

REPORT TO THE UNIT HOLDERS IN THE ASPIRING FUND FOR THE  
MONTH JUNE 2018

	Aspiring Fund	NZ50G	ALL Ords Accumulation Index (rebased in NZ\$)
<u>Short-term returns</u>			
Month	1.72%	3.28%	4.18%
Last 3 Months	7.11%	7.50%	10.88%
Last 12 Months	13.22%	17.50%	18.47%
Financial Year to Date	7.11%	7.50%	10.88%

Long-term\* returns and volatility

Return (annualised)	10.98%	7.12%	3.27%
Return volatility (annualised)	8.59%	11.35%	16.17%

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

Unit Price \$3.65

**ASSET ALLOCATION (approximately):**

New Zealand Equities	35.2%
Australian Equities	22.7%
International Equities	18.9%
Bonds	2.6%
Total Cash	20.5%
Short Equities	-0.1%

**Net Asset Value of the Fund (approximately):** 409.3m

# Fund Performance



The Fund returned 1.72% in June, assisted by good performance from our Australian portfolio, and currency gains as the NZ\$ fell on deteriorating economic indicators.

The NZ top-50 equities index was up 3.3%, with around half the return attributed to two large index weight stocks (Fisher and Paykel Healthcare and Ryman). This continued what we see as the main story of 2018 – strong index performance driven by a small number of stocks, masking the lower return of the majority of the market.

The table below illustrates this, showing local currency total returns (including dividends) for the first half of 2018 for the three equities markets in which the Fund principally invests. The portfolio returns are all calculated on a market cap weighted basis.

	Total return CY18 (30-June)	NZ50 return contribution		Total return CY18 (30-June)	S&P500 return contribution		Total return CY18 (30-June)	ASX200 return contribution
Synlait	59%	0.4%	Netflix	104%	0.4%	Sirtex Medical	90%	0.1%
a2 Milk	42%	2.7%	Amazon	45%	0.9%	Altium	71%	0.1%
Summerset	40%	0.5%	Adobe	39%	0.2%	Nine	65%	0.0%
Kathmandu	21%	0.1%	Mastercard	30%	0.2%	Flight Centre	45%	0.1%
Ryman	14%	0.8%	NVIDIA	23%	0.1%	Reliance Wld	43%	0.0%
Tourism Hldgs	12%	0.1%	Visa	17%	0.1%	a2 Milk	43%	0.1%
Mainfreight	11%	0.3%	Microsoft	16%	0.5%	Beach Energy	42%	0.1%
Meridan	9%	0.4%	Facebook	10%	0.2%	CSL	37%	1.5%
Restaurant Bds	9%	0.1%	Apple	10%	0.4%	Seven West	37%	0.0%
Contact Energy	8%	0.3%	Google	7%	0.2%	Evolution Mng	34%	0.1%
Portfolio of top-10 returners	21%	5.7%	Portfolio of top-10 returners	20%	3.2%	Portfolio of top-10 returners	40%	2.0%
<b>Remaining 40 stocks</b>	<b>1%</b>	<b>0.7%</b>	<b>Remaining 490 stocks</b>	<b>-1%</b>	<b>-0.6%</b>	<b>Remaining 190 stocks</b>	<b>2.4%</b>	<b>2.3%</b>
NZ50	6.5%	6.5%	S&P500	2.7%	2.7%	ASX200	4.3%	4.3%

The NZ50 was up a highly respectable 6.5% over this six month period. However, as the table demonstrates 87% of this index return was achieved from the top-10 returning companies (and 67% from just 2 milk companies and 2 retirement village developers!). A portfolio of the top-10 returners delivered a +21% return, while a more diversified portfolio of the remaining 40 stocks returned a meagre 1%. Note that this return includes dividends so capital returns from these 40 stocks were negative.

The top-10 returning stocks of the massive US S&P top-500 company index, returned +20% and contributed ~120% of the total index return. A portfolio holding the remaining 490 stocks returned -1% (USD).

In Australia, the top 10 returners provided +40% (contributing 2% of the index's 4.3% return). The remaining 190 stocks gave a total return of 2.4%, or zero capital return after allowing for dividends.

The underlying broad-based low returns mentioned above are consistent with the wider MSCI World Equities Index, which at the time of writing has barely moved, up 0.8% calendar year to date. In our view this reflects a challenging valuation environment following strong market returns in 2017, elevated geo-political uncertainty, and ongoing concern around how a highly indebted global economy transitions out of a period of ultra-accommodative monetary policy.

While the Fund does not hold a position in Fletcher Building we think it is worth a comment on their June investor day. The company has an ambitious target of doubling earnings from their beleaguered Australian businesses, but what we have inferred from their presentation is an outlook for benign growth in NZ. A slowdown in the contribution to economic growth from the building and construction sector is an unwelcome potential headwind, as other recent macro drivers also appear to be fading.

Population growth from migration continues to decline, with a net gain of 2,322 in May, the lowest monthly change for four years. Auckland house price momentum has stalled and auction clearance rates continue to be poor (~35% of auctions since January achieving a sale under the hammer, vs ~40% with no bids). Together with continuation of policy surprises from the new Government and concerns around cost inflation, business confidence unsurprisingly hit a seven year low in June.

Our New Zealand portfolio had a good month in absolute terms but lagged the New Zealand market by a wide margin. Three stocks, Fisher and Paykel Healthcare, Ryman and a2 Milk, have a collective 23.5% weighting in the NZ50 and accounted for ~55% of the index's 3.28% return. Our exposure to this group is a 1.7% weighting in a2 Milk. We have no issue with the quality of business or management in Healthcare and Ryman but we believe both have become seriously over-valued.

Our portfolio is far more diversified than the NZ50 and its performance was driven by a large number of stocks delivering positive returns and a much smaller number delivering negative returns of which Heartland Bank was the worst with a -5.5% return for the month.

The ASX200 had a strong month being up just over 3% in A\$ as a result of broad-based strength, with resources and industrials +3%, and financials (+4%) finally catching a bid as news quietened out of the Royal Banking Commission. Outside of the large caps there were many extreme performances in stocks such as Appen (+31% - high growth favourite) and Gateway (+29% after 3 takeover offers).

Our Australian portfolio did slightly better than the market, however did not catch any of the extreme winners or losers, some of which we have held in the past. Our biggest contributors came from a wide range of industries including NRW Holdings (Mining services), Woolworths (Retail), Nanosonics (Healthcare), Websters (Agriculture), Cleanaway (Waste) and Woodside (Oil and Gas). While it felt unusual that so many sectors could perform in concert, we suspect Australia and New Zealand collectively benefited from inward flows as the US/China tariff spat took another step up. In all cases we banked some profits in these stocks over the month.

The International portfolio was flat for the month but it certainly wasn't as quiet as that return would suggest. In the first two weeks, the basket of stocks we own was up 6% before a reversal was triggered by the Tweet in the White House. A number of companies in Asia are now approaching cheap valuations compared to their western counterparts, with strong forward growth profiles. Many are not

directly affected by trade tariffs but have been sold down in sympathy with those that are. We are keeping an eye on opportunities in this market (from our current ~2% allocation) but will tread cautiously.

Amazon paid \$1 billion for a small online pharmacy company called PillPack, wiping out \$14 billion from the market cap of the pharmacy sector in the US. This highlights the fear and expectation that Amazon's slim margin offering will affect the whole sector in due course. When this fear is realised or even whether it is, may mean some of these companies' share prices may recover, as we saw following Amazon's entry into the supermarket sector. The key risk for incumbent firms is Amazon continuing to rollout new lines of business at marginal returns so they become the dominant provider of products delivered to the home.

July is normally a fairly quiet month as companies are in a black out period before they report to the market and the northern hemisphere takes their summer holidays, however there is no sign of the global trade noise fading anytime soon.

Our investment strategy remains unchanged and conservatively set for what we view as difficult market conditions. We have been lightening our exposure to NZ equities for some time in anticipation of wider appreciation of the unwelcome cocktail of record NZ equities valuations and slowing growth. At this stage we feel a little like the boy who cried wolf or the economist who predicted 12 of the last 3 recessions but we will not change course unless the facts change.

Even the yield stocks in New Zealand warrant careful scrutiny as government policy changes raise the prospect of stagflation necessitating interest rate increases faster than the RBNZ currently expects.

We are more comfortable with the higher liquidity and better priced risk available in offshore equities markets but, in the absence of compelling low risk ideas, cash remains our favoured way to de-risk the Fund.

## TOP 10 HOLDINGS

Mercury	3.3%
Amazon	3.1%
Precinct Convertible Notes	2.4%
Metlifecare	2.3%
Google	2.0%
Apple	2.0%
Visa	1.9%
EBOS	1.9%
Contact	1.9%
Spark	1.8%

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