Stonehouse Core Value Portfolio

Monthly Update – October 2019

October Performance Overview

The Stonehouse Core Value Portfolio (CVP) generated a return of +0.36% in October. Performance of equity markets was mixed, with the Australian equity market posting a small loss (-0.37%) and the MSCI World Equity Index posting a small gain (+0.41%).

Within the domestic equity component of the Portfolio the best performing strategy was the small cap exposure SGH ICE (+1.8%) as some normality in fundamentals returned to the small cap sector. This was followed by Firetrail Australian High Conviction (+0.3%) and IML Equity Income (+0.1%). The biggest detractor was Allan Gray Australian Equity (-2.9%) followed by the beta exposure held in Macquarie Australian Shares True Index (-0.4%).

The global equity exposures also provided mixed results. The best performing strategy was Northcape Emerging Markets (+1.9%) followed by Platinum International (+0.50%). The biggest detractor was Loomis Sayles Global Equity (-1.3%), followed by Talaria Global Equity (-0.5%) and Lazard Global Equity Franchise (-0.3%).

Within Alternatives, Bennelong Long Short Equity (+8.8%) had a stellar month, with returns spread across many pair trades and across all sectors as news continued to flow through to markets along with company AGMs. Partners Group Global Multi-Asset (+0.8%) also provided a positive return but GMO SGM Major Markets (-1.4%) detracted.

Property and infrastructure exposures performed well despite bond yields rising throughout the month. The best performing strategy was Lazard Global Listed Infrastructure (+1.6%), followed by Resolution Capital Global Property (+0.9%) and Cromwell Phoenix Property Securities (+0.8%). The only slight detractor was AMP Capital Core Infrastructure (-0.1%).

Performance of the fixed income exposures was mixed in October as bond yields continued to rise. The best performing strategies were Aquasia Enhanced Credit (+0.4%) and Alexander Fixed Income (+0.4%). Ardea Real Outcome (+0.3%) and Payden Global Income Opportunities (+0.2%) were also positive contributors. The biggest detractor was Franklin Templeton Australian Core Bond Plus (-0.6%), due to its duration exposure. CQS Credit Multi-Asset (-0.2%) also generated a small loss.

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Portfolio Summary

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Unit Price at 31 October 2019	$1.0933

Asset Class Ranges & Current Allocations [1]		Current Exposure
Cash & Fixed Interest	15% - 60%	37.9%
Property	0% - 25%	10.6%
Equities	25% - 65%	40.6%
Alternatives	5% - 35%	10.8%

[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.	Franklin Templeton Australian Core Bond
2.	Aquasia Enhanced Credit
3.	Northcape Emerging Markets
4.	IML Equity Income
5.	Macquarie Australian Shares True Index
6.	Talaria Global Equity
7.	Platinum International
8.	Alexander Fixed Income
9.	Lazard Global Equity Franchise
10.	Ardea Real Outcome

Market Performance and Outlook

After starting October on a cautious note, markets became a little more optimistic about global economic conditions as the month progressed. News that the US and China would sign the so-called "Phase 1" agreement in the trade dispute contributed to the markets' improved mood, as did the Federal Reserve cutting the cash rate by another 0.25%. The RBA also cut, bringing the Australian cash rate to a new record low of 0.75%. US equity markets reached new highs, but the Australian markets had a subdued month.

Emerging market equities performed well on the trade news and the US rate cut. These factors also helped our currency. The A$/US$ rose from around US$0.675 at the start of the month to US$0.693 at the close. Slightly better than expected local inflation data reduced expectations of further RBA rate cuts and helped support the A$ as well.

On the political front, Elizabeth Warren is moving up the field of contenders for the Democratic Presidential nomination as Joe Biden's momentum fades. The UK heads to the polls on December 12 after Parliament refused to pass Boris Johnson's Brexit deal. Political unrest continues in Hong Kong and is spreading in South America.

Although we have not been as bearish as the global recession story, our economic outlook does include soft growth, low inflation, and little further improvement in unemployment rates. Some key economic indicators we follow suggest increasing risks to key parts of the US economy, which, if realised, could seriously challenge the ability of the S&P500 to maintain its current elevated levels. This would then impact other equity markets, including ours.

Taken together, these circumstances imply lower expected returns on equities over the coming year, but with no reduction in expected equity market volatility. If anything, volatility could increase as we move closer to the US Presidential election, Brexit developments unfold and difficulties in Hong Kong and South America continue.

From a portfolio management perspective, this means we do not see equity risk being rewarded anywhere near as well in the coming year as it has been in the past year. It is prudent to pro-actively reduce equity market risk in the portfolios and re-allocate exposures to assets which offer better risk adjusted returns and the ability to hedge equity market falls if they happen. This includes selected fixed income and infrastructure. We will also introduce some exposure to gold to hedge both equity market and geo-political risks.