return (pre-fee, pre-tax)	0.73	3.11	8.62	8.93	14.32	10.88	7.37	10.57	8.84
Benchmark	0.27	2.35	6.66	6.53	10.47	10.35	6.73	8.83	7.54

Performance data (post-fee) assumes reinvestment of distributions and is calculated using exit prices, net of management costs. Performance data (pre-fee) is calculated by adding back management costs to the (post-fee) performance. Past performance is not a reliable indicator of future performance. The term 'benchmark' refers to the index or measurements used by an investment manager to assess the relative risk and the performance of an investment portfolio.

BTIM is the issuer of the following products:

- *BT Wholesale Core Australian Share Fund ARSN 089 935 964*
- *BT Wholesale Smaller Companies Fund ARSN 089 939 328*
- *BT Concentrated Global Share Fund ARSN 613 608 085*
- *BT Wholesale Core Global Share Fund# ARSN 089 938 492*
- *BT Wholesale Global Fixed Interest Fund ARSN 099 567 558*
- *BT Wholesale Enhanced Credit Fund ARSN 089 937 815*
- *BT Wholesale Fixed Interest Fund ARSN 089 939 542*
- *BT Wholesale Property Investment Fund ARSN 089 939 819*
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