BT Wholesale Moderate Fund

ARSN: 610 997 709

About the Fund

The BT Wholesale Moderate Fund (**Fund**) is an actively managed diversified portfolio that invests in Australian and international shares, Australian and international listed property securities, Australian and international fixed interest, cash and alternative investments. The Fund has a similar weighting towards defensive assets as it does towards growth assets.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the Fund's benchmark over the medium to long term. The suggested investment timeframe is five years or more.

Benchmark

The benchmark for the Fund is created from a range of published indices. The benchmark is based on the asset allocation neutral position and the index returns for each asset class. Details of the particular market indices used for the Fund's benchmark can be found at www.btim.com.au/BT-Wholesale-Moderate-Fund

Investment Process

At BTIM, we actively manage our portfolios to meet their investment objectives by diversifying investments across both asset classes *and* strategies. We employ three main approaches to do this:

1. **Strategic asset allocation** – weighted asset class exposures designed to meet the investment objectives over the long term investment horizon
2. **Active management** – exploitation of market inefficiencies within asset classes
3. **Tactical asset allocation** – exploitation of market directionality across asset classes

The underlying investments in the Fund are managed by BTIM together with a number of external partners. BTIM manages investments in the asset classes of Australian shares, Australian fixed interest and cash, global fixed interest, Australian property securities and alternative investments. These investments are augmented by our arrangements with leading global investment managers who have a competitive advantage in the management of global asset classes.

The BTIM Diversified team also manages an active tactical asset allocation process designed to increase portfolio returns within a defined risk budget.

Investment Guidelines

Asset allocation ranges (%)	Neutral Position	Ranges	
		Min	Max
Australian shares	24	10	30
International shares	17	0	20
Australian fixed interest	20	10	45
International fixed interest	15	5	40
Australian property securities	4	0	15
International property securities	1	0	15
Alternative investments	14	0	20
Cash	5	3	30

Investment Team

The Fund is managed by Stuart Eliot who has more than 26 year's industry experience. The team has a diverse skill set; combining a range of global and domestic market experience and drawing on the resources of BTIM's other specialist teams: Income & Fixed Interest Strategies and Equity Strategies.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	0.53	0.60	0.23
3 months	4.02	4.24	3.70
6 months	5.80	6.24	4.74
1 year (pa)	8.91	9.82	7.20
Since Inception (pa)	8.00	8.91	7.00

Asset Allocation (as at 31 December 2017)

Australian shares	23.1%
International shares	18.9%
Australian fixed interest	16.4%
International fixed interest	13.0%
Australian property securities	4.5%
International property securities	0.9%
Alternative investments	15.3%
Cash	7.9%

Other Information

Fund size (as at 31 Dec 2017)	$105 million
Date of inception	June 2016
Minimum investment	$25,000
Buy-sell spread[1]	0.24% (0.12%/0.12%)
Distribution frequency	Quarterly
APIR code	BTA0487AU

[1] The buy-sell spread represents transaction costs incurred whenever you invest or withdraw funds, and may vary from time to time without notice.

Management Costs[2]

Issuer fee[3]	0.85% pa
Estimated indirect costs[4]	0.06% pa

[2] You should refer to the latest Product Disclosure Statement for full details of fees and other costs you may be charged.

[3] This is the fee we charge for overseeing the operations of the Fund and managing the assets of the Fund. The Issuer fee is paid from the assets of the Fund and is reflected in the unit price of your investment.

[4] This is an estimate of the last financial year's indirect costs. These are reflected in the unit price of the Fund and are not charged to you as a fee or retained by us.

Risks

An investment in the Fund involves risk, including:

- **Market risk -** The risk associated with factors that can influence the direction and volatility of an overall market, as opposed to security-specific risks. These factors can affect one country or a number of countries.
- **International investments risk** – The risk arising from political and economic uncertainties, interest rate movements and differences in regulatory supervision associated with international investments.
- **Currency risk -** Currency exchange rate fluctuation risk arising from investing across multiple countries.
- **Credit risk -** The risk of an issuing entity defaulting on its obligation to pay interest/principal when due.
- **Liquidity risk -** The risk that an asset may not be converted to cash in a timely manner.
- **Counterparty risk -** The risk of another party to a transaction failing to meet its obligations.

Please read the Fund's Product Disclosure Statement (**PDS**) for a detailed explanation of each of these risks.

Market review

Performance for the domestic equity market was strong over the final quarter of 2017. The S&P/ASX 300 Accumulation Index advanced by 7.7% over the quarter, where most of the hard lifting was done by Resources (+15.6%) as commodity prices continue to rise, supporting the miners and the oil companies. Industrials (+6.1%) enjoyed a lower, albeit positive return.

In terms of sector performance, all the 11 GICS sectors finished the quarter with positive returns, with Materials (+13.0%) leading the group. The diversified miner duo, BHP (BHP, +14.7%) and Rio Tinto (RIO, +13.9%) both finished the quarter meaningfully higher, assisted by rising iron ore and copper prices on the back on the continuous local production curbs imposed by China. Also contributing to sector performance was steel manufacturer, Bluescope (BSL) which added a hefty 40.1% over the quarter. BSL sold off in August when management reported underwhelming FY17 results, alongside a weak guidance for the current half yearly earnings. This guidance was upgraded in December as a result of higher steel prices and domestic volumes. The company will also benefit from the latest US tax reform as a partial US dollar earner. Conversely, notable detractors within Materials over the quarter include lower-grade iron ore producer, Fortescue (FMG, -5.1%), and explosives manufacturer, Orica (ORI, -7.0%). As the discount between high-grade and low-grade iron ore continued to widen due to increased demand for quality ores from Chinese buyers, FMG's share price weakened. For Orica, the disappointing FY17 result released in November saw the share price retreat over the period but recouped some of the losses in December. Outside of Materials, performance from Energy (+18.3%) was also strong over the quarter. The oil price rose over the quarter and touched a two-year high during December as strong global demand as well as production disruptions in Libya and the North Sea supported the commodity price. As such, major oil companies, including Origin Energy (ORG, +25.9%), Woodside Petroleum (WPL, +13.7%) and Santos (STO, +35.6%) all recorded meaningful gains. For STO, the revelation of Harbour Energy's offer to acquire the company back in August also lifted investor sentiment. Other sectors that posted a double-digit gain over the quarter include Consumer Staples (+10.6%), Consumer Discretionary (+10.3%) and Information Technology (+16.7%).

On the other side of the spectrum, performance from index heavyweight, Financials (+3.7%), was less impressive. The confirmation of a Royal Commission into the banks weighed on the Big Four, with two of the four finishing the quarter in the red (ANZ, -0.3%; NAB, -3.1%); whilst gains from the other two were also somewhat muted (WBC, +1.1%; CBA, +6.8%). NAB incurred some selling after unveiling the additional spending of $1.5 billion for the restructure plan over the next three years. Also finishing below the index's return was Real Estate (+6.5%). Outperformance of Westfield (WFD, +21%) which was largely attributed to news of a cash and scrip acquisition offer from European commercial property giant Unibail-Rodamco, was somewhat offset by the 8.8% loss from Lendlease (LLC). Management downgraded the outlook for its Australian construction business for FY18 due to issues with some engineering projects, which weighed on LLC's share price.

Global equity markets closed the year with strong returns for the December quarter, with the MSCI World ex Australia Total Return (A$) Index returning 5.8%. Market sentiment continued to favour the major share markets, aided by strong earnings from the US, a moderating of geopolitical news on the North Korea front, and the prospect of a major overhaul of US tax policy which came to fruition in December. Key commodity prices moved along an upward trajectory, with crude oil (West Texas Intermediate) trading above the US$60/bbl mark, iron ore rising above US$75/mt and copper rallying to well above US$3/lb on supportive demand from China. The red metal has risen by over 30% for the year, while crude oil has risen to its highest level since June 2015. Bullish conditions in capital markets have pushed the MSCI World ex Australia (A$) Index to its sixth consecutive year of strong positive returns.

The US equity market enjoyed a strong quarter, buoyed by continuing strong economic momentum and policy developments. The Trump agenda for tax cuts reached completion following passage of the US Tax Reform Bill through both houses of Congress to be signed into law. The policy will see the corporate tax rate fall to 21% from its current 35%, together with measures to improve interest on debt and spending deductions for companies. This spurred a rotation away from the technology sector towards financials. Although, major technology heavyweights – Microsoft, Intel and Alphabet – reported earnings that were above consensus estimates and acted to support sentiment across the market. The US Federal Reserve also followed through with its well-flagged intention to raise interest rates, with the policy setting board passing a unanimous decision to raise the Fed Funds Rate by 25 basis points. The S&P500 delivered a 6.6% total return while the Nasdaq was up 6.3%.

Returns from major European equity markets were mixed for the December quarter, with returns from the German DAX (+0.7%) and the French CAC (-0.3%) highlighting the muted sentiment across the region. Falling bond yields and benign inflation indications led to a risk-off environment, while positive signals on the Eurozone economy such as unemployment falling to 8.8% the lowest level in nine years – together with generally strong private sector, manufacturing and consumer sentiment surveys, failed to placate markets. Companies within the base metals and consumer sectors were among the best performers, while utility stocks were generally weak.

The UK market delivered strong gains, aided by the broad representation of resource companies that enjoyed strengthening commodity prices. The FTSE Index rose by 4.7% for the quarter, while the Bank of England decided unanimously to maintain interest rates at 0.5%, but confirmed it expects 'further modest increases' as the economy moves towards the 2% inflation target. The country's latest quarterly GDP growth came in at 0.6%, slightly ahead of expectations.

Asian markets benefitted from the positive developments offshore and strong conditions domestically to deliver gains for the quarter. Japan (+11.8%) and Hong Kong (+8.6%) led the region's gains, with investors indicating support for Japan's ruling coalition's return to power. The consolidation of Xi Jinping's power at China's 19th Communist Party assembly similarly supported the Hong Kong and Chinese stock markets. Meanwhile, data released during the period revealed that China grew at a healthy 6.8% over the year, which added to support for the market.

The Australian dollar finished the quarter little changed against the US dollar and British pound, but was 1.9% weaker against the euro. The local currency was a direct beneficiary of stronger commodity prices and stabilising demand from China, thereby rising during December in spite of the hike in US interest rates.

Within the fixed interest sector, Global yield curves witnessed a pronounced flattening during the final quarter of 2017. US 2 year yields rose a sizeable 40bp to 1.89%, while 10 year yields added a more modest 8bp to 2.41%. The front-end increase was shaped in part by the Federal Reserve's December hike, which had been well-broadcast leading up to the meeting. Investor sentiment more broadly was supported by the passing of much-anticipated US tax reform. Strong US data like ISM manufacturing, retail sales and GDP growth also helped support risk appetite. Economic releases were also solid in Europe and dovish messaging from the ECB was perceived positively. Meanwhile, in Asia Xi Jinping consolidated his power at the 19th Communist party assembly and emphasised quality over quantity for future growth. Data released during the period revealed the Asian giant grew at a healthy 6.8% over the year. Reasonable leading indicators and import figures were also encouraging. Elsewhere, pockets of geopolitical risks like Catalonia's push for independence, Merkel's coalition losing its majority and North Korean missile tests had little impact on markets.

The Australian bond market performed reasonably well during the final quarter of 2017. A flattening of the curve was a prominent feature over the period, which was in sympathy with its global peers. Australian 10 year yields fell 19bp to 2.65%, while at the shorter end 90 day BBSW and 3 year yields rose 9bp and 2bp to 1.80% and 2.14% respectively. Rhetoric from the RBA during the period suggested little need to change policy in the nearer term. Statements from Governor Lowe highlighted several areas of strength in the local economy like business conditions and employment growth. At the same time, persistently subdued inflation, particularly wage inflation as well as soft consumption remained a feature in his communication. These points were echoed in data throughout the quarter. The NAB Business Conditions survey hit its highest level on record, before retreating slightly in December. Strong job growth helped bring the unemployment rate down 0.2% to 5.4% and was encouragingly skewed to full-time positions. Third quarter inflation data revealed a weaker-than-expected 0.4% increase in the trimmed mean measure. Wages were also softer-than-anticipated with a 0.5% rise over the quarter. GDP for the September quarter was more constructive with a 0.6% gain, which brought year-on-year growth to 2.8%.

Fund performance

The Fund outperformed its benchmark over the December quarter. The Fund's performance for December quarter was materially driven by the strong performance of growth assets, while exposure to fixed interest assets made smaller but positive contributions. Exposure to alternatives also contributed to returns.

The key factors influencing our active management returns were our material exposure to Australian and global equity strategies. Within the Australian equity strategy, stock selection outcomes were the primary driver of active returns, particularly through overweight positions in Metcash and Santos. Contributions were also sourced from holding no exposure to National Australia Bank, although the manager's preferred banking exposure in ANZ Banking Group detracted from relative performance.

All of our developed market global equity managers delivered outperformance over the quarter, which more than offset a minor detraction from active returns by our emerging markets manager. Stock selection and industry exposure outcomes for both our core and concentrated managers added value.

Our Alternatives strategy delivered a positive return for the quarter, with a significant contribution from the core component. The Alternatives strategy delivered a total return (before fees) of 2.14% vs a cash return of 0.42%. Within the underlying strategies, contributions were sourced from the managed futures, market neutral, asset allocation, risk parity and equity income strategies, while our global macro and Australian fixed interest components detracted from returns.

Our tactical positioning within alternatives made a further contribution to returns. A long position in copper together with long equity market exposure and tactical positioning in gold and crude oil produced a material contribution to returns, as did the Fund's short volatility position These positions more than offset a small detraction from long positions in Australian and German bonds.

Strategy and Outlook

Looking into 2018, there are several key issues which we believe should remain at the forefront of investor focus. The first is liquidity, which is no longer providing a tailwind to markets as central banks around the world tighten policy and start to shrink balance sheets. At this point the pace of tightening remains moderate and should allow the market to retain the prevailing valuation rating, however we remain mindful of the risk of over-tightening and keep a watchful eye on this space. We also maintain a close eye on bond yields, given the sensitivity which a large swathe of the Australian market has to changes here.

China remains crucial to equity market fundamentals and sentiment. The economic outlook remains stable at this point, with GDP growth expected to continue on its multi-year path of moderate deceleration. The Government remains focused on corporate profitability to help address the country's debt problem and relieve stress on the financial system.

The US economy has received significant impetus for further gains. While the market is not considered cheap based on valuations, many corporates are in strong positions supported by buoyant economic conditions, strong balance sheets and policy support through still low interest rates and forthcoming tax cuts.

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.