



REPORT TO THE UNIT HOLDERS IN THE ASPIRING FUND FOR THE
MONTH DECEMBER 2017

	Aspiring Fund	NZ50G	ALL Ords Accumulation Index (rebased in NZ\$)
<u>Short-term returns</u>			
Month	1.40%	2.58%	1.43%
Last 3 Months	5.22%	5.90%	9.63%
Last 12 Months	15.32%	22.04%	19.11%
Financial Year to Date	10.43%	16.69%	8.46%

Long-term* returns and volatility

Return (annualised)	11.18%	6.82%	3.11%
Return volatility (annualised)	8.65%	11.56%	16.37%

* since the introduction of the PIE Tax regime, 30 Sept 2007

Unit Price \$3.53

ASSET ALLOCATION (approximately):

New Zealand Equities	37.6%
Australian Equities	24.0%
International Equities	13.9%
Bonds	3.3%
Total Cash	21.2%
Short Equities	-1.5%

Net Asset Value of the Fund (approximately): 386.6m

Fund Performance



Global risk appetite continued at solid levels throughout December with continental Europe taking a breather while the rest of the world powered on. New Zealand and Australia both benefitted from this with market returns of 2.6 and 1.8% respectively. The Fund's return of 1.40% looks a bit lacklustre against such stellar numbers.

Our individual portfolios performed well with both NZ and Australia posting very solid gains and the International portfolio delivered a positive US\$ return but a -3% NZ\$ return. NZ dollar strength is nearly always a corollary or consequence of strong risk appetite and it cost the Fund about 0.7% in December with the 3.9% appreciation against the US\$ being particularly painful.

For the calendar year the Fund returned 15.3%. We are satisfied with this return given the defensive structure of the aggregate portfolio. If we can capture the majority of market returns with reduced exposure and volatility in an aging bull market we feel this is a good outcome for our fellow unit-holders.

December capped off a strong year for markets globally with the MSCI World Accumulation Index returning 22.4% for the year. As remarkable as this number is, the way in which it occurred is even more so. The MSCI World, the S&P 500 and the NZ50G all had 12 consecutive months of gains. This was a first for the S&P500, had not happened for the NZ market since at least the Fund's inception, and for the MSCI World Index was the first time in over 30 years!

Simply put, markets failed to recognise risk in any meaningful way for the entire year. Given the world's geo-political state and the number of specific issues which arose and might, on historical precedents, have been expected to give pause for thought, at least, we can only interpret this as evidence of the overwhelming influence of the actions of global central banks on investor behaviour.

In New Zealand we are well removed from the worst effects of this but phenomena like 10 trillion dollars of sovereign debt trading at negative yields and Portuguese and Italian 10 year bonds trading over 0.5% lower in yield than US 10 years are not a consequence of rational investor behaviour- unless the rational private sector investor is aware of a market participant with a different agenda.

We have commented, at length, in previous newsletters so we won't subject you to much more on this but we are too old to embrace the concepts of perpetual central bank omniscience and omnipotence

and will continue to invest on the basis that their risk suppression will not translate to risk elimination despite their success over the last 8 years.

In fact, we are certain that their actions will result in new risks arising from the unintended consequences of their actions. Growing social discord as a result of rising wealth inequality and significantly underfunded pension schemes, whose actuarial assumptions can never be realised in a world of negative interest rates, are two immediately obvious issues.

Our international portfolio had a slightly unusual month. It finished up about 1% in USD terms but most of the tech stocks we own sold off in the immediate aftermath of the US tax cuts before recovering in to month end. We did not understand the immediate reaction, which was at odds with the broader market, and note that our stocks have continued to strengthen in the early days of January. While we believe these businesses deserve their premium rating they had stellar years in 2017 and the valuation support they enjoyed when we bought them is less obvious now. Against a backdrop of a record 17.5+ multiple for the New Zealand market we expect to add to and diversify our international portfolio in 2018.

The best performer from our NZ portfolio was Scales (25%) after it updated the market on earnings which they now expect to be at the top end of its recent guidance range, despite challenging growing conditions. Scales has been a good story for the past couple of years with its share price doubling, driven by increasing offshore demand for its apples and effective diversification of the business- and multiple expansion, of course. Other key contributors to fund performance were Chorus (6%), Heartland Bank (4%), EBOS (6%) and Xero.

By the middle of the month Xero's share price had fallen 19% from November's highs. Rod Drury runs a brilliant software company but we believe he was poorly advised when his board decided to abandon the New Zealand market. Xero is a large cap stock by NZ standards which means it was widely held by passive funds who had no choice but to sell when it exited the index. With no countervailing demand from passive funds (0.22% of the ASX300 doesn't count for much) the volume of selling from passive funds was always going to be difficult for the market to absorb. In the long run, the board's decision makes no difference to value and we took advantage of this weakness to build a position mid- month, which we were able to trim within a week at an 8% gain.

EBOS has been a core holding for many years and we were extremely disappointed to hear of Patrick Davies' resignation as MD in December. We believe EBOS is one of the best managed companies in the market and Patrick has been a significant contributor to this. However, his replacement, John Cullity, has also been a key member of the senior management team for many years and we expect the transition to be as seamless for the market as the Simon Challies/ Gordon MacLeod handover at Ryman. We will miss our regular sessions with Patrick- they were always interesting and illuminating- but wish him all the best for the future.

We also trimmed our Contact Energy holding following strong 2017 gains (~25% including dividends) after the media pre-announced that the new Government will be reviewing NZ power companies. Contact has been one of our key holdings for some time, but required more patience than we anticipated as the market took a while to appreciate the significant dividend growth ahead of it. We have been reducing our exposure to the sector for some time and the introduction of new political risk is likely to see this continue.

Our well-diversified Aussie portfolio had another particularly strong month with the bulk of holdings generating positive returns, however it was our resource sector holdings that shone most brightly. Aussie has largely been a 2 speed market this year, characterised by a relatively weaker industrials sector, and a cranking resources sector. The Aussie industrials returned a little over 9% for the year in comparison to the +30% return of Aussie resources as commodity prices recovered. The February reporting season should show strong cash-flows from the resource sector, with the potential for capital management and analyst upgrades should the commodity prices at least hold their ground – arguably current share prices are anticipating such moves.

We expect the significant amount of takeover activity in 2017 to continue into 2018. December was a particularly strong month with bids for Westfield and Aconex announced in Aussie, Trilogy in NZ, and

Disney's mega bid for Fox in the US. We hope to see the listing of Vodafone NZ in 2018, which would partially compensate for the flow of NZ companies exiting our market, but we do expect more to follow Trilogy in 2018. Below our top 10 holdings are quite a few mid to small cap stocks where we assess a non-trivial chance of corporate activity.

TOP 10 HOLDINGS

Google	2.9%
Precinct Convertible Notes	2.6%
Chorus	2.3%
Heartland	2.2%
Metlifecare	2.2%
EBOS	2.1%
Amazon	2.1%
Woodside	1.9%
Sanford	1.9%
Contact	1.8%

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