Stonehouse Core Value Portfolio
Monthly Update - April 2016

April Performance Overview

The Stonehouse Core Value Portfolio (CVP) rose +1.41% over April with Equity and Fixed Income markets staging a welcome rally over the month.

Almost all Equity holdings delivered positive returns with Henderson Natural Resources (+12.95%) and Allan Gray (+7.46%) being the standout performers in this asset class. Listed Property and Infrastructure strategies delivered good results with the highest returns coming from Cromwell (+2.50%) and SG Hiscock (+1.65%).

Fixed Income Holdings were also broadly positive with CQS (+1.61%), Kapstream (+0.47%) and Payden & Rygel (+0.96%) all performing well.

Negative performance came from our Alternatives holdings with Invesco GTR being the best performer with a positive return of +1.07%. Other Alternative strategies including 36 South, AQR Managed Futures, Bennelong Long Short and Blackrock Absolute Return drew back over this period with returns ranging from -1.93% to -2.36%. As previously noted however these Alternative holdings often act as 'insurance' against negative equity market movements, so it is not unusual to see these results in a fairly bullish month for Equities.

While the last few quarters have seen the Investment Committee focused on capital preservation and managing downside volatility, recent months have also seen the Committee undertake a thorough review of our Fixed Income holdings with a particular focus on re-modelling the mix of assets in this space. Accordingly, we removed one underperforming manager (Schroder Fixed Income) and added a new, T. Rowe Price, who adopt a more dynamic management style with an absolute return focus. In addition, we are presently re-evaluating all Equity and Alternative holdings to ensure the Portfolio captures most upside equity market movements whilst continuing to limit downside risk in the Portfolio.

Portfolio Summary

	Stonehouse Core Value Portfolio
Unit price	$1.0613

Asset class ranges & current allocations[1]	Range	Current exposure
Cash & Fixed Int.	15% – 60%	26.4%
Property	0% – 25%	4.4%
Equities	25% – 65%	46.3%
Alternatives	5% – 35%	22.9%

Top 10 investment holdings (ex cash)
1. Statestreet S&P/ASX 200 ETF
2. AQR Managed Futures
3. Northcape Emerging Markets
4. Bennelong Long Short Equity
5. Payden and Rygel Global Income Opportunities
6. Kapstream Absolute Return
7. Ardea Inflation Plus
8. Wingate Global Equity Income
9. Platinum International Class A
10. Invesco GTR

[1] The current exposures include the underlying asset allocations of each investment. The total exposure may not sum to 100% due to any direct derivative investments (such as options and futures).

AFSL: 292 469

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Market Performance and Outlook

Following the strong equity rally over the past two months, the well-known adage of "sell in May and go away, come back on St Leger's Day" is front of mind.

Our main concern continues to be the high valuation levels in the US against a backdrop of weakening earnings growth and heightened political uncertainty. While the consensus is growing that central banks will continue to support markets, given the muted growth and a number of structural headwinds (high debt levels, China transitions, excess capacity, etc.) the risk of correction in the short to medium term remains elevated.

In the US, politics is increasingly likely to spill over into markets in coming months now that two likely candidates for the presidential race have emerged, Donald Trump and Hillary Clinton. While the latter has made plenty of promises to crack down on Wall Street, the former is the more feared of the two as the market may have to contend with the possibility of capricious policymaking in areas ranging from immigration to finance. However, the equity market continues to be complacent in pricing these risks with the VIX (a measure of US equity market risk) currently below 15 - well below its long term average of 20.

Valuations outside the US remain more attractive, especially in Europe, Japan and Emerging Markets, however, these regions face their own challenges.

In Europe, the European Central Bank (ECB) decided to keep rates on hold at its latest meeting though President Draghi indicated that the ECB remains ready to do more if needed. On a negative front, the IMF has again started placing pressure on the European Union to resume talks with Greece in order to resolve the country's ongoing debt problems, meanwhile in Greece there was a general strike over changes to the country's pension and tax systems (Bailout funding from the EU is contingent on the reforms being implemented).

The Bank of Japan (BoJ) also surprised markets by leaving its monetary policy unchanged while continuing to gauge the impact of their negative interest rate policy. Markets reacted by strengthening the Yen and Japanese stocks selling off – the exact opposite of the BoJ's intentions. We anticipate further policy measures in the near future and continue to monitor these developments closely as this may provide us an opportunistic investment entry point.

The Australian share market has held up well recently as renewed stimulus measures in China have lifted resources and concerns about the risks around the Australian banks have abated somewhat, at least for now. In addition, the local equity market received a boost from the Reserve Bank of Australia's (RBA) surprising cut in the official cash rate, to its lowest on record at 1.75%. In justifying the move, the RBA cited unexpectedly low inflation data in the March quarter and the Bank's downward revision to the inflation forecast (from 2.0% to 1.5%). Further interest rate cuts are likely, as it appears that the RBA is trying to stay ahead of the curve and pre-empt a potential self-perpetuating deflationary cycle that has been evident in Japan.

For investors reliant on interest from cash, the decision by the RBA to cut the cash rate again will push deposit rates down to levels not seen since the 1950s. Beyond day to day cash requirements, a key decision for investors currently holding cash or term deposits is to determine what is of greatest importance: absolute certainty regarding the nominal capital value of their investment or taking some risk by investing in a risk-controlled portfolio that aims to compound returns over time.

The upcoming Australian election may also add to the uncertainty especially in the absence of a decisive victory. Historically, the domestic share market has tracked sideways in the run up to elections however on average it has gained around 5% in the three months that follow.

In these turbulent markets, we remain disciplined long-term investors, focusing on capturing upside opportunities whilst maintaining downside protection. It is critical to remain vigilant and continue monitoring and adjusting equity holdings within the Portfolio bearing in mind valuations, policy stance and macroeconomic considerations. More broadly, it is important to maintain diversification across the asset classes whilst relying on active investment managers with a good track record who are able to exploit opportunities as they are presented.