

→ Fund Manager Commentary

February 2018

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Australian Shares

BT Wholesale Core Australian Share Fund

Market review

A spike in market volatility and sell-off in global and domestic equities early in the month prompted some market concern of a sharp correction following a sustained period of strength. However, the falls were arrested swiftly in most markets, which then spent the remainder of the month clawing back lost ground. At its low point for the month, the S&P 500, had fallen a touch over 10% in US\$ terms from its peak in late January, but had regained half of this by the end of February.

The Australian market demonstrated its relatively defensive nature during this episode. It had fallen just over 4% from the start of the month to its lowest point on the 12th of February, but managed to regain all of this by the month's end to finish 0.3% higher. As a result, the local bourse was among the best performing markets globally, ahead of the S&P 500 (-3.9%), German DAX (-5.7%) and Japanese Nikkei (-4.5%).

A key point to consider in the context of this divergence is that Australian equities have not enjoyed the same surge as other developed markets over the last year. For example, the S&P/ASX 300 had gained roughly +7.5% for the 12 months to end January 2018 – versus around +23.8% for the S&P 500. This partly reflects the more defensive nature of the ASX and the different market composition, with **technology stocks** – which have outpaced the rest of the US market on valuation re-rating comprising a much lower proportion of the local market.

The catalyst for the sell-off was stronger than expected wage data from the US, which prompted speculation of an uplift in inflation and the possibility that the Fed might raise rates faster than previously anticipated. It was therefore the bond-sensitive sectors which bore the brunt of the market's early weakness and **telecommunications (-6.2%)**, **REITs (-3.2%)** and **utilities (-1.6%)** all ended the month down. For the telecommunications sector, the challenging macroeconomic backdrop was exacerbated by a disappointing result from **Telstra (TLS)**, which fell -5.7% for the month. Crude oil also edged lower, down 4.8%, which weighed on the **Energy** sector (-3.8%).

February's reporting season has been received quite positively, with analysts pointing to a greater number of companies beating expectations than missing. In our view the consensus expectation for FY18 earnings growth held fairly steady at 5-6%, with the current path of downgrades running below its historical average. Positive earnings were certainly a key driver of the **Health Care** sector (+7.0%) – the market's strongest in February – as **CSL (CSL)** (+11.4%) and **Cochlear (COH)** (+5.9%) both delivered well-received results. **Consumer Staples** (+2.1%) also outperformed as **Woolworths (WOW)** (+2.5%) and **Treasury Wine Estate (TWE)** (+2.2%) nudged higher. However, **A2 Milk (A2M)** was the key driver as it surged a further 47.5%.

Portfolio performance

The BT Wholesale Core Australian Share Fund returned 1.44% (post-fee, pre-tax) in February 2018, outperforming its benchmark by 1.10%.

Contributors

Overweight Nine Entertainment

Nine Entertainment's (NEC, +37.5%) result confirmed the company's ability to survive in a challenging environment and serves as a prime example of the opportunities that corporate disruption is throwing up for investors in the Australian market. We bought NEC at a time when the market was giving up on traditional media stocks, largely on the basis that advertising revenue was under serious pressure from online competition. The market was almost pricing NEC for oblivion, yet we believed that management had the ability and strategy to cope via cost control, better content, and a divestment of non-core activities to help bolster the balance sheet. NEC has demonstrated this over the last year, culminating in a return to advertising revenue growth and overall profitability in the most recent half. The opportunity for investors lies in the swift and strong share price reactions that can occur when a previously abandoned company returns to favour; NEC is now up over 135% for the last 12 months.

Overweight Qantas

Qantas (QAN, +11.8%) weakened over the last half of 2017 on the combination of some technical selling related to its exclusion from the MSCI World Index as well as a higher oil price – notwithstanding that the company hedges a substantial portion of its fuel costs. However, it bounced back in February, posting strong revenue and profit growth which was driven primarily by the domestic business. The key factor here remains the discipline that both it and rival Virgin Australian (VAH) are exercising in terms of capacity in the domestic market. Limited growth in capacity, coupled with moderate growth in demand, is underpinning high yields and profitability for QAN which the company believes will go some way to offsetting the pressure from higher fuel costs as its hedging programme rolls over. Strong free cash flow continues to be returned to the shareholder, with management announcing \$500 million to be returned via buybacks and dividends. Despite a gain of over 62% in the last 12 months, QAN remains among the cheaper stocks compared to both the local market and its global peer group.

Underweight Woodside

Woodside's (WPL, -8.9%) result was essentially in line with the market's expectation, however the news that it was raising \$2.5 billion to purchase Exxon's stake in the Scarborough reserve off the Western Australian coast did come as a surprise. The market's key concern is that the company will now probably have to invest more to develop its reserves than was previously thought. This, in turn, brings pressure to bear on the 80% pay-out ratio that management have maintained. There are also some questions over the timing of the capital raising, given that a final investment decision on Scarborough is not expected until 2020. We continue to prefer other opportunities within the energy sector.

Underweight South32

South32's (S32, -13.1%) results were broadly in line with consensus, with commodity prices continuing to support strong free cash flow and capital return to the shareholder. However, the stock suffered downgrades in the wake of its result, based on the combination disappointing production guidance, cost inflation at its main assets, and the potential for lower commodity prices. At this point, we prefer the diversified miners with iron ore exposure such as BHP (BHP) and Rio Tinto (RIO), where we have a degree of confidence that Chinese policies aimed at bolstering domestic steel mill profitability and reducing pollution will continue to provide an ongoing level of support.

Detractors

Overweight JB Hi-Fi

JB Hi-Fi (JBH, -8.4%) delivered a very strong first half result, particularly within the context of the challenges facing traditional brick-and-mortar Australian retailers from global and on-line competition and stalled wage growth. Excluding the effect of its acquisition of the Good Guys, its Australian stores grew sales by 7.8% for the half. The stock dropped despite a result that beat most expectations as management retained a degree of caution in their guidance for the full year. In particular, there is a degree of uncertainty over the outlook for Good Guys given its relatively poor performance versus the JB Hi-Fi branded stores. We believe that there is still scope for material improvement in the Good Guys franchise and further realisation of synergies. We maintain our conviction that the market is under-estimating JBH's ability to navigate a challenging environment for traditional retailers and retain our position.

Underweight A2 Milk

A2 Milk (A2M, +47.5%) gained more than 30% on its result, which demonstrated better-than-expected growth from its Chinese distribution and came on top of the company opening up a new market in the north-eastern United States last month. We have a positive view on the company and management, however we have a preference for other growth-style stocks within our large cap portfolios, given valuation differentials. Our underweight here has dragged on relative performance.

Overweight CYBG

CYBG (CYB, -6.7%), the NAB spin-off which manages a portfolio of UK banks, fell late in the month as Lloyds TSB announced a top-up to contingent liabilities for claims related to previous mis-selling. This issue remains a risk for CYB; NAB apportioned a sizeable provision as part of its spin-off, however it is not yet certain whether it will be enough to meet all potential claims. Nevertheless, we believe the move by Lloyds only brings it into a position consistent with CYB, rather than signalling an increase in this risk. Meanwhile, CYB continues to deliver a decent turnaround, with loan growth, strong cost control, and margin improvement as rates rise and the potential for an improved capital position if it receives advanced accreditation.

Underweight Insurance Australia

IAG (+15.3%) delivered a decent first-half result, with net profit for the half up 24% and some key underlying trends turning positive for the first time in a few halves, resulting in some small upgrades for FY18. That said, there was a material proportion of one-off factors such as reserve releases which supported the result. At this point we believe that the insurance sector does not look cheap, while there is significant potential for the market's expectations of a turnaround in margins on the back of improved pricing to be disappointed, given trends in claims costs and government scrutiny of premiums.

Strategy & outlook

The portfolio outperformed the Index in February, following what was a generally good reporting season for our holdings. Both Nine and Qantas delivered strong results, while BlueScope Steel also bounced back from a disappointing previous period, helped by strength in both its Australian and North American businesses. While we tend not to take large thematic positions within the portfolio – preferring our identification of idiosyncratic stock-level opportunities to drive returns – we have nevertheless had a moderate underweight in bond-sensitives in recent years. This has been driven by a combination of an environment of rising yields, coupled with valuations which are in many cases, stretched. This also helped in February, against a backdrop of persistent speculation that inflationary pressures in the US may see the Fed raise rates faster than previously expected. The underweights in REITs and Transurban helped to drive outperformance. The position in JB Hi-Fi dragged as did Telstra, which disappointed the market with its result.

There is always the risk that the bout of weakness in early February may ultimately lead to a sustained bear market in Australian equities, however at this point we do not believe it to be the case. It is important to note that the Australian market has not surged to the same extent as US or global markets, driven partly by its differing composition, and hence has not reached the extended valuation levels of some other markets. The Australian market's aggregate valuation, while slightly above its long-term average, is entirely consistent with where we would expect it to be given our low interest rates. With little to suggest that the Reserve Bank of Australia (RBA) is likely to start raising rates aggressively, we are relatively comfortable with the market's valuation level. At the same time, we are seeing little sign of the complacency which traditionally accompanies the start of a sustained downturn.

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. That said, it is worth remembering that in recent years the US economy has displayed a meaningful sensitivity to bond yields. The strength of US business confidence and persistence of benefits from recent tax reform may allow a greater proportional rise in yields than in recent years, but we must be mindful that if yields continue to rise - and tempers the US expansion as a result – then there is every chance that the Fed will not accelerate rate hikes which could see sentiment reverse again.

The local market remains supported by reasonable corporate health and earnings growth – as evidenced by the reporting season – as well as by signs of a pick-up in capital expenditure and infrastructure spending. There are challenges; not least the scale of corporate disruption from new business models and competitions – however this is actually driving a number of the more compelling investment opportunities in the market, given the mis-pricing that ensures.

Outside of the stock specific opportunities within industrials, we remain broadly positive on resources, supported by Chinese policy and management discipline on cost and capital expenditure. We believe that the downside to banks is limited from here and the sector is offering attractive yield; however, it is hard to see strong near-term outperformance given the significant uncertainties that surround the Royal Commission.

BT Wholesale Smaller Companies Fund

Market review

A spike in market volatility and sell-off in global and domestic equities early in the month prompted some market concern of a sharp correction following a sustained period of strength. However, the falls were arrested swiftly in most markets, which then spent the remainder of the month clawing back lost ground. At its depth the S&P 500, for example, had fallen a touch over 10% in USD terms from its peak in late January, but had regained half of this by the end of February.

The Australian market demonstrated its relatively defensive nature during this episode. The S&P/ASX 300 had fallen just over 4% from the start of the month to its lowest point on the 12th of February, but managed to regain all this by the month's end, to finish +0.3% higher. As a result, the local bourse was among the best performing market globally, ahead of the S&P 500 (-3.9%), German DAX (-5.7%) and Japanese Nikkei (-4.5%).

The local small cap sector outperformed the broad market index in February. The **S&P/ASX Small Ordinaries Accumulation Index** fell slightly further than the S&P/ASX 300 in the month's early weakness – reaching a trough at around 5% lower than its point at the start of February, but then rebounded faster with greater alacrity to end the month flat. This was driven in part by the strong reaction to good results in reporting season from index heavyweights such as **Cleanaway Waste Management** (CWY, +5.9%), **Costa Group** (CGC, +19.3%), **Altium** (ALU, +32.8%) and **Nine Entertainment** (NEC, +35.7%).

February's reporting season is generally considered reasonable at a broad level, with analysts pointing to a greater number of companies beating expectations than missing. In our view, the consensus expectation for S&P/ASX 200 FY18 earnings growth held fairly steady at 5-6%, with the current path of downgrades running below its historical average. The results helped drive the wide dispersion in sector performance within the mid-cap sector.

Telecommunications (-7.2%) was the worst performing sector. The key factor here was little sign of receding competitive intensity in the Australian mobile market as **Amaysim's** (AYS) results came in well below market expectations. **Financials ex-Property Trusts** (-4.8%) was also weak, with the market volatility weighing on some of the diversified financials. **Small cap REITs** (-1.44%) underperformed, having to contend with the twin challenges of being a bond-sensitive sector in an environment of expected rate rises, as well as sustained pressure on traditional Australian retail translating to rent pressure for the retail-focused mall owners.

Utilities (+4.6%) did best, driven by strong gains in **ERM Power** (EPW), while **Health Care** (+4.2%) was only slightly behind. Well received results from companies such as **Primary Health Care** (PRY) (+9.9%) helped the sector, as did successful trials from cell-based medicine developer **Mesoblast** (MSB) (+32.8%). **Consumer Discretionary** (+1.5%) also outperformed, helped by the return to profitability of **Nine Entertainment** (NEC) as well as a decent result from the travel sector.

Portfolio performance

The BT Wholesale Smaller Companies Fund returned 3.26% (post-fee, pre-tax) in February 2018, outperforming the S&P/ASX Small Ordinaries Accumulation Index by 3.23%.

Contributors

Underweight A2 Milk

A2 Milk (A2M, +66.8%) surged on its result, which demonstrated better-than-expected growth from its Chinese distribution and came on top of the company opening up a new market in the north-eastern United States last month. We have a positive view on the company and management, however the stock's strong performance breached our valuation target and we used the post-result reaction to lock in our gains and sell out of the position.

Overweight IDP Education

IDP Education (IEL, +20.0%), which provides university placement and English language testing services in Australia, New Zealand, Canada and the US, delivered a well-received set of results. Strong structural trends of students from developing nations seeking overseas tertiary education helped underpin 18% growth in student placements. This, in turn, translated to a 29% gain in revenue and 33% gain in EBITDA for the half (on a constant currency basis). We maintain conviction in the stock based on a strong management team and decent organic growth opportunities.

Detractors

Underweight Bellamy's Australia

The underweight in Bellamy's (BAL, +21.6%) detracted as it continued its remarkable rebound following the travails of last year. We have had exposure to the Chinese food demand theme via A2 Milk and Synlait Milk, which more than offset the detraction from not owning BAL.

Underweight Altium

Altium (ALU, +32.8%) creates software which helps design and test electronic circuits for new products. ALU released a very strong set of figures, with revenue up 30% for the half helped along by strong demand from China. This, alongside disciplined cost management, saw EBITDA and net profit after tax (NPAT) rise by 51%. We have a position in ALU, however it is less than the Index, creating a drag in performance in February.

Review and outlook

The portfolio had a strong month, making good gains even as the index remained flat, in what was a generally good reporting season for our holdings. In addition to A2 Milk and IDP Education, the travel sector delivered strong gains, with Webjet (WEB) reporting that total transaction volume passing through its website was up over 51% for the half. Our position here – and in Corporate Travel Management (CTD) – also helped drive outperformance. Our lack of exposure to some of the retail stocks hardest hit by ongoing challenges to brick-and-mortar retail – including Myer (MYR) and Super Retail (SUL), was likewise beneficial.

The small cap reporting season painted a generally supportive picture, with the index ending the month in positive territory despite the bond-driven tantrum of early February. Downward revisions to consensus earnings outweighed upward moves, however stock generally responded more readily to the latter. It was also the smallest aggregate downward revision in aggregate in 6 halves. Stocks often exhibited a wild initial reaction to results, with stocks shifting up or down up to 15% in a day, which suggests the market is highly tuned to individual companies in this environment. Travel and technology were the strongest sectors, while strong cash flow also supported resources. There was also further signs of a rebound in the long-moribund mining services and infrastructure sectors. Market darlings such as Wisetech, Blackmores and BWX were punished on disappointments, which demonstrates the vulnerabilities that still exist due to elevated valuations in some parts of the small cap market.

Small Cap stocks remain above their historical valuations, in aggregate, and the key to outperformance lies as much in the avoidance of richly-valued stocks which are vulnerable to a de-rating as it does in picking the outperformers. We continue to find opportunities among what we believe to be the latter, with key positions across a broad swathe of industries such as health (Ryman Healthcare), education (IDP Education), agriculture (Synlait Milk), technology (Technology One) as well as those retailers such

as Bapcor, which we believe have a degree of insulation from the challenges facing other segments of the traditional Australian consumer market.

International Shares

BT Concentrated Global Share Fund

Market review

Global equity markets experienced a sharp correction early in February, following a period of relatively sustained bull market conditions that have been in place particularly in the US since October 2016. Markets took a sharp rise in bond yields as a catalyst to sell down equities, which was precipitated by a stronger than expected reading of US labour market data which led to investor concerns over rising inflation, together with the expansionary impact of the US tax cuts package. Key commodity prices were also impacted, with crude oil dipping below the US\$60 mark before partially recovering late in the month, while iron ore made modest gains.

Stocks in the US were carried down with the broader market correction, despite a positive backdrop of resilient corporate earnings and a favourable environment for corporates. The latest earnings season saw a continuation of the positive earnings growth momentum, with a large majority of companies in the S&P500 exceeding the market's consensus expectations. Investors honed in on the prospective risks to growth from more aggressive increases in interest rates by the US Federal Reserve (Fed) and took that as a signal to take profits. Within sectors, there was a fair degree of performance dispersion, with Information Technology being the standout performer, while Energy was the weakest amid rising concerns of high production levels of shale oil in the US and the prospective impact on the oil price. The S&P500 recovered some of its earlier losses to end the month 3.7% lower while the Nasdaq declined by 1.9%.

The major European equity markets were not immune to the US-led global correction in values, which saw the German DAX (-5.7%), the French CAC (-2.9%) and the UK FTSE100 (-4.0%) fall into negative territory. Again, these declines came amid a backdrop of relatively favourable indications for growth in the euro-area economy. Unemployment continued to trend lower, while private sector activity surveys moderated in February following a trend of healthy levels of investment. Within the region, Information Technology was the best performing sector, while the Health Care and Consumer Goods were the worst performers.

The Asian region also followed the path of major developed markets, falling early in the month before retracing some of the losses. Hong Kong (-6.2%) and Japan (-4.5%) were notable laggards this month, while the south-east Asian markets fared better. This group includes Singapore (-0.5%), Malaysia (-0.7%) and Thailand (+0.2%). China dominated most of the region's attention this month, owing to an

expected major shift in the country's constitution to remove the current limitation of two terms on the positions of President and Vice President, thereby providing greater control on growth plans and economic outcomes.

The Australian dollar weakened on currency markets in February, reversing its prior month advance against the US dollar to close 3.6% weaker. The local unit was also 5.9% weaker against the yen, 0.6% lower against the British pound and 1.9% weaker against the euro. Market noise in relation to trade protections and the ramifications for commodities played its part in weakening sentiment towards the local currency.

Portfolio performance

The BT Concentrated Global Share Fund returned 0.32% (post fee, pre-tax) in February 2018, outperforming its benchmark by 0.73%. We are pleased that the Fund was able to obtain a positive return during a volatile and overall negative equity market during the month.

The quarterly reporting season in the US drew to its conclusion in February, with 475 companies of the S&P 500 having reported. 79% of companies reported positive earnings growth on average of 14.5% with 78% of companies having positively surprised versus consensus expectations. However, the earnings season was not an indicator of market direction for the month. After the strongest start to the year in two decades in January, February has proved to be an altogether different month for markets, with the **MSCI All Country World Index** falling 8% in the first week of February, to then recover half of the losses by the end of the month. At the same time the **VIX Index**, (which reflects estimates of future volatility) increased by ~around 180% in the first week of February, and ended up 50% by month end.

Our investment in **CME Group** was up around 8% this month. Our position in CME is consistent with a view at fund launch that over time, interest rates would normalise and volatility would increase from cyclically low levels. CME is the largest derivatives Exchange operator in the world, with the company handling more than 90% of futures trade in the US. Products include futures and options on interest rates, equities, energy, foreign exchange and metals, with about 30% of revenues derived from interest rate products. The company reported fourth-quarter and full-year results for 2017 in February, achieving double-digit average daily volume growth in five out of six product lines. All-time highs in total open interest were reported, along with a record number of large open interest holders across several asset classes. The outlook for 2018 was encouraging, with quarter-to-date revenues in 2018 up 18%. We believe the prospect of rising interest rates, a normalisation of volatility and a strong product pipeline will lead to further year over year increases. By virtue of its strong competitive positioning, the company has been able to increase contract pricing, and together with considered cost control, we believe shareholders will continue to be rewarded with a dividend which currently represents a 6% yield.

Our investment in **Boeing** was up 2% this month. After reporting a strong 2017 result at the end of January, with record earnings, cash flow and commercial airplane deliveries, management presented an upbeat assessment for 2018 when we met with them in the US this month. Management view

aerospace as the strongest industrial sector worldwide, being underpinned by passenger traffic growth at around 7% a year, which compares to the long term trend of 5%. While Boeing views the passenger growth in part as a reflection of the continuing economic growth around the world, they also suggest that the strong fundamentals are consistent with structural changes in the market, with an estimated 100 million passengers in Asia flying for the first time in 2017. Prudently, they remain focused on finding additional efficiencies through the entire supply chain and are guiding for US\$15 billion of operating cash-flow this year, up from \$13.3 billion in 2017. Management remain committed to 100% free cash flow being returned to shareholders and with a strong order back-log, we see little risk to management guidance in 2018.

Our investment in **Wells Fargo** was down 11% this month after the US Federal Reserve issued a cease and desist order to the company, which will require management to cap the growth in assets until the firm submit plans to further enhance Board oversight, compliance and operational risk management. Whilst we are disappointed by the circumstances that resulted in the Federal Reserve Board's actions, we support the order, despite the resultant 2% hit to earning expectations for 2018 and the limited victim and financial impact arising from events leading up to the order .

We initiated our position in Wells Fargo at the Fund's launch in August 2016. We felt that earnings were cyclically depressed and the company had an earnings profile positively exposed to a rising interest rate environment. It was subsequently revealed that between 2011 and 2015 there had been localised abuse of an incentive compensation plan, whereby bank accounts were opened without customer's knowledge. The Board were made aware of the risks in 2014, yet failed to act. The forced resignation of senior management (including the CEO), the claw-back of compensation from management and the part overhaul of the Board were necessary steps in our view. A review of the risk and compliance policies was already under way at Wells Fargo when the Federal Reserve issued its order. However, we believe the additional oversight ensures a third party review of the plans which will ultimately help repair reputational damage associated with the event and give shareholders certainty that a robust system of risk, compliance and oversight becomes entrenched throughout the organisation. Whilst there is a risk of further volatility in the share price as a result of ongoing investigations by other regulators in the US, we continue to believe that the company represents compelling long term value and thus will have patience as we are paid a 7% annual payout rate (Dividend + annual stock buy -back) to wait for these changes to be fully implemented.

Strategy & outlook

Our view at fund inception was that the next five years would be unlike the previous five years, and in a normalising interest rate environment we would see rotation out of the "bond proxies" where valuations still appear fully valued. The Fund is positioned to benefit from a rising interest rate environment. Whilst we expect further volatility, we believe the environment is best suited to owning a concentrated portfolio of companies rather than having broader market exposure. Our portfolio features companies with robust balance sheets, dominant market positions and strong management teams. We invested in these

companies when they were trading below what we considered to be their intrinsic value, and we believe they will continue to prosper in a rising interest rate environment.

BT Wholesale Core Global Share Fund, managed by AQR

Market review

Global equity markets experienced a sharp correction early in February, following a period of relatively sustained bull market conditions that have been in place particularly in the US since October 2016. Markets took a sharp rise in bond yields as a catalyst to sell down equities, which was precipitated by a stronger than expected reading of US labour market data which led to investor concerns over rising inflation, together with the expansionary impact of the US tax cuts package. Key commodity prices were also impacted, with crude oil dipping below the US\$60 mark before partially recovering late in the month, while iron ore made modest gains.

Stocks in the US were carried down with the broader market correction, despite a positive backdrop of resilient corporate earnings and a favourable environment for corporates. The latest earnings season saw a continuation of the positive earnings growth momentum, with a large majority of companies in the S&P500 exceeding the market's consensus expectations. Investors honed in on the prospective risks to growth from more aggressive increases in interest rates by the US Federal Reserve (Fed) and took that as a signal to take profits. Within sectors, there was a fair degree of performance dispersion, with Information Technology being the standout performer, while Energy was the weakest amid rising concerns of high production levels of shale oil in the US and the prospective impact on the oil price. The S&P500 recovered some of its earlier losses to end the month 3.7% lower while the Nasdaq declined by 1.9%.

The major European equity markets were not immune to the US-led global correction in values, which saw the German DAX (-5.7%), the French CAC (-2.9%) and the UK FTSE100 (-4.0%) fall into negative territory. Again, these declines came amid a backdrop of relatively favourable indications for growth in the euro-area economy. Unemployment continued to trend lower, while private sector activity surveys moderated in February following a trend of healthy levels of investment. Within the region, Information Technology was the best performing sector, while the Health Care and Consumer Goods were the worst performers.

The Asian region also followed the path of major developed markets, falling early in the month before retracing some of the losses. Hong Kong (-6.2%) and Japan (-4.5%) were notable laggards this month, while the south-east Asian markets fared better. This group includes Singapore (-0.5%), Malaysia (-0.7%) and Thailand (+0.2%). China dominated most of the region's attention this month, owing to an expected major shift in the country's constitution to remove the current limitation of two terms on the

positions of President and Vice President, thereby providing greater control on growth plans and economic outcomes.

The Australian dollar weakened on currency markets in February, reversing its prior month advance against the US dollar to close 3.6% weaker. The local unit was also 5.9% weaker against the yen, 0.6% lower against the British pound and 1.9% weaker against the euro. Market noise in relation to trade protections and the ramifications for commodities played its part in weakening sentiment towards the local currency.

Portfolio performance

The BT Wholesale Core Global Share Fund returned -0.08% (post-fee, pre-tax) in February 2018, outperforming its benchmark by 0.33%. Outperformance was sourced from Europe and North America, while developed Asia underperformed its regional benchmark over the month.

Thematically, the outperformance in Europe was driven by positive performance of valuation and business quality signals, outweighing negative contributions from momentum and investor sentiment themes. In North America, outperformance was most notably sourced from industry momentum and earnings quality signals, offset somewhat by negative returns to valuation and investor sentiment factors. Developed Asia underperformance was largely attributable to positioning in Japan, where industry valuation themes and earnings quality signals outweighed the positive performance of indirect momentum signals.

From a stock and industry attribution perspective, active industry tilts were the predominant source of outperformance, with intra-industry stock selection also contributing positively to active returns. At a sector level, the underweights to Energy and Consumer Staples were the largest contributors and overweight to Materials the largest offsetting detractor from active returns over the month. Stock selection within industry groups was a positive contributor to outperformance over the month, notably within the Industrials sector. The largest offsets were within Consumer Discretionary and Health Care sectors, where active stock positioning detracted from overall outperformance.

At a stock level, the strongest positive contributors came from overweight positions in Micron Technology Inc., a US headquartered manufacturer of semi-conductors and data storage devices; The Boeing Company; an American multi-national aircraft manufacturer and defence contractor; and Applied Materials Inc., a US headquartered supplier of equipment, services and software to the electronics & technology industries. The largest detractors from active returns were overweight positions in Walmart Inc., an American multinational retail corporation; LyondellBasell Industries N.V., a multinational chemicals company incorporated in the Netherlands; and Atos SE, a European IT services corporation headquartered in France.

Strategy & outlook

Moving into March, 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, Europe and Japan.

Australian Fixed Income

BT Wholesale Fixed Interest Fund

Market review

The Australian government bond curve steepened further in February, which was in sympathy with its global peers. While bond markets experienced reasonable volatility, their swings were much less pronounced than their equity counterparts, particularly the US. Front-end yields in Australia fell as RBA communication suggested the current policy setting would remain appropriate in the near-term. The central bank's Statement on Monetary Policy also revealed its forecasts for inflation and GDP growth were unchanged. Economic data was mixed: Retail sales fell 0.5% and consumer confidence eased back to 102.7. The monthly labour force report revealed 16,000 jobs were added, however this was significantly skewed to part-time roles and quarterly wage figures reported a 0.6% increase for the fourth quarter. Meanwhile, business conditions and confidence numbers rose to a strong +19 and +10 respectively. The local reporting season was also encouraging with more companies beating earnings estimates than missing them. Based on those that had reported by the end of February total EPS had risen 8% for the half year versus the prior corresponding period. Finally in terms of market movements, Australian 3 year yields finished 4 basis points lower at 2.13% while the 10 year maturity ended flat at 2.80%. At the front-end, 90 day BBSW rose 1 basis point to 1.79%.

Portfolio performance

The BT Wholesale Fixed Interest Fund returned 0.31% in February 2018 (post-fees, pre-tax), outperforming its benchmark by 0.02%.

In the alpha overlay, the Duration and FX strategies added to performance, while Yield Curve, Macro and Relative Value strategies detracted. The Government bond component outperformed its benchmark with the Relative Value and Cross-Market strategies adding to performance.

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 Reserve Bank's Statement on Monetary Policy forecast underlying inflation to be at 1.75% for the year ended December 2018, below the low end of their 2 to 3% target band. Labour market slack is expected to remain, with the Reserve Bank seeing the unemployment rate at 5.25% by June 2020. These forecasts do not indicate that the Reserve Bank will be tightening monetary policy anytime soon.

There are however positive signs for the Australian economy despite the subdued inflationary environment. Business confidence and conditions remain above longer term averages. 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 it 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. We question whether monetary policy settings need to be as stimulatory now, despite the current lack of inflationary pressures. The Reserve Bank have however talked down the prospect of any near term policy tightening and appear to be on hold for most, if not all, of 2018.

International Fixed Income

BT Wholesale Global Fixed Interest Fund

Market review

Global bond markets witnessed a further steepening of sovereign curves as yields rose at the long end. Bonds experienced reasonable volatility, however their swings were much less pronounced than their equity counterparts, particularly in the US. The shift in volatility was sparked by a stronger-than-expected rise in US wages, which in turn fed fears of faster monetary tightening. This was compounded by positive comments on the health of the economy by new Fed Chair Jerome Powell. A strong US corporate earnings season and fiscal spending increase were not enough to turn sentiment around. Similarly in Europe, investors found little comfort in another round of dovish comments from ECB President Mario Draghi. That said, risk sentiment did improve towards month-end as the market reassessed the potential impact of higher inflation and outlook for rates. In Asia, confidence in China's economic health was dampened to some degree with weaker-than-expected leading indicators like manufacturing activity. Finally in terms of market movements, US yields were higher across the curve with the 2 year and 10 year rising by 11 basis points and 15 basis points to 2.25% and 2.86% respectively.

Portfolio performance

The BT Wholesale Global Fixed Interest Fund returned -0.25% in February 2018 (post-fees, pre-tax), underperforming its benchmark by 0.21%.

Over the month, the FX strategies added to performance, while the Macro, Duration, Yield Curve and Relative value strategies detracted and the Cross-Market strategy was roughly flat. The portfolio began the month with 4 risk units and closed the month with 8 risk units.

The Duration strategy detracted over the month. The majority of the losses were from long duration positions opened in the US front-end as we believed the front end sell off had become too stretched.

We were stopped out of the positions as market volatility fell after the vol spike. Losses also came from short duration positions in JGBs opened early in the month. These losses were somewhat offset by a long duration position in the long-end of the Japanese curve. Gains were contributed by our existing long duration positions in the front-ends of Australia, New Zealand, Europe and South Korea. Later in the month we opened long duration positions in the front end of Sweden and the long end of Australia and Europe, which also contributed to gains.

The FX strategy added to performance over the month. Among the developed market currencies, short NZD against USD was one of the most profitable trades as the worse-than-expected trade data further weakened the currency. Our intra-month positions in short AUD, NZD and EUR against USD and JPY were roughly flat. In emerging market currencies our short INR against USD and SGD trades were the strongest performers. The existing short MYR and a newly opened short IDR positions were flat for the month. In FX volatility space, we took profit on vol positions in EURUSD, NZDUSD and USDJPY. Early in this month we opened long vol positions in EURAUD, AUDJPY, NZDJPY and GBPJPY. These closed the month largely flat.

The Yield Curve strategy detracted from performance over the month. The majority of losses came from the steepening positions in the Japanese long end as the curve flattened. Losses also came from our steepening positions in the US as the front-end sold off more aggressively than the 5y point. Partially offsetting these losses, our steepeners in New Zealand continued to perform well.

The Cross-Market strategy was roughly flat over the month. We closed our long Australia short New Zealand 5y position in the month and there were no trades remaining as of month end.

The Macro strategy experienced significant performance moves but ended the month with a negative return. Volatility picked up early in the month and credit spreads widened significantly, especially in indices with higher risks such as CDX HY and CDX EM. As expected our Macro trades performed very strongly during the spike in volatility. As risk sentiment turned, credit spreads tightened and we used this opportunity to add to our defensive bias; lifting some of our decompression trade hedges.

The Relative Value strategy detracted over the month. The majority of losses came from our US 2y invoice spread positions which were closed out during the month. Our Australian 3y EFP widener performed steadily over the month and helped to reduce the losses.

Strategy & outlook

The February flash crash and volatility spike served as a warning shot to the market to expect further volatility ahead. As risk assets recovered into the end of the month, that the VIX only recovered back to the top of last year's range is a sign that the worst is not yet behind us. The concerns which triggered the severe market correction during the month linger on, and coupled with the steady drain of central bank liquidity over the next twelve months, we believe this is the year where volatility trends higher. Yet, the growth and inflation backdrop is such that long duration positions cannot be relied upon to be defensive. It is therefore appropriate to increase the level of explicit protection on the portfolio, as US credit markets stand to bear the brunt of a protracted bond sell-off.

Credit

BT Wholesale Enhanced Credit Fund

Market review

The Australian credit market outperformed its global peers and proved resilient in the face of broader negative risk sentiment. After a spike higher in spreads early in the period, caused by fears of higher US inflation, they gradually retraced most of their widening into month's end as the market reassessed the outlook.

In terms of local credit market activity, it was another strong month for issuance with \$6.6 billion in volume across 15 deals. The bulk of this was again from Financials. Westpac issued \$2.6 billion via a 5 year bond at 83 basis points (bp) over swap and a subordinated 10 year bond at 140bp over swap. UBS Australia also raised significant debt capital (\$1.55 billion) with a 3 year note at 70bp over and 5 year at 90bp over swap. Similarly, Lloyds tapped investors for \$750 million via a 7 year bond at 140bp over swap. Corporates accounted for a more modest \$700 million, with GPT Wholesale Shopping and utilities provider AusNet Services both issuing during the month.

The new supply was met by strong demand and signalled appetite for new issuance remained healthy despite the broader softening for risk sentiment. This was echoed in the synthetics space as the Australian iTraxx index (Series 28 contract) traded in a wide 11 bp range, but finished the month only 2bp wider at +59bp. Physical credit spreads were generally unchanged. Semi-government bond spreads slightly underperformed closing 1bp wider to government bonds over the month.

Portfolio performance

The BT Wholesale Enhanced Credit Fund returned 0.36% in February 2018 (post-fees, pre-tax) outperforming its benchmark by 0.02%.

Another strong month of accruals as well as a small tightening in credit spreads and fall in underlying swap rates helped drive a positive return. Positive excess returns were again experienced from positions in infrastructure and utilities. There was no physical portfolio activity during the month.

Strategy & outlook

Our macro credit view is neutral. While we continue to remain cautiously constructive on a fundamental basis, we acknowledge risks have increased due to increasing volatility across markets. Recent volatility has arisen as expectations have changed on the future US rate outlook.

During 2018 it's expected there will be further central bank cash rate increases in the US and the reduction of QE actions by the ECB. Market price dislocations will occur should expectations of central bank actions and emerging economic growth, inflation and labour data not accord to market positioning.

Exogenous factors that could impact credit markets include geopolitical risks emanating from the US, Middle East or China.

Balancing these risks are solid corporate fundamentals, and in turn we are constructive on investment grade credit. Balance sheets are generally strong and earnings are improving as evidenced by solid corporate earnings seasons in Australia, the US and Europe. Further, Australian domestic issuers have not increased balance sheet leverage over the past number of years. The major Australian banks have stronger capital ratios than any years previous supporting domestic financial stability.

Domestically we expect the Australian economy to exhibit improving growth, underpinned by continued commodity demand. However, weak wage growth could continue to dampen overall domestic demand and housing appears to be softening. As such we continue to recommend a defensive approach with any overweights in operationally resilient sectors such as Utilities and Infrastructure that provide a higher yield to index returns.

Cash

BT Wholesale Managed Cash and BT Wholesale Enhanced Cash Funds

Market review

The Australian government bond curve steepened further in February, which was in sympathy with its global peers. While bond markets experienced reasonable volatility, their swings were much less pronounced than their equity counterparts, particularly the US. Front-end yields in Australia fell as RBA communication suggested that the current policy setting would remain appropriate in the near-term. The central bank's Statement on Monetary Policy also revealed its forecasts for inflation and GDP growth were unchanged.

Economic data was mixed during the month. Retail sales fell 0.5% and consumer confidence eased back to 102.7. The monthly labour force report revealed 16,000 jobs were added, however this was significantly skewed to part-time roles and quarterly wage figures reported a 0.6% increase for the fourth quarter. Meanwhile business conditions and confidence numbers rose to a strong +19 and +10 respectively. The local reporting season was also encouraging with more companies beating earnings estimates than missing them. Based on those that had reported by the end of February, total EPS had risen 8% for the half year versus the prior corresponding period.

The US reporting season was also healthy with a strong 15% increase in EPS for the quarter. However, this was not enough to offset concerns over faster-than-anticipated monetary tightening sparked by a strong 2.9% year-on-year rise in average hourly earnings. These fears were fanned by positive comments on the health of the economy by new Fed Chair Jerome Powell in his first testimony to Congress. Meanwhile on the fiscal front, the Senate agreed to a US\$300 billion spending increase over two years.

Turning to Europe, reporting season revealed earnings rose an impressive 36%, based on data for companies that had reported at the end of February. However, regional bourses still suffered as a broader spike in volatility spooked investors. Dovish comments from ECB President Mario Draghi were not enough to turn sentiment and ongoing political squabbles had little impact on markets.

In Asia, confidence in China's economic health was dampened to some degree with weaker-than-expected leading indicators like manufacturing activity. President Xi Jinping removed a constitutional limit on the maximum term the country's ruler can serve after recently announcing his intention to remain in power. In neighbouring Japan, BOJ Governor Kuroda also cemented another term, signalling a continuation of the central bank's policy settings.

Finally in terms of market movements, Australian 3 year yields finished 4bp lower at 2.13% while the 10 year maturity ended flat at 2.80%. At the front-end, 90 day BBSW rose 1bp to 1.79%. US yields were higher across the curve with the 2 year and 10 year higher by 11bp and 15bp to 2.25% and 2.86% respectively. This saw the AU-US 10 year spread cross into negative territory for the first time in 18 years. This weighed on the AUD/USD (-3.6%) to some extent, which was also hurt by a broader risk-off move across markets.

Portfolio performance

Managed Cash

The BT Wholesale Managed Cash Fund returned 0.14% in February 2018 (post-fee, pre-tax), outperforming the benchmark return by 0.01%.

With a higher running yield than the index, the Fund 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 60 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.

Enhanced Cash

The BT Wholesale Enhanced Cash Fund returned 0.16% in February 2018 (post-fee, pre-tax), outperforming its benchmark by 0.03%.

Positive performance came from infrastructure, financials and industrial sectors. Activity during the month included reducing exposure to banks, infrastructure and industrial sectors. As at the end of the month, the portfolio had a credit spread of 60bp over bank bills, interest rate duration of 0.12 years and credit spread duration of 1.69 years.

Strategy & outlook

The Reserve Bank's Statement on Monetary Policy forecast underlying inflation to be at 1.75% for the year ended December 2018, below the low end of their 2 to 3% target band. Labour market slack is expected to remain, with the Reserve Bank seeing the unemployment rate at 5.25% by June 2020. These forecasts do not indicate that the Reserve Bank will be tightening monetary policy anytime soon. There are however positive signs for the Australian economy despite the subdued inflationary environment. Business confidence and conditions remain above longer term averages. 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 it 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. We question whether monetary policy settings need to be as stimulatory now, despite the current lack of inflationary pressures. The Reserve Bank have however talked down the prospect of any near term policy tightening and appear to be on hold for most, if not all, of 2018.

Australian Property

BT Wholesale Property Securities Fund

Market review

The S&P/ASX 200 A-REIT Index declined by 3.3% in February, underperforming the broader market (+0.4%) by 360 basis points (bp). A-REITs were sold off on the back of a steepening US yield curve with US 10-year bonds +5bp to close +15bp higher at 2.86%. The Australian yield curve also steepened by +5bp, although 10-year bonds were flat at 2.81%. It is interesting to note that Australian 10-year bond yields are now lower than US bond yields, something that has not occurred since 2000. Global REITs were down 6.6% for the month, with Japan the best performing market (-3.2%) and the UK the worst performing market (down 8%, both in USD terms).

The AREITs reported their results during the period, with the strongest results in the residential REITs and the Fund managers. Most notably, Goodman Group and Charter Hall Group upgraded guidance for FY18.

Revaluation gains for the six-month period were the highest on record, +\$5.5 billion which was driven mostly by cap rate compression (-17bp to 5.4%) and redevelopment profits (Westfield and Scentre Group). Mirvac Group, Dexus Property Group and Lend Lease all announced stock buybacks, however Vicinity Centres and Investa Office chose not to continue buy backs. Vicinity Centres was very weak over the month (-7.8%), a result of soft comparable income growth of +1%, negative leasing spreads of -1.5% and negative comparable specialty sales growth (-0.7%).

Global equity markets were very soft in February, with the MSCI All Country World Index registering a 4.4% decline, with none of the 11 sectors delivering positive returns. US Headline CPI increased 0.5% (January) and core CPI was +0.35%, the largest monthly gain since March 2005. Non-farm payrolls were strong (+200,000) and the unemployment rate was steady at 4.1%. Consumer confidence continues to be robust, increasing from 124.3 to 130.8, a new high for the current expansion.

In Australia, the Reserve Bank of Australia (RBA) left interest rates on hold. Data was mixed, with an increase in the wage price index (0.6%), taking the annual rate to 2.1% over the year. Retail sales were very weak (-0.5%), dragged down by household goods retailing (-2.6%) and department stores (-0.6%). The Westpac Consumer Confidence Index was lower, down 2.3% to 102.7 and the 12-month forward expectations for the economy was very weak, down 4.7%.

Portfolio performance

The BT Wholesale Property Securities Fund returned -3.22% in February 2018 (post-fee, pre-tax), underperforming its benchmark by 0.07%.

The portfolio underperformed over the month, with positive attribution from underweight positions in Vicinity Centres and GPT Group, and overweight positions in Arena REIT, Charter Hall Group and Westfield Group. Underweight positions in Goodman Group, Shopping Centres Australia, Cromwell Property Group, National Storage and Growthpoint Properties detracted from performance.

Over the month we closed our underweight position in Goodman Group (to neutral) and increased our overweight positions in Charter Hall Group and Dexus Property Group. This was funded by increasing our underweight positions in Scentre Group and GPT Group.

Strategy & outlook

The A-REIT sector is now priced on an FY18 dividend yield of 5.5%, a PE ratio of 15.1 times and a 15% premium to net tangible assets (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 200bp 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)

The global property securities market (on an ex-Australia basis) as measured by the FTSE EPRA/NAREIT Developed Index declined in February, posting a total return of -6.6%. Europe (-7.6%)

was the weakest performing region, followed by North America (-7.2%), and Asia Pacific (-4.5%). In Europe, performance was negative across the region. Italy (-14.8%) posted the largest decline, followed by Finland (-11.4%) and Netherlands (-10.4%). Similarly, in Asia Pacific, results were negative across the region. Singapore (-6.8%) was the worst performer, followed by New Zealand (-5.9%), Hong Kong (-5.3%), and Japan (-3.2%). In North America, the US and Canada returned -7.3% and 5.3%, respectively.

Portfolio performance

The BT Wholesale Global Property Securities Fund returned -6.31% in February 2018 (post-fee, pre-tax) outperforming the benchmark return by 0.12%.

North America

The North America portfolio returned -7.24% in February (before fees and taxes), slightly trailing the FTSE EPRA/NAREIT North America Index by three basis points. Marginal underperformance relative to the benchmark was attributable to negative stock selection results, which were partially offset by positive sector allocation results. In terms of stock selection, results were weakest in the diversified, health care, and triple net lease sectors and were strongest in the hotel, shopping centre, and regional mall sectors. Regarding sector allocation, positive results were largely driven by the portfolio's small cash position, which was a contributor to relative performance in light of the regional benchmark's negative absolute performance for the month. Conversely, the portfolio's overweight to the underperforming data centre sector was a notable detractor. Among the portfolio's holdings, top individual contributors to relative performance included overweight positions in outperforming Retail Properties of America Class A (RPAI), Extended Stay America (STAY), and Boston Properties (BXP). Detractors most notably included overweight positions in underperforming Gramercy Property Trust (GPT) and Empire State Realty Trust Class A (ESRT), and a lack of exposure to the outperforming Extra Space Storage (EXR).

Europe

The European portfolio returned -7.41% in February (before fees and taxes), outperforming the regional EPRA benchmark by 14 basis points. Modest 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 Sweden, Netherlands, and Spain and were weakest in Germany, France, and the United Kingdom. Regarding country allocation, negative results were attributable to the portfolio's underweight to the outperforming Switzerland market and a lack of exposure to the outperforming Austria and Belgium markets. Conversely, the portfolio's small cash position was a contributor to relative performance given the regional benchmark's negative absolute performance for the month. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Fabegé AB (Sweden) and Merlin Properties Socimi SA (Spain), and a lack of exposure to the underperforming Wereldhave NV (Netherlands). Detractors most notably included a lack of exposure to outperforming Swiss Prime Site AG (Switzerland) and overweight positions in underperforming Workspace Group PLC (United Kingdom) and Gecina SA (France).

Asia

The Asia portfolio returned -4.98% in February (before fees and taxes), lagging the regional EPRA benchmark by 51 basis points. Underperformance relative to the benchmark was driven by negative stock selection results, while country allocation results were neutral. In terms of stock selection, results were negative across the region, most notably in Hong Kong and Japan. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming MCUBS MidCity Investment (Japan), Kenedix Office Investment (Japan), and Nippon Building Fund (Japan). Detractors most notably included a lack of exposure to outperforming Hysan Development (Hong Kong) and Orix JREIT (Japan), and an overweight position in underperforming Mapletree Logistics Trust (Singapore).

Active Balanced

BT Wholesale Active Balanced Fund

A spike in market volatility and sell-off in global and domestic equities early in the month prompted some market concern of a sharp correction following a sustained period of strength. However, the falls were arrested swiftly in most markets, which then spent the remainder of the month clawing back lost ground. At its low point for the month, the S&P 500, had fallen a touch over 10% in US\$ terms from its peak in late January, but had regained half of this by the end of February.

The Australian market demonstrated its relatively defensive nature during this episode. It had fallen just over 4% from the start of the month to its lowest point on the 12th of February, but managed to regain all of this by the month's end to finish 0.3% higher. As a result, the local bourse was among the best performing markets globally, ahead of the S&P 500 (-3.9%), German DAX (-5.7%) and Japanese Nikkei (-4.5%).

A key point to consider in the context of this divergence is that Australian equities have not enjoyed the same surge as other developed markets over the last year. For example, the S&P/ASX 300 had gained roughly +7.5% for the 12 months to end January 2018 – versus around +23.8% for the S&P 500. This partly reflects the more defensive nature of the ASX and the different market composition, with **technology stocks** – which have outpaced the rest of the US market on valuation re-rating comprising a much lower proportion of the local market.

The proximate cause of the sell-off was stronger than expected wage data from the US, which prompted speculation of an uplift in inflation and the possibility that the Fed might raise rates faster than previously anticipated. It was therefore the bond-sensitives sectors which bore the brunt of the market's early weakness and **telecommunications (-6.2%)**, **REITs (-3.2%)** and **utilities (-1.6%)** all ended the month down. For the telecommunications sector, the challenging macroeconomic backdrop was exacerbated by a disappointing result from **Telstra (TLS)**, which fell -5.7% for the month. Crude oil also edged lower, down 4.8%, which weighed on the **Energy** sector (-3.8%).

Global equity markets experienced a sharp correction early in February, following a period of relatively sustained bull market conditions that have been in place particularly in the US since October 2016. Markets took a sharp rise in bond yields as a catalyst to sell down equities, which was precipitated by a stronger than expected reading of US labour market data which led to investor concerns over rising inflation, together with the expansionary impact of the US tax cuts package. Key commodity prices were also impacted, with crude oil dipping below the US\$60 mark before partially recovering late in the month, while iron ore made modest gains.

Stocks in the **US** were carried down with the broader market correction, despite a positive backdrop of resilient corporate earnings and a favourable environment for corporates. The latest earnings season saw a continuation of the positive earnings growth momentum, with a large majority of companies in the S&P500 exceeding the market's consensus expectations. Investors honed in on the prospective risks to growth from more aggressive increases in interest rates by the US Federal Reserve (Fed) and took that as a signal to take profits. Within sectors, there was a fair degree of performance dispersion, with Information Technology being the standout performer, while Energy was the weakest amid rising concerns of high production levels of shale oil in the US and the prospective impact on the oil price. The S&P500 recovered some of its earlier losses to end the month 3.7% lower while the Nasdaq declined by 1.9%.

The major **European equity markets** were not immune to the US-led global correction in values, which saw the German DAX (-5.7%), the French CAC (-2.9%) and the UK FTSE100 (-4.0%) fall into negative territory. Again, these declines came amid a backdrop of relatively favourable indications for growth in the euro-area economy. Unemployment continued to trend lower, while private sector activity surveys moderated in February following a trend of healthy levels of investment. Within the region, Information Technology was the best performing sector, while the Health Care and Consumer Goods were the worst performers.

The **Asian region** also followed the path of major developed markets, falling early in the month before retracing some of the losses. Hong Kong (-6.2%) and Japan (-4.5%) were notable laggards this month, while the south-east Asian markets fared better. This group includes Singapore (-0.5%), Malaysia (-0.7%) and Thailand (+0.2%). China dominated most of the region's attention this month, owing to an expected major shift in the country's constitution to remove the current limitation of two terms on the positions of President and Vice President, thereby providing greater control on growth plans and economic outcomes.

The **Australian dollar** weakened on currency markets in February, reversing its prior month advance against the US dollar to close 3.6% weaker. The local unit was also 5.9% weaker against the yen, 0.6% lower against the British pound and 1.9% weaker against the euro. Market noise in relation to trade protections and the ramifications for commodities played its part in weakening sentiment towards the local currency.

Within the fixed interest sector, **Global bond markets** witnessed a further steepening of sovereign curves as yields rose at the long end. Bonds experienced reasonable volatility, however their swings were much less pronounced than their equity counterparts, particularly in the US. The shift in volatility was sparked by a stronger-than-expected rise in US wages, which in turn fed fears of faster monetary tightening. This was compounded by positive comments on the health of the economy by new Fed Chair Jerome Powell. A strong US corporate earnings season and fiscal spending increase were not enough to turn sentiment around. Similarly in Europe, investors found little comfort in another round of dovish comments from ECB President Mario Draghi. That said, risk sentiment did improve towards month-end as the market reassessed the potential impact of higher inflation and outlook for rates. In Asia, confidence in China's economic health was dampened to some degree with weaker-than-expected leading indicators like manufacturing activity. Finally in terms of market movements, US yields were higher across the curve with the 2 year and 10 year rising by 11 basis points and 15 basis points to 2.25% and 2.86% respectively.

The **Australian government bond** curve steepened further in February, which was in sympathy with its global peers. While bond markets experienced reasonable volatility, their swings were much less pronounced than their equity counterparts, particularly the US. Front-end yields in Australia fell as RBA communication suggested the current policy setting would remain appropriate in the near-term. The central bank's Statement on Monetary Policy also revealed its forecasts for inflation and GDP growth were unchanged. Economic data was mixed: Retail sales fell 0.5% and consumer confidence eased back to 102.7. The monthly labour force report revealed 16,000 jobs were added, however this was significantly skewed to part-time roles and quarterly wage figures reported a 0.6% increase for the fourth quarter. Meanwhile, business conditions and confidence numbers rose to a strong +19 and +10 respectively. The local reporting season was also encouraging with more companies beating earnings estimates than missing them. Based on those that had reported by the end of February total EPS had risen 8% for the half year versus the prior corresponding period. Finally in terms of market movements, Australian 3 year yields finished 4 basis points lower at 2.13% while the 10 year maturity ended flat at 2.80%. At the front-end, 90 day BBSW rose 1 basis point to 1.79%.

Portfolio performance

The BT Wholesale Active Balanced Fund returned -0.72% (post-fee, pre-tax) for the month of February, underperforming its benchmark by 0.51%.

The Fund's performance in February was impacted by weak or negative returns from bond-sensitive assets. Equity markets also weakened, however the Fund's asset selection outcomes within Australian and global equity markets delivered positive returns. Exposure to alternatives detracted from returns, while some capital preservation was afforded through the Fund's exposure to cash.

Tactical asset allocation contributions were driven by the Fund's overweight exposure to Australian and 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 Nine Entertainment and Qantas, and underweight positions in Woodside and Souh32. Partially offsetting these contributions were overweight positions in JB Hifi and CBYG, and underweight positions in A2Milk and Insurance Australian Group.

Active returns from our global equities portfolio were sourced primarily from stock selection by concentrated manager, with contributions from positions in CME Group and Boeing, while our holding in Wells Fargo detracted from returns.

Our Alternatives portfolio detracted from returns this month, whereby six of the eight underlying strategies within the core component of the sector generated negative returns. The Alternatives strategy delivered a total return (before fees) of -3.20% vs a cash return of 0.13%. A minor contribution was generated from the Event Driven strategy, which benefitted from low deal cancellations. The Managed Futures strategy suffered from reversals in equity, commodity and currency markets, although losses were offset somewhat by gains within Fixed Income markets. Within the Equity Market Neutral strategy, positioning within all major regions generated losses over February, though most pronounced in the US. Thematically, Value was the main detractor over the period, with Quality themes also underperforming during the market sell off. Within the Dedicated Short Bias strategy, while the directional short equities component generated profits, these were outweighed by the underperformance of the market neutral stock portfolio. The Alternatives core strategy is operating at slightly less than its long-term risk target, with the largest underweights being Convertible Arbitrage and Fixed Income Relative Value. The sole overweight as at the end of February was Long/Short Equity.

February was the first negative month for our tactical positioning within alternatives since the 3bp deduction in May of last year. Deductions occurred from our managed futures and commodity exposures. This outcome is considered normal behaviour for TAA during short-term market pull-backs. Within our managed volatility strategy, given the record movements and unpredictable volatility of this market over the course of the month, an underperformance of around 10bp is considered a respectable result.

Strategy and Outlook

February's market volatility has again illustrated the importance of 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. Despite the short-term pullback, we remain overweight in all three equity markets as one-year momentum remains strong. We retain an overweight to Australian 10-year bonds, but our models have turned to a short signal in both US and Germany. We are implementing this change incrementally over the course of March as we see these markets vulnerable to a short-term squeeze higher. As with equities, we remain overweight all three commodity markets despite the short-term pullback as one-year momentum remains strong.

We recognise the inherent uncertainty of financial markets and continue to hold a broad range of diversifying exposures to defensive and alternatives assets to preserve capital and diversify the asset base.

Performance as at 28 February 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									
Total Return (post-fee, pre-tax)	144	4.09	9.82	11.45	15.33	16.53	6.20	9.34	10.10
Total Return (pre-fee, pre-tax)	151	4.30	10.27	12.05	16.27	17.46	7.05	10.21	11.10
Benchmark	0.34	1.80	7.72	8.54	10.34	16.02	5.22	7.95	9.98
BT Wholesale Imputation Fund									
Total Return (post-fee, pre-tax)	0.82	2.79	7.99	8.59	11.32	14.86	4.05	7.37	9.58
Total Return (pre-fee, pre-tax)	0.89	3.02	8.47	9.24	12.32	15.89	4.98	8.34	10.60
Benchmark	0.34	1.80	7.72	8.54	10.34	16.02	5.22	7.95	8.74
BT Wholesale Focus Australian Share Fund									
Total Return (post-fee, pre-tax)	176	5.03	10.64	12.30	17.75	18.76	8.15	11.48	9.55
Total Return (pre-fee, pre-tax)	2.02	5.74	11.54	13.51	20.01	20.20	9.50	12.65	10.69
Benchmark	0.34	1.80	7.72	8.54	10.34	16.02	5.22	7.95	7.53
BT Wholesale Ethical Share Fund									
Total Return (post-fee, pre-tax)	127	4.11	9.84	11.44	15.26	16.42	6.35	9.45	8.75
Total Return (pre-fee, pre-tax)	134	4.36	10.36	12.15	16.37	17.52	7.36	10.49	9.81
Benchmark	0.34	1.80	7.72	8.54	10.34	16.02	5.22	7.95	8.10
Australian Shares - Mid Cap									
BT Wholesale MidCap Fund									
Total Return (post-fee, pre-tax)	180	5.82	15.95	18.94	26.34	22.13	14.31	15.08	11.18
Total Return (pre-fee, pre-tax)	2.08	6.78	17.15	20.51	28.38	23.67	15.84	16.87	13.47
Benchmark	0.85	2.95	13.28	13.91	21.32	20.82	12.63	12.23	6.11
Australian Shares - Small Cap									
BT Wholesale Smaller Companies Fund									
Total Return (post-fee, pre-tax)	3.26	4.78	15.18	18.81	22.30	17.41	12.38	10.48	13.40
Total Return (pre-fee, pre-tax)	3.36	5.11	15.90	19.80	23.83	18.87	13.78	11.86	14.69
Benchmark	0.03	2.67	14.58	18.09	20.81	18.78	10.81	6.22	7.89
Australian Shares - Micro Cap									
BT Wholesale MicroCap Opportunities Fund									
Total Return (post-fee, pre-tax)	-0.77	5.55	13.95	18.35	22.69	23.25	18.24	18.77	18.99
Total Return (pre-fee, pre-tax)	-0.94	5.86	14.22	19.33	24.61	25.67	21.50	23.50	24.31
Benchmark	0.03	2.67	14.58	18.09	20.81	18.78	10.81	6.22	3.26
International Shares									
BT Wholesale Core Global Share Fund									
Total Return (post-fee, pre-tax)	-0.08	0.16	11.05	10.98	17.13	13.66	8.01	17.14	5.89
Total Return (pre-fee, pre-tax)	-0.01	0.40	11.58	11.69	18.25	14.74	9.04	18.26	7.05
Benchmark	-0.41	-0.40	10.91	9.94	15.99	14.16	8.47	17.23	7.30
BT Global Emerging Markets Opportunities Fund - Wholesale									
Total Return (post-fee, pre-tax)	-154	-123	7.64	11.29	25.20	20.95	6.94	11.95	11.90
Total Return (pre-fee, pre-tax)	-142	-0.88	8.39	12.32	26.95	22.64	8.43	13.67	14.14
Benchmark	-0.88	4.29	12.55	17.91	28.77	24.44	9.13	10.91	12.23
BT Concentrated Global Share Fund									
Total Return (post-fee, pre-tax)	0.32	2.35	13.21	12.53	21.34	N/A	N/A	N/A	17.39
Total Return (pre-fee, pre-tax)	0.41	2.66	13.91	13.47	22.85	N/A	N/A	N/A	18.86
Benchmark	-0.41	-0.40	10.91	9.94	15.99	N/A	N/A	N/A	14.38
Property									
BT Wholesale Property Securities Fund									
Total Return (post-fee, pre-tax)	-3.22	-6.04	143	2.45	0.05	4.46	4.76	9.72	7.23
Total Return (pre-fee, pre-tax)	-3.17	-5.89	176	2.89	0.71	5.14	5.44	10.44	8.04
Benchmark	-3.15	-6.18	158	2.96	0.52	4.29	5.04	10.19	7.10
BT Wholesale Global Property Securities Fund									
Total Return (post-fee, pre-tax)	-6.31	-6.25	-4.27	-2.95	-1.91	4.98	1.22	7.07	8.73
Total Return (pre-fee, pre-tax)	-6.24	-6.03	-3.83	-2.35	-1.00	5.95	2.15	8.07	9.72
Benchmark	-6.43	-6.55	-4.54	-3.43	-2.68	5.28	1.21	7.24	8.44
Fixed Interest									
BT Wholesale Fixed Interest Fund									
Total Return (post-fee, pre-tax)	0.31	-0.47	0.94	1.24	2.72	1.22	1.45	3.61	6.41
Total Return (pre-fee, pre-tax)	0.35	-0.35	1.19	1.58	3.23	1.72	1.96	4.13	6.96
Benchmark	0.29	-0.50	1.15	1.40	2.87	2.15	2.42	4.08	6.63
BT Wholesale Global Fixed Interest Fund									
Total Return (post-fee, pre-tax)	-0.25	-0.93	-1.21	0.09	0.92	0.43	1.72	3.75	5.99
Total Return (pre-fee, pre-tax)	-0.21	-0.80	-0.95	0.45	1.46	0.97	2.26	4.30	6.58
Benchmark	-0.04	-0.70	-0.68	0.66	1.65	1.57	2.92	4.61	6.91
BT Wholesale Enhanced Credit Fund									
Total Return (post-fee, pre-tax)	0.36	0.09	1.64	2.30	3.82	3.28	3.08	4.47	5.76
Total Return (pre-fee, pre-tax)	0.39	0.20	1.87	2.60	4.29	3.75	3.54	4.94	6.29
Benchmark	0.34	0.09	1.56	2.15	3.75	3.27	3.06	4.44	5.86
Cash & Income									
BT Wholesale Enhanced Cash Fund									
Total Return (post-fee, pre-tax)	0.16	0.73	1.46	2.05	3.11	2.97	2.72	2.97	4.96
Total Return (pre-fee, pre-tax)	0.18	0.79	1.59	2.22	3.36	3.22	2.98	3.23	5.30
Benchmark	0.13	0.43	0.86	1.15	1.75	1.87	1.99	2.30	4.90
BT Wholesale Managed Cash Fund									
Total Return (post-fee, pre-tax)	0.14	0.43	0.88	1.18	1.78	1.91	2.02	2.28	6.47
Total Return (pre-fee, pre-tax)	0.15	0.49	0.99	1.32	2.00	2.13	2.24	2.51	6.77
Benchmark	0.13	0.43	0.86	1.15	1.75	1.87	1.99	2.30	6.55
BT Wholesale Monthly Income Plus Fund									
Total Return (post-fee, pre-tax)	-0.07	0.44	2.96	3.87	5.44	4.43	3.48	4.79	5.57
Total Return (pre-fee, pre-tax)	-0.02	0.60	3.29	4.32	6.13	5.11	4.16	5.48	6.24
Benchmark	0.12	0.37	0.75	1.00	1.51	1.59	1.75	2.09	2.95
Diversified									
BT Wholesale Active Balanced Fund									
Total Return (post-fee, pre-tax)	-0.72	0.72	6.39	7.54	10.58	10.12	5.02	8.72	7.72
Total Return (pre-fee, pre-tax)	-0.64	0.96	6.90	8.23	11.62	11.16	6.02	9.76	8.79
Benchmark	-0.21	0.44	5.73	6.30	8.59	10.50	5.42	8.25	7.51

All returns calculated by BT Investment Management (Fund Services) Limited, ABN 13 161 249 332, AFSL 431426 (BTIM). No part of this Fund Manager Commentary (Commentary) is to be circulated without this page attached.

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