Stonehouse Core Value Portfolio
Monthly Update - May 2018

May Performance Overview

The Stonehouse Core Value Portfolio (CVP) returned -0.39% in May, as volatility during the month and mixed performance from underlying holdings impacted returns.

Within the Portfolio's Australian Equity holdings, SGH ICE (+2.6%) outperformed the index whilst Allan Gray (-1.4%) underperformed. Our International Equity managers exposed to Asia and Emerging Markets were the largest detractors, as J O Hambro Asia ex-Japan (-4.0%), Blackrock Japan High Divided Yield ETF (-3.8%) and Northcape (-2.0%) detracted from returns along with diversified global managers Wingate Global Equity Income (-2.2%) and Platinum International (-1.3%). Lansdowne European Equity (+4.5%) had a strong month benefitting from their short positions. Old Mutual World Equity (+2.4%) and Lazard Global Small Caps (+2.2%) also contributed positively.

Alternatives managers produced mixed results, with Invesco (-0.5%), JP Morgan Global Macro (-0.7%), AQR Managed Futures (-4.6%) and Acadian Diversified Alpha (-1.8%) detracting from performance. Bennelong Long Short Equity however continues to be a standout performer and produced an impressive return (+4.0%). BlackRock Absolute Return was also up +0.6%. Within the Property and Infrastructure sector Cromwell Phoenix Property Securities climbed +2.4% and Resolution Global Property added +0.4%, but Lazard Global Infrastructure retreated-2.3% after last month's outstanding gain (+6.1%).

Fixed Income managers provided solid returns in May, with positive returns from CQS Credit Multi Asset Fund (+1.3%), Ardea Real Outcome (+0.5%) and Smarter Money Active Cash (+0.1%); T Rowe Dynamic Global Bond (-1.0%) was the only detractor in this sector.

Given the current market volatility and uncertainty around geo-political events we remain cautious within the Portfolio with increased Defensive allocations as well as elevated cash levels as we wait for better risk reward opportunities to present themselves.

Portfolio Summary

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Unit price	$ 1.1195

Asset class ranges & current allocations[1]	Range	Current exposure
Cash & Fixed Int.	15% – 60%	33.7%
Property	0% – 25%	4.4%
Equities	25% – 65%	43.6%
Alternatives	5% – 35%	17.8%

Top 10 investment holdings (ex cash)
1. Wingate Global Equity Income
2. Old Mutual World Equity
3. Northcape Emerging Markets
4. Macquarie True Index Aus Shares
5. Invesco GTR
6. T Rowe Dynamic Global Bond
7. Platinum International Class A
8. Payden and Rygel Global Income Opportunities
9. Ardea Inflation Plus

[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).

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Market Performance and Outlook

May saw stability for most of the month as geopolitical tensions in Asia receded and softer economic data, which indicated we will see three rather than four Fed hikes in 2018, painting a rosier outlook for equity investors. The end of May however did see a flare up in risk aversion, this time centred on political developments in Italy. Complications with anti-establishment parties' attempts to form a government saw investors sell down Italian debt and equities. With the yield on the 2-year Italian government bond jumping from under 0.50% on 28 May to over 2.80% a day later, the prospects of a 2011-style Euro crisis/ scare had investors gripped with panic. However, as the end of month drew near, investors saw the move as overdone. The events of those few days reinforce the investment committee's decision to remain vigilant, cautious and overweight defensive assets as the prospect of a Minsky moment remains a possibility.

Within Fixed Income, government bond yields retreated outside of peripheral Europe as softer economic data reduced the probability of four US Fed hikes in 2018 and the angst in Europe saw a flight to safety, with these two factors combining to drive up demand for US debt. The US and Australian 10-year government bond yields finished the month at 2.86% and 2.67%, falling from 2.95% and 2.77% at the end of April, respectively. Global Credit indices gained 0.4% (hedged to AUD).

The ASX200 Accumulation added +0.74% for the month, while the MSCI World (AUD Hedged) rose +1.3%, the S&P500 Index (USD) gained +2.4% and the MSCI Emerging Markets Index (AUD Hedged) finished the month -3.8% lower. With a risk-on sentiment returning to markets, the AUD gained against the major currencies.

Within Australia, the majority of the major market sectors registered gains alongside the ASX200 Index, with Health Care (+5.6%), and Consumer Discretionary (+5.1%) the stand out performers. Telecoms was the noticeable anomaly, falling -10.2% as Telstra sold off sharply to drag the sector significantly lower.

As we enter June 2018, markets are in a state of calm as concerns around geopolitical tensions and rising interest rates have eased. The US appears to be more constructive with regard to improving relations with China and North Korea, and this has been a positive for risk sentiment. Although trade and geopolitical risks remain a concern, including the Middle East and oil prices, there is a compelling argument suggesting that after the strong gains of 2017 and the sharp run up in January 2018, a continued period of consolidation in equity markets is required and to be expected. If this argument comes to fruition, we could see rotation within equity markets while the major indices make little or no significant gains. However, we believe further downside risks cannot yet be ruled out in an environment of tightening global liquidity. Under either scenario, we have confidence in our active managers to selectively allocate to those sectors that will outperform in the event of an equity market downturn.