Stonehouse Core Value Portfolio
Monthly Update - September 2016

stonehouse

September Performance Overview

Over the month of September the Stonehouse Core Value Portfolio (CVP) had a pull back of -0.38% in a challenging month for Global Equity markets which saw a decline of -0.89%. The CVP ended up +1.23% for the July – September quarter.

Equity managers were mixed with Macquarie Australian True Index +0.52%, new entrant Australian long/short LHC Australian High Conviction +0.50%, Henderson Global Natural Resources +2.14% and JO Hambro[1] +2.19% delivering positive returns. International managers predominantly detracted with Wingate Global Equity -3.01%, iShares Global 100[1] -2.16%, iShares MSCI Japan High Dividend[1] -0.81% and Platinum International -0.47%.

Listed Infrastructure manager Lazard contributed +0.79% whilst listed Property holdings continued their poor recent performance with Cromwell -3.96% and SG Hiscock -2.78%. Note we remain heavily underweight in the Listed Property sector so these negative movements have not had a large material effect on the CVP.

Alternatives managers were also predominantly negative with 36 South Kohinoor[1] -4.67%, AQR Managed Futures -0.88%, Bennelong Long Short -1.06%, Acadian -0.85% and Invesco -0.21%, however Blackrock Absolute Return delivered a solid +1.23% for the month.

Fixed Income holdings, Ardea +0.15%, CQS +0.51%, Kapstream +0.22%, Payden +0.42% contributed to performance, with fixed income investments acting as a diversifier within the CVP's portfolio.

Although the CVP undertook no significant opportunist trading activity over the month, the Investment Committee remains vigilant and continues to monitor markets closely noting that a number of risk events are on the horizon. Risk and scenario analysis performed by the Investment Committee continue to highlight the CVP's resilience across a broad spectrum of scenarios.

Portfolio Summary

Stonehouse Core Value Portfolio	
Unit price	$1.0582

Asset class ranges & current allocations[2]	Range	Current exposure
Cash & Fixed Int.	15% – 60%	30.2%
Property	0% – 25%	4.1%
Equities	25% – 65%	40.8%
Alternatives	5% – 35%	19.1%

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

[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).

AFSL: 292 469

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Market Performance and Outlook

September saw a moderate injection of volatility into markets after a quiet North American summer period with the ASX 200 selling off more than -4% intra-month to then retrace losses to end fairly flat. Most equity markets have delivered solid returns over the September quarter, driven by the outperformance of more cyclical (pro-growth) sectors. With economic growth in the developed world still remaining subdued and political uncertainty increasingly becoming a focus for markets, increased volatility is likely to be a notable theme going into the final quarter of 2016.

As expected, the US Federal Reserve left rates on hold in September but left the door open for a move later in the year. Three members of the Fed voted to increase rates, evidence of the increasingly divided Fed. A sequence of weaker economic data out of the US in recent months has been enough to justify the Fed's overall cautious stance. Of greater significance, however, was the lowering of the projections for the trajectory of interest rates over the next few years. Focus in the US now shifts onto politics with the presidential election looming in November.

Japanese equity markets were initially buoyed by news that the Bank of Japan (BoJ) is to fine-tune its monetary stimulus programme, and a commitment to overshoot its 2% inflation target. The BoJ is attempting to steepen the yield curve by modifying its Japan government bond purchases and setting a target for the ten-year yield at zero. By allowing banks to borrow lower (shorter term) rates and lend out at a higher (longer term) rate, this steepening of the yield curve is an ambitious attempt to help boost bank profitability and increase inflation expectations. We continue to watch this development closely as its success is likely to provide further support to the Japanese equity market.

Despite a temporary rise in September, bond yields remain at very low levels with higher yielding assets continuing to receive a bid with expectations of interest rates rising slowly and longer term rates remaining at historically low levels. Central Bank officials continue to note the limits of monetary policy are being reached and that the growth baton must now be taken up by Fiscal Policy. On this note there is an increasing view emerging that a world of more active fiscal policy is forthcoming, in which finance ministers take greater charge of economic management. Even in Europe, the idea of deficit spending is becoming less taboo.

In a relative value context, Equities are still attractive when compared to low Government Bond yields and even High Yield Bonds. Overall, Equities still remain our largest risk allocation and we continue to hold Australia and Emerging Markets at a higher weight which indicates a pro-cyclical stance. In our view there may be further losses from the historically outperforming sectors like REITS and Infrastructure in a scenario where long term rates are allowed to rise to levels in 2013. In this scenario we prefer to hold Resources and Financials as these tend to perform well as the yield curve steepens, with a rise in inflation expectations part of this shift in sentiment. The Australian Dollar appears to have found a floor above 75c however as the US Fed hikes, the interest rate spread will close further and may put more pressure on the Aussie.