

NTA and Monthly Update – May 2017

Company at a Glance

ASX Code	ALF
Fund Size	AU\$344.3m
Fund Strategy	Variable Beta
Share Price	\$1.24
Shares on Issue	272.5m
Dividend (HY17 Interim)	4 cents
Dividend Yield (annualised)	7.0%

Net Tangible Asset (NTA) Backing

	Apr 17	May 17
NTA Before Tax	\$1.26	\$1.27
NTA After Tax	\$1.27	\$1.28

Gross Portfolio Structure

Long Exposure	122.3%	119.9%
Short Exposure	-116.5%	-121.4%
Gross Exposure	238.8%	241.3%
Cash	94.2%	101.5%

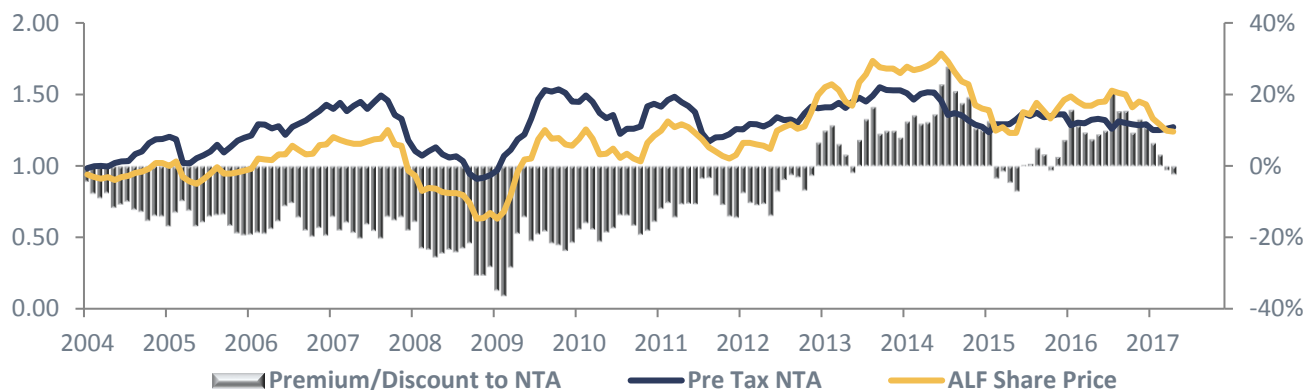
ALF Performance

	1 Mth	6 Mths	1 Yr	3 Yrs (pa)	5 Yrs (pa)	7 yrs (pa)	S.I. (pa)
Portfolio Return (net)	0.7%	1.0%	3.6%	3.4%	12.6%	11.2%	13.1%
All Ords Accum Index	-2.6%	6.9%	10.2%	6.2%	11.6%	8.4%	8.8%
Outperformance (net)	3.3%	-5.9%	-6.6%	-2.8%	1.0%	2.8%	4.3%

Net Equity Exposure



Premium/Discount to NTA History



Month in Review

The Australian share market significantly underperformed global peers in May, posting its largest fall since January 2016. Weakness in the domestic market was concentrated in the banking sector which is facing a myriad of challenges. Consumer confidence was also lower, reflecting growing concerns from households over levels of indebtedness and record low wage growth. Heat continues to come out of the housing sectors, as macroprudential controls and rising interest rates curtail demand from investors.

Global markets continue to show resilience in the face of a range of geopolitical issues creating potential uncertainty for investors. Notwithstanding this resilience, investors remain skittish that recent momentum in the global economy could be derailed, as evidenced by the dramatic (but short-lived) spike in volatility during the month as markets digested the looming prospect of a Trump impeachment. While strong results from US and European companies through their respective reporting seasons were encouraging, this will undoubtedly provide further cover for central banks to push ahead with tightening measures, providing further tests for markets in the months ahead.

The Fund performed well relative to the weak domestic market, delivering a net return of 0.7% as compared with the benchmark All Ordinaries Accumulation Index which fell by 2.6%. While the fund has no net exposure to the share market, we have been short the domestic shares while retaining a long exposure offshore. This worked well, with both parts of the portfolio making solid contributions. The strongest performance came from the mining, financials, and information technology sectors, while positions in healthcare and consumer weighed on performance.

May was another strong month for global consumer staples shares while Australian domiciled staples companies finished the month slightly down. The more economically sensitive consumer discretionary shares were largely flat in both global and domestic markets. New positions were established in US companies Walgreens Boots Alliance (pharmacies) and O'Reilly Automotive (aftermarket parts). Domestic gaming companies Tabcorp and SkyCity were both trimmed following strong performance while our JB Hi-Fi position was sold as it appears increasingly likely that the Australian housing cycle is appreciably slowing.

Consumer positions detracted from performance, particularly an investment in Super Retail Group which is facing concerns around the impending arrival of Amazon in Australia and a weaker domestic consumer environment that is impacting trading across the company's various retail banners. A short position in electronics retailer Best Buy also detracted from returns in the international portfolio, with improvement in video game console and mobile phone sales more than offsetting our thesis around declining profitability from high definition TVs. A core investment in Heineken continues to perform well.

Technology shares continued to perform strongly in the month. Internet names recovered sharply after concerns eased around brand safety and measurability (YouTube video ads being displayed among extremist content). Similarly, semiconductor shares struggled for the first few weeks of May as US auto sales (one of the larger end markets) showed signs of weakness and Chinese smartphone shipments continued to slow, before recovering these losses rapidly. The European telco sector, which has struggled with regulatory pressures and anaemic growth for many years now, surged 10% in the month as opportunities for consolidation in some key markets again took centre stage. US media shares had a rocky month as the cable providers' results demonstrated a clear acceleration in cord-cutting, while broadcast networks across the US and Europe guided towards a weaker ad market.

Performance in this sector was solid. A bidding war erupted for a core holding in Fairfax Media, while positions in French telcos benefitted from the market-wide uplift following the French election. Nokia and Intuit also reported strong results. Conversely, negative contributions came from an investment in Vocus Group, which downgraded guidance yet again, and a short position in Autodesk which reported better than expected subscription growth.

A decelerating Chinese economy is weighing on demand for commodities, leading to further softening in the prices of bulk commodities and base metals. We are short the mining sector on the basis that this trend will continue through the second half of 2017. We took profits on an investment in Iluka Resources, which bucked the negative trend in the month, rallying with the price of Zircon.

We re-established an investment in James Hardie Industries, following a difficult 12 months for the company as it grappled with plant execution issues. We believe these issues have been addressed and the de-rating of the shares has provided an attractive entry-point for an investment in a strong growth company. The oil price rallied in anticipation of an extended OPEC agreement, only to fall sharply once the agreement was announced. US shale continues to provide a swing factor for oil supply, with increases in production whenever the oil price rallies. We are neutral in the energy sector as a result.

Shares of global pharma companies found some support in May as rhetoric around drug pricing softened in the US. European pharma companies continued to rally with the broader market and are playing catch-up with US peers. Core investments in Merck and Roche were positive contributors. We remain concerned that drug pricing pressures are a structural headwind for global pharma companies and that the worst is yet to come, particularly as Pharmacy Benefit Managers have come under scrutiny around drug rebating practices. Specialty and generic pharmaceuticals were notable underperformers with several large players reporting double digit declines in the prices of generic drugs. Aggregation of distributors and pharmacy chains in the US has exacerbated these pricing pressures, weighing heavily on the shares of Mayne Pharmaceuticals; a detractor from performance in the month. In our view, the sector needs to see increased M&A, accelerated generic drug approvals from the FDA and reduced pricing pressure to justify a re-rating. While some of these factors are beginning to appear, it remains early days.

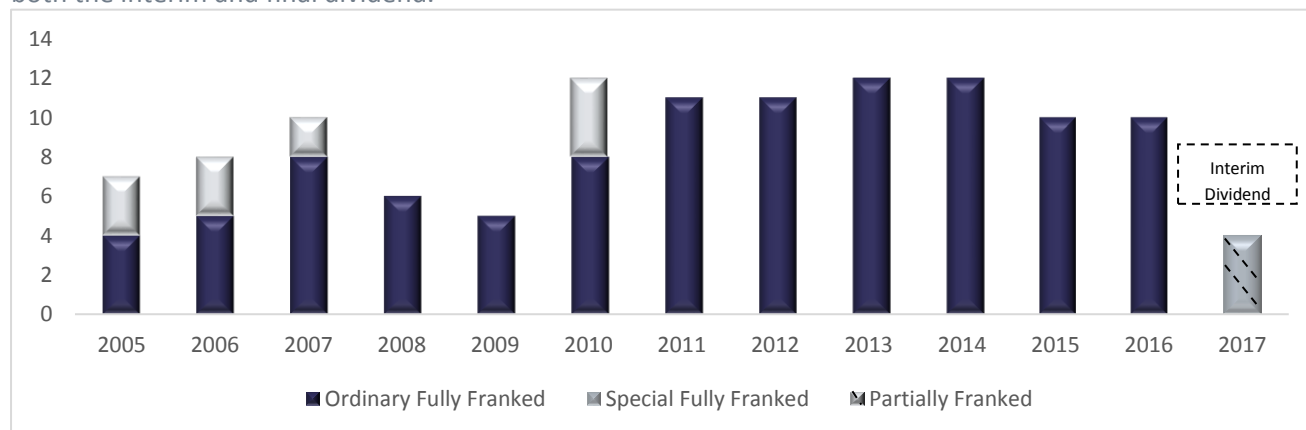
A sharp pullback in NEVRO shares provided an attractive buying opportunity after a softer than expected quarterly result. We believe lower sales volumes were a temporary issue and are confident revenues will bounce back next quarter. Australian healthcare shares in many cases are trading near record-high valuations and are expensive relative to offshore peers. As result, we remain short the domestic sector, with better investment opportunities to be found offshore.

The brunt of domestic market falls in May were borne by the banks. Longstanding concerns around deteriorating credit quality and the Banks' prospects for future earnings growth were compounded by the announcement in the Federal Budget of the proposed banks levy. The Fund was well positioned to capitalise on the resulting weakness in the domestic banking sector. Shorts in Australian mortgage lenders and mortgage insurers also performed well. An investment in the newly merged Janus Henderson Group was a standout performer, with the improved size and liquidity of the merged entity making it investible to a broader range of institutional investors.

Following a series of meetings with US financial institutions, we initiated a new long position in consumer finance company Synchrony Financial, as we believe credit quality in the US will remain generally robust despite some deterioration in parts of auto and unsecured card lending.

Dividend History

The Board is committed to paying an increasing stream of fully franked dividends to shareholders, provided the Company has sufficient profit reserves and franking credits and it is within prudent business practices. Dividends are paid on a six-monthly basis and the dividend reinvestment plan is available to shareholders for both the interim and final dividend.



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