Stonehouse Core Value Portfolio
Monthly Update - November 2016

November Performance Overview

The Stonehouse Core Value Portfolio (CVP) had a challenging month in November with a return of -0.29%. The Investment Committee took a cautious approach and adopted a defensive positioning as we entered a period of heightened political risk due to the imminent US presidential election and Italian referendum on Senate reform; however, the Portfolio's allocation has since been rewarded with a strong bounce back at the time of writing.

Whilst Equity markets have reacted positively to the expected economic impact of President-elect Trump's proposed policies in 2017 and beyond, the Investment Committee believes this leap of faith is premature. In particular, it does not seem to consider the high starting valuation levels for developed market equities and the "de-rating" effect that may come from higher bond rates if growth and inflation do indeed accelerate as expected. Equally, there is no apparent consideration of the impact of other policies such as increased trade protection and a more uncertain geopolitical outlook in the "multi-polar" world President-elect Trump seems to support.

Whilst being cautious, the Investment Committee has used market volatility through the US Election period to increase exposure to attractively valued equity markets such as Japan and has tactically shifted allocations to active managers where we expect outperformance over their relative indices – this reflects our bias toward quality over passive benchmark allocations. Alternative exposures have shown mixed performance over the shorter term however our analysis of both market conditions and underlying strategies suggests improving conditions going forward.

Equity Managers predominantly contributed for the month with Blackrock iShares MSCI Japan* +6.7%, Lansdowne European Equity* +6.2%, Lazard Global Small Caps +6.1%, Wingate Global Equity Income +5.8% and Henderson Global Natural Resources +5.20% being the standout positive contributors. Emerging Market and Australian Small Caps remain preferred allocations from a valuation perspective, but detracted over the month with SGH ICE -4.4%, Northcape Emerging Markets -3.7% and LHC Australian High Conviction -1.8%.

Portfolio Summary

	Stonehouse Core Value Portfolio
Unit price	$1.0419

Asset class ranges & current allocations[2]	Range	Current exposure
Cash & Fixed Int.	15% – 60%	32.6%
Property	0% – 25%	4.0%
Equities	25% – 65%	42.6%
Alternatives	5% – 35%	18.4%

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

[1] In local currency terms.
[2] 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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November Performance Overview (continued)

Alternatives exposures which are held to lower volatility and provide diversification have been the key detractor for the month. Equity and Fixed Income Market Insurance detracted -0.27% from the Portfolio's total return for the month. The diversifying, trend following exposure to AQR Managed Futures detracted -7.5% and has struggled in choppy market conditions over recent months; however analysis of AQR's past performance highlighted that subsequent to its previous two largest drawdowns, the strategy delivered six month returns of 23.7% and 20.47% respectively. Bennelong, a quality Australian market neutral manager, has also struggled in the current challenging market dynamics returning -2.3% for the month. Yet analysis of its performance subsequent to its previous two largest drawdowns showed that the strategy delivered six month returns of 21.9% and 12.28% respectively. JP Morgan Global Macro -3.2%, Invesco -1.6% and Blackrock -0.9% also detracted from returns but for reasons well understood during a period of almost inexplicable euphoria. The Investment Committee's ongoing review of these strategies highlight that while performance has been disappointing, on a forward-looking basis market conditions are likely to be conducive to their outperformance, particularly under more challenging Equity Market conditions.

Property and Infrastructure Holdings contributed to returns after a poor recent run – SGH Property Income +0.6%, Cromwell Phoenix +0.5% and Lazard Global Infrastructure +0.4%.

Fixed Income managers were flat which was a pleasing result in the context of a material sell-off in Fixed Income Markets.

Market Performance and Outlook

US markets have taken centre stage again since Donald Trump took the world by surprise on election day, defying polls, pundits and much of the political press to secure the US presidency. Almost as surprising was the breaking of the political stalemate as Republicans kept control of both houses of Congress. Whilst US Equity Futures and Asian Equities responded to the political bombshell with a sharp 5% drop, markets dramatically reversed course focusing on expectations of pro-growth fiscal policy with the key US market subsequently reaching new found highs. Outcomes outside the US have been more mixed with Australian, European and Japanese equities rising but still well below their prior peak levels.

In spite of an overall Equity market rise, there have been clear winners and losers from the shock US Election result. Sectors such as Healthcare and Financials have rallied with expected policy tailwinds going forward. Bond Markets will now have us believe that July was the long term peak in prices and low in yields. Emerging Markets were hit the hardest following Trump's election victory. The potential for Trump to remain consistent with his campaign rhetoric and pursue isolationist policies would clearly be a negative for global trade and developing economies. Combined with a stronger US dollar and potentially higher interest rates in the US, and Emerging Markets could well face continued headwinds going forward. Although a negative for Emerging Markets, the recent surge in the US dollar has weakened the Japanese Yen and therefore boosted Japanese Equities. An improving US economy and more hawkish Fed could see the US dollar move higher still and thereby provide a continuing catalyst for growth in Japanese Equities.

The European Central Bank (ECB) has just extended its latest QE program until the end of 2017. In Europe, the Italian referendum defeat was another blow to the EU as a whole and centrist-establishment politics as populism continues to surge. Thanks in part to the ECB, Equity markets have once again taken this momentous event in stride and even the Italian banks have been bid up in spite of all the issues that remain. Next year the market and the Eurozone face bigger tests in French, Dutch and German elections.

In Australia a disappointing miss on GDP has seen some economists raising the likelihood of a recession in 2017 – the first time in 25 years. The Australian Dollar has been under pressure but downside appears muted. This is likely due to the fact that the market is also pricing in hikes from the RBA, though not until 2018.

The Investment Committee continues to monitor market developments closely noting that post the 20 January 2017 inauguration of Trump greater insight into his policy direction will be revealed. While we remain cautious, the initial assessment of Trump's policies has favoured exposure to US Financials, Japanese Equities and reduced exposure to Emerging Markets whilst maintaining sufficient Alternative Exposures in the event market sentiment turns.

*In local currency terms.