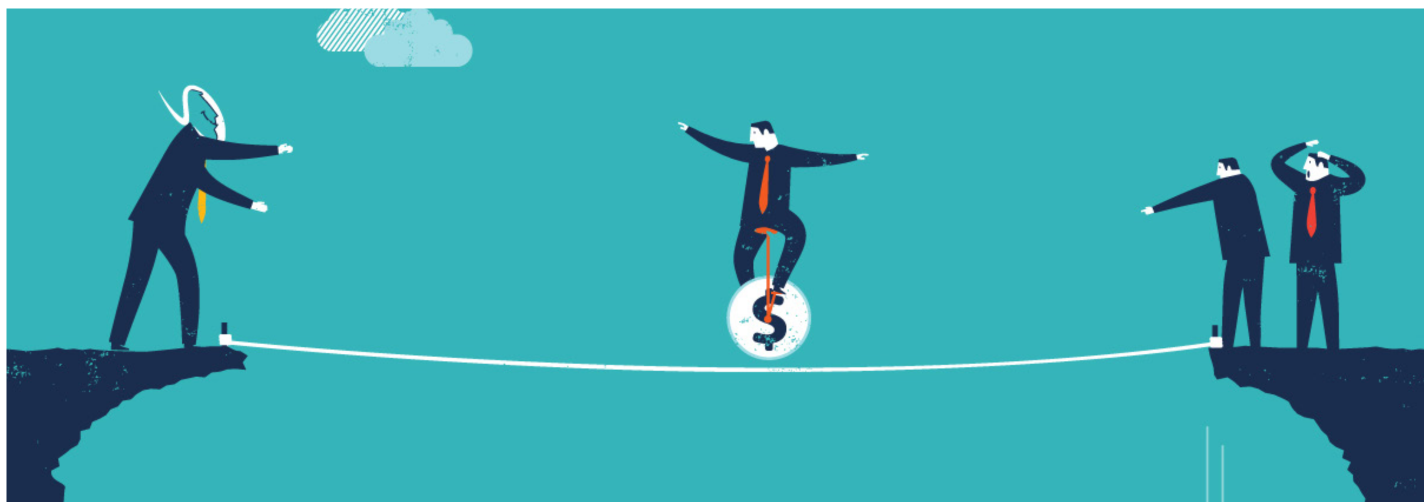
Affluence INVESTMENT FUND

INVEST DIFFERENTLY

Investment Report - March 2015



Fund vs Benchmark

To 31 March 2015	1 Month	3 Months	1 Year	Inception*
Affluence Investment Fund	1.0%	1.7%	N/A	9.4%
Benchmark - Inflation + 5%	0.6%	1.9%	N/A	7.6%
Outperformance	0.4%	(0.2%)	N/A	1.8%

Market Commentary

In Australia, the ASX300 stock market index rose strongly, up 10% for the quarter. The increase was driven mostly by the Reserve Bank of Australia somewhat unexpectedly (and we believe reluctantly) cutting the cash rate in February to just 2.25%. This was the first cut in 18 months and drove the latest instalment of the "search for yield" brigade to buy stocks once again. Predictably, banks, utilities and retailers were outperformers, while resources stocks once again lagged.

International stocks again performed relatively well for the quarter, (as measured by the MSCI World ex Australia Accumulation index) up 5.2%. This return increased to 9.5% for investments that were not currency hedged, benefiting from the Australian dollar's continued fall against the US dollar. The AUD ended the quarter at 76 cents per USD, down from 82 cents at the end of December.

Property continued to do well, with listed A-REIT's up 9.2% for the quarter and unlisted property also performing well. Residential property continued to be in demand, with the RBA rate cut fuelling another round of the debt-funded buyer frenzy we have become used to.

Unemployment in Australia reached 6.3% for the quarter, extending the trend of slow increases in the number of unemployed, as a sputtering economy fails to make up for the continuing slowdown of the mining sector.

Bonds continued to offer substandard returns, except for those who are prepared to take bets that the interest rate trend will continue to be downwards and acquired long-terms bonds with fixed yields. Australian Government 10 year bonds were offering a yield of just 2.32% at the end of March, reflecting both a dismal market view of the potential for economic recovery, and the prevalence of even lower rates in most other developed economies.

Fund Performance

The Fund commenced investing on 1 December 2014. Initial investments were made into the Cromwell Direct Property Fund, Cromwell Australian Property Fund and the Phoenix Opportunities Fund. We currently have around 86% of the Fund's capital employed.

The Fund's investments at 31 March 2015 were allocated 26% to Australian equities, 60% to listed and unlisted property and 14% in cash. However because a number of the funds we invest with are themselves carrying significant amounts of cash, the underlying cash exposure is approximately 43%. This reflects our philosophy of achieving reasonable returns with limited downside exposure and means the impact of any market correction on our portfolio should be less severe than, say, a portfolio constructed only of listed stocks.

The portfolio increased in value by 1.7% during the March quarter, net of all fees and costs. Performance to date is equivalent to a 9.4% annualised return, well ahead of our target returns of 7.6%.

All investments contributed positively to performance. The Direct Property Fund saw increases in the value of a key asset, the Australian Property Fund benefitted from continuing increases in listed A-REIT values and the Phoenix Opportunities Fund lagged the market but still delivered a positive return for the quarter.

The Fund aims to be fully invested by the end of this year, holding 15-25 investments in Australia's best managed funds, providing a diversified exposure to various asset classes

We anticipate making additional investments during the September quarter, subject to market conditions. During 2015 we are aiming to expand the Fund holdings into some offshore equities, a broader range of Australian equities, selected fixed interest investments and one or two strategies designed to cushion the Fund in market corrections.

We are currently looking at well over 200 potential investment opportunities for the fund across all asset classes. Some we have been monitoring for a year or more – others we have more work to do on.

We will continue to methodically work through these potential investments and select only those which we feel are the absolute best for inclusion in the portfolio.

Energex House, Brisbane - An asset in which the Cromwell Direct Property Fund is invested in.

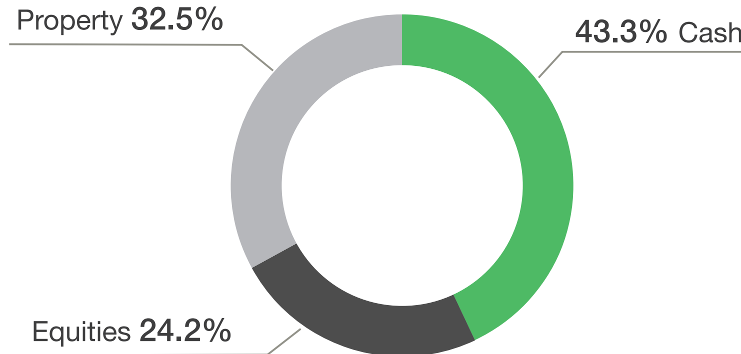
Fund Investments

Fund investments as at 31 March 2015.

Investment	Class	Portfolio %
Cash	Cash	14%
Cromwell Australian Property Fund	Listed Property	11%
Cromwell Direct Property Fund	Unlisted Property	49%
Phoenix Opportunities Fund	Equities	26%
		100%

Asset Allocation (underlying assets)

The Fund aims to be fully invested during 2015, holding 15-25 investments in Australia's best managed funds, providing a diversified exposure to various asset classes. The graph below analyses the underlying asets of each fund we invest in.



Key Fund Statistics

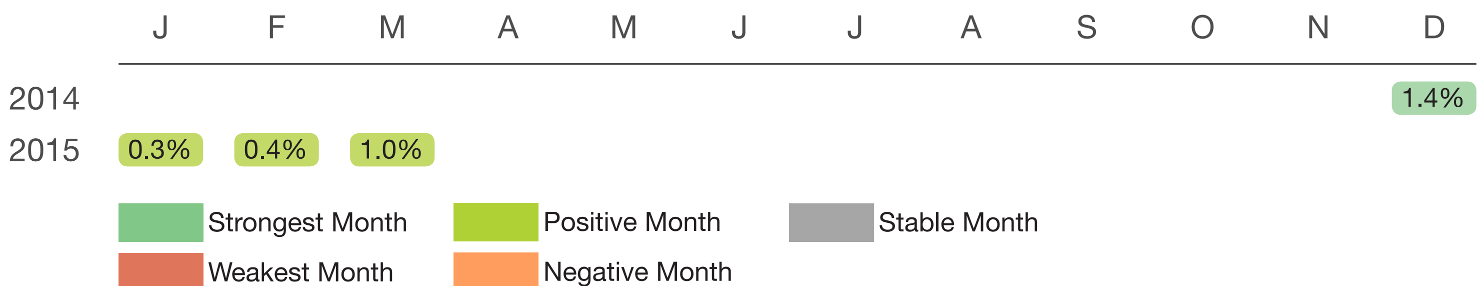
Status	Opening Soon[1]
Investment Class	Diversified fund-of-funds
Minimum Investment	$20,000[1]
Issue Price	$1.0329[1]
Withdrawal Price	$1.0312[1]
Annual Distributions	5.20 cpu
Distribution Yield	5.04% p.a.[2]
Distribution Frequency	Monthly
Target Returns	Inflation + 5%[3]

Applications	Monthly[4]
Withdrawals	Monthly[4]
Suggested Timeframe	At least 5 years
Distribution Reinvestment	Yes
Borrowing Policy	No borrowings in Fund
Fees	Performance based [5]
Buy/Sell Spread	0.20%/0.20%

1. The Fund is expected to be open to new investors during 2015
2. Annualised distribution divided by withdrawal price
3. The Fund targets a return of inflation plus 5% over rolling 3 year periods
4. The Fund is not currently open for investment
5. The performance fee is 12.5% of positive resturns. Costs in excess of 0.25% of net assets are borne by the manager.

Fund Returns

The Fund is structured in a way that aims to withstand volatile markets to create a smoother return flow. The heat map below shows the Fund's historic monthly returns and provides an indication of historic volatility. Past performance (returns and volatility) are not indicative of future performance.



	J	F	M	A	M	J	J	A	S	O	N	D
2014												1.4%
2015	0.3%	0.4%	1.0%									

Market Outlook

After a strong March quarter, it feels like the yield chase theme is getting towards an end – or at least a long breather.

Interest rate futures markets are currently expecting a further two interest rate cuts from the RBA which will take the cash rate to an unbelievable 1.75%. While that may well occur, it is hard to see much more, particularly in an environment when US rates, and potentially those in the UK as well, are expected to rise sooner rather than later. Without the stimulus of a greater number of cuts than the market expects, or upside surprises in economic indicators or company earnings, it would seem to be difficult for stock market and property prices to move much further upwards in the near term.

There is one potential beacon of hope for stock markets, and that comes in the form of the performance of resource stocks, which could well surprise on the upside. The mining environment is not getting better, but at least it does seem to be getting less bad. While it remains difficult to get excited about iron ore, many other commodities and energy stocks, and the companies that service them, could see some improvement from the current dismal outlooks priced in.

We do expect some volatility in stock markets this year, perhaps soon. It may well come in the form of a 10-15% market correction, particularly in the US market which has still to get through the psychologically important first interest rate rise. While there is plenty of historical evidence suggesting stock markets do not fall drastically when interest rates start to rise, we still expect a short term adjustment in the US as reality sets in and huge bets by hedge funds and other leveraged traders on a continuing market boom are unwound.

Such a correction would, in our view, be healthy at this point and it is hard to see our local market escape unscathed from such an event.

We will likely take this as an opportunity to add to our equity investments if indeed it does occur.

Bond Market Lunacy

"There was once a time, perhaps, when unprecedented things happened only occasionally. In today's financial markets, unprecedented things are commonplace. The Queen in Lewis Carroll's '[Alice] Through the Looking-Glass' would sometimes believe as many as six impossible things before breakfast. She is probably working in the bond markets now, where believing anything less than twelve impossible things before breakfast is for wimps."

Tim F Price, PFP Wealth Management

We read a lot of market information and commentary here at Affluence. Much of what is out there is mundane, boring even. Tim Price, luckily for us, is not and his regular articles normally also contain a hint of humor to help get us through the day. The quote above from Tim has rather succinctly summed up the current problem with Bond markets worldwide. The picture below, courtesy of ftalphaville and others, also perfectly explains the situation.

We are, to put it mildly, in interesting times. Bonds around the world are trading at never before seen yields in most cases. The only other time we have come

close, at the end of World War 2, was followed by an unbelievable spike in yields for the next 40 years. You have been warned! There are two important takeaways from the current situation.

Firstly, bonds such as US Treasuries (promises to pay issued by the US Government), are supposed to offer risk free returns, (although Bond guru Bill Gross and others in recent years have referred to them as delivering "return free risk"). The supposedly risk free characteristic of bonds means the price of every other traded investment on the planet is referenced back to yields on government bonds such as US Treasuries. In theory, an investment's return should be the sum of the required investor return due to an investments' specific risk characteristics, plus the risk free rate. Thus if the risk free rate today is 4% lower than it was 8 years ago, it therefore follows that every investment, at least in theory, should carry a total return 4% lower than it was 8 years ago. In many cases that is what has occurred. Certainly, for example for term deposits.

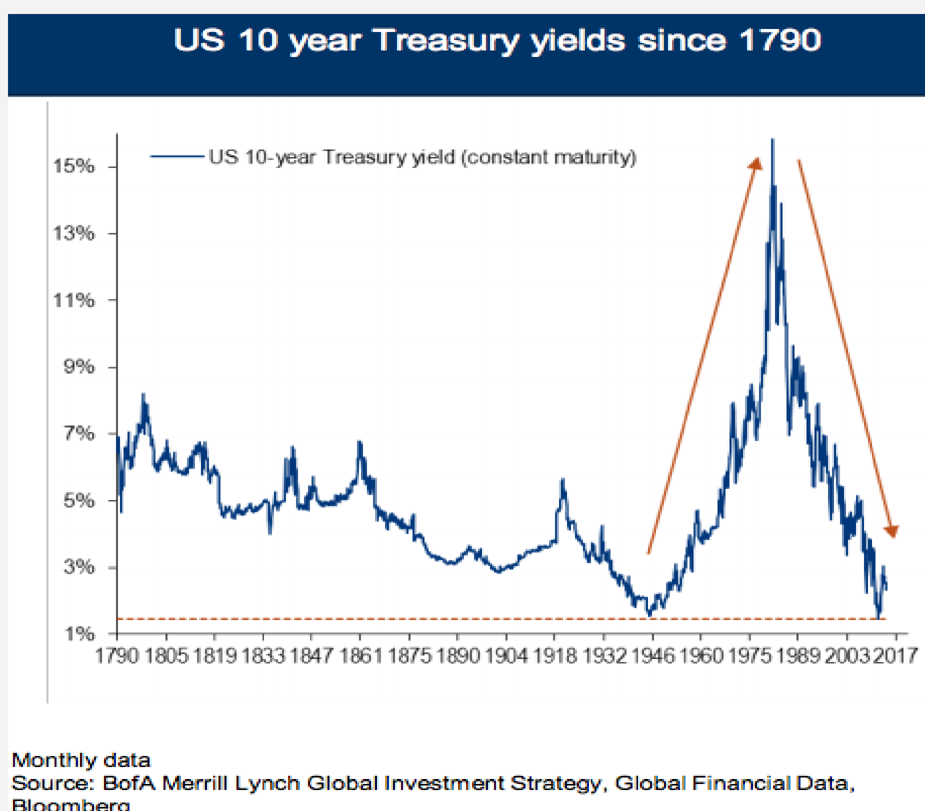
And that is why, in a nutshell, almost every investment on the planet is trading at a relatively high value. Not because world economies are going well. Not because profits are growing at a great pace. But because the key reference point, risk free bonds, are trading at (almost) never before seen low yields.

It is a huge global financial experiment that may well continue to go on for years. We have no idea how it will turn out, but it could end very badly. Regardless of the exact timing, we must recognise when evaluating any investment in this environment that there is a very good chance bond yields will be substantially higher in the next few years than they are now, and we must factor that risk into our assessment of value.

The second problem with most current bonds is, in our opinion, you would have to be quite mad to invest in them at todays yields. Income of less than 3%, locked in for years into the future is not attractive. You could argue that the trend for yields in the past 30 years has been down and therefore bond values can still go up if yields fall further. But that, to us, sounds like the greater fool theory at work. We do not like to own any investment that requires the continuation of an unhealthy trend to make a reasonable return.

The bond conundrum also gives rise to a related problem. How do you properly diversify your portfolio if the one thing that has been used successfully for the past 40 years to protect you against falling stock markets, is no longer an attractive proposition?

The answer is not an easy one, and investment professionals the world over are currently struggling with it. Our answer is to make sure we are a careful investor in stocks – via a few managers who are still able to find quality companies at reasonable prices in an overpriced market. Such stocks that should go down less than the market if it corrects. Combine this with some cash, some property and other assets which don't necessarily move together with stocks and maybe a little bit of portfolio insurance incase of a big correction, and you have a combination that should get us through pretty much anything. Which is good, because pretty much anything could come our way in this environment!



Contact Us

If you have any questions, please do not hesitate to contact us:

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Feedback

One of the things we value at Affluence is feedback from our members and investors. If you love what we're doing, let us know. Just as importantly, if you have a question or a suggestion of something we could do better, please tell us.

If you see an investment opportunity you think is exceptional, we would love to hear from you. Although remember - we are seeking the best fund managers and investors, so we don't usually invest in individual stocks. Also, we cannot give you any personal advice relating to your specific investments or specific circumstances.

You can call us anytime on 1300 233 583, provide feedback on the web directly at affluencefunds.com.au or e-mail me directly with your investment ideas or comments at daryl.wilson@affluencefunds.com.au. You can also connect with us on social media to get regular updates as we post them.

Risk Disclosure

The key risks of investing in the Fund are typical of the risks associated with managed investment schemes. It is important that you understand the value of your investment will go up and down over time, the Fund's returns will vary over time, future returns may differ from past returns, and returns are not guaranteed. All of this means that there is always the chance that you could lose money on your investment.

Affluence
FUNDS MANAGEMENT

Affluence Funds Management is the trustee and investment manager of the Fund.

Affluence is a boutique fund manager which specialises in providing high quality investment opportunities to a wide range of investors.

The Affluence business was formed to provide better investment solutions. Affluence's focus is on delivering superior long term investment performance. We believe in doing things differently, and we believe diversification is essential to any investment portfolio.

Affluence has a strong customer service focus. Investors can speak to our staff directly about their investments and information on performance and activities is communicated quarterly.

Additional Information on Affluence can be found on our website.

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