Core Value Portfolio

Monthly Update – December 2019

December Performance Overview

Performance for equity markets was weak in December with both the Australian equity market (-1.9%) and MSCI World Equity Index (-0.9%) posting losses. The Core Value Portfolio (CVP) capped off the year with a flat monthly return of +0.02%, a pleasing result which brought the calendar year return to +11.2%.

Despite the Australian equity market falling in December, SGH ICE delivered a small positive return (+0.1%). The remaining managers detracted for the month, led by the beta exposure in Macquarie Australian Shares True Index (-2.0%). The active managers all outperformed the index with Allan Gray Australian Equity (-1.9%), IML Equity Income (-1.8%) and Firetrail Australian High Conviction (-1.4%).

The global equity exposures provided mixed results in December. The best performing strategy was Northcape Emerging Markets (+2.1%) followed by Platinum International (+1.5%) and Loomis Sayles Global Equity (+0.0%). While Lazard Global Equity Franchise (-1.9%), and Talaria Global Equity (-0.8%) had a tough December period.

The Alternatives allocation had a convincing month, delivering much needed diversification. BetaShares Gold Bullion ETF returned a solid +4.4% followed by Bennelong Long Short Equity (+2.4%) and Partners Group Global Multi-Asset (+0.6%).

The performance of the property and infrastructure managers also varied in December. Both Lazard Global Listed Infrastructure (+2.9%) and AMP Capital Core Infrastructure (+1.5%) were positive contributors to the portfolio return while Resolution Capital Global Property (-3.9%) and Cromwell Phoenix Property Securities (-1.3%) both detracted..

Performance for most of the fixed income exposures was strong. The best preforming manager was CQS Credit Multi-Asset (+1.3%) followed by Alexander Fixed Income (+0.5%), Aquasia Enhanced Credit (+0.4%) and Payden Global Income Opportunities (+0.1%). Franklin Templeton Australian Core Bond Plus (-1.7%) was a drag on returns while Ardea Real Outcome (-0.0%) was flat.

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stonehouse

Portfolio Summary

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Unit Price at 31 December 2019	$1.1090

Asset Class Ranges & Current Allocations [1]		Current Exposure
Cash & Fixed Interest	15% - 60%	39.7%
Property	0% - 25%	11.3%
Equities	25% - 65%	37.4%
Alternatives	5% - 35%	11.6%

[1] The total exposure may not sum to 100% due to any direct derivative investments (such as options and futures).

Top 10 Investment Holdings (ex cash)	
1.	Aquasia Enhanced Credit
2.	Alexander Fixed Income
3.	Franklin Templeton Australian Core Bond
4.	Ardea Real Outcome
5.	Talaria Global Equity
6.	IML Equity
7.	Platinum International
8.	Loomis Sayles Global Equity
9.	Lazard Global Equity Franchise
10.	Northcape Emerging Markets

Market Performance and Outlook

Markets went into December hoping for better news on the economic growth front. The economic data were, on the whole good enough to suggest that global growth might be stabilising after the softer trend seen in previous months. For example, in the US, although the key ISM indices for both the services and manufacturing sectors were a touch softer in November compared with October, they were enough to satisfy the markets for now. News from China that their services and manufacturing PMI's both rose in November suggested China is weathering the trade dispute better than expected, while in Europe there were some modest signs of stabilisation in some key growth indicators.

The best news for the markets in December was that the US and China would sign the so-called "Phase One" trade deal in January. The trade dispute between these two nations has been a major source of worry for the markets over the past year, with fears it could push the world into recession. News of the deal reassured investors and helped push equity markets, especially in the US, to new record highs. Emerging market equities outperformed strongly, given the positive impact of the deal not just on China directly, but also on the Asian trading nations so dependent on China and the US.

On the geo-political front, Boris Johnson resoundingly won the UK general election, paving the way for passage of his delayed Brexit legislation. In the US, the Democrats moved to impeach Donald Trump, but the President sees it as an opportunity to embarrass the Democrats given that the Senate will not impeach him. In the Middle East, tensions with Iran continued as they provoked attacks against US personnel in Iraq.

Heading into 2020, the global environment of slow growth and low inflation looks set to continue for some time. This means interest rates will have to stay low as well, but the bulk of the rate cuts are just about done in most countries, and many equity markets have already priced both current and prospective cuts in coming months. The US is one country where there may be scope for some positive surprise on this front in 2020.

Without further P/E re-rating from lower interest rate cuts, which is what really drove equities higher in 2019, we need to see better earnings growth to push markets higher in 2020. Unfortunately, the global growth outlook does not look strong enough to deliver that result and it is hard to see equity markets having as good a year in 2020 as they did in 2019. Bond market returns will also be subdued and the A$/US$ will be expected to trade in a US$0.65-0.70 range. Geo-political developments may provide opportunities to hedge equity market risks with positions in gold.

From a portfolio management perspective, we will continue to carefully manage how much allocation to equity risk is appropriate given the underlying fundamentals and compared with other assets offering attractive risk adjusted returns and the ability to hedge equity market falls. This includes selected fixed income and infrastructure assets. Overall, diversification and pro-active portfolio management will be key in 2020.