CI PENSIONS FUND
QUARTERLY REPORT

Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

MARCH 2016

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTH	-1.60%	-2.29%	0.69%
ROLLING 1 YEAR	-1.83%	-8.13%	6.30%
ROLLING 2 YEAR	8.92%	3.17%	5.75%
SINCE INCEPTION*	9.06%	3.31%	5.75%
SINCE INCEPTION^	19.78%	7.00%	12.78%

*Annualised
^Cumulative (3 March 2014)
**Before fees and expenses and adjusted for franking credits
#S&P ASX200 Accumulation Index – adjusted for franking credits

The purpose of the CI Pensions Fund is to provide a conservative equities portfolio that may be suitable for investors who are in the pensions/ decumulation phase. The portfolio may also be suitable for charities, foundations and others who are looking for a conservative equities exposure.

Whilst return is important the portfolio also aims to perform much better in down markets and to exhibit lower than market volatility.

Market and Portfolio Performance

The March quarter continued the extreme volatility we saw in 2015. The ASX200 Accum Index fell 5.5% in January, and then again fell 1.7% in February, only to recover 4.7% in March to leave the market down 2.7% for the quarter. However the main constituents of the index showed even greater variability, the Resources Index falling 9.5% in January but rose in February and March by 6.37% and 5.87% respectively. The Financials Index, of which the banks comprise a major part, was equally volatile, falling 7.4% and 6.2% and then recovering 5.6%.

While overseas stock markets were mixed, the majority of the international stocks in the portfolio are listed in the US and New Zealand and these markets showed gains. The Australian dollar was generally higher over the quarter, in particular against the US$ and the NZ$ and as a consequence the international stocks in the portfolio detracted from the portfolio's return.

Bond yields fell again as inflation expectations remained low and some central banks pushed cash rates further into negative territory.

The portfolio returned -1.60%% over the quarter and -1.83% over the year whilst the benchmark returned -2.29% and -8.13% respectively. Since the portfolio's inception date of 3 March 2014 the portfolio return has been 9.06% compared with the benchmark return of 3.31%.

There was a very wide dispersion of returns with better performing stocks including **Brambles (BXB), Recall (REC), TPG Telecom (TPM)** and the property and infrastructure holdings while poorer performing stocks included the banks and **Caltex (CTX)**.

At the end of the quarter the portfolio held 39 securities, 4 of the securities are US and UK listed and there was around 7% in cash.

The quarterly performance of the portfolio and the market is set out below.

Quarter Ended	CI Pensions Fund	ASX 200 Accum	Relative Performance
Mar-14	0.96%	0.52%	0.44%
Jun-14	1.35%	1.19%	0.16%
Sep-14	0.63%	-0.09%	0.72%
Dec-14	7.33%	3.40%	3.93%
Mar-15	10.41%	10.83%	-0.42%
Jun-15	-4.88%	-6.31%	1.43%
Sep-15	-0.50%	-6.03%	5.53%
Dec-15	5.41%	6.80%	-1.39%
Mar-16	-1.60%	-2.29%	0.69%

Note: Before fees and expenses and adjusted for franking credits

As discussed earlier in the report, the volatility of the Australian stock market has been rising and was particularly high during the March quarter. Since the portfolio commenced the volatility of the portfolio has been 70% of the market's volatility, during the March quarter the portfolio volatility dropped to around 64% of the market's volatility.

The portfolio has continued to perform better than the market on down days. In the last quarter the market fell on 30 days and the portfolio fell by less than the market on 29 of these days.

Since our Pensions strategy commenced on 3 March 2014 the market has been up on 53% of days and down on 47% of days. On the days where the market has risen, the portfolio has "captured" 70% of this upside. On the days when the market has fallen, the portfolio has captured 63% of the downside. The sum of these two occurrences is that the portfolio has outperformed the market since inception and has been much less volatile than the market.

The Portfolio

Over the quarter we added Ryman **Healthcare (RYM.NZ)** to the portfolio, reduced **Summerset (SUM.NZ)** by a little and sold the **Clydesdale (CYB)** shares that came into the portfolio as it demerged from NAB.

Ryman is the leading retirement/aged care business in New Zealand with a phenomenal track record of growth and shareholder returns. Ryman adds to the portfolio's exposure to the retirement/aged care industry which clearly has a tailwind from the increase of people aged over 75 in the next couple of decades. We reduced the Summerset exposure a little as it operates in similar markets in New Zealand.

National Australia Bank (NAB) finally achieved separation from its UK subsidiary Clydesdale Bank through a demerger. We sold the Clydesdale shares primarily because the bank does not have a strong track record nor is it planning to pay a dividend in the short term. We would classify Clydesdale as a turnaround stock and this portfolio does not look for exposure to turnarounds as they can be volatile and problematic.

Stock News

The portfolio owns three infrastructure stocks, **Transurban (TCL), Auckland Airport (AIA) and Sydney Airport (SYD).** These stocks have clearly benefitted from the lower interest rates and the continuing search by investors for yield and stability, however it is very comforting that their businesses are performing very strongly.

Transurban's revenue growth for the last reported quarter was around 17% ahead of the previous corresponding quarter, this growth came from a combination of toll price rises and increases in traffic. Transurban has a portfolio of projects and options that should lead to strong dividend growth over the medium term.

Passenger numbers at Auckland Airport are up around 8% on an annual basis and recent months have shown even stronger growth. Sydney airport had an increase in passengers of 4.3% on an annual basis with more recent months showing stronger growth especially for international passengers. Again we expect dividend growth over the medium term.

After one of the longest take-over negotiations in Australian history it looks as though Iron Mountain (IRM.US) will be successful in its take-over of **Recall (REC)** after the relevant competition authorities approved the transaction. The takeover is still subject to Recall shareholder approvals however that should be a formality. If approved Recall shareholders will receive a combination of Iron Mountain shares and a small amount of cash. Iron Mountain shares will be traded on the ASX from early May. We expect to continue to hold Iron Mountain in the portfolio.

Wesfarmers (WES) completed the acquisition of Homebase in the UK for $700m. The company's intention is to take the Bunnings concept to the UK. Wesfarmers looks likely to spend in the order of $2B to refurbish and restock the acquired store network. Wesfarmers are going to trial the new format in a small number of stores prior to rolling it out across the entire store network. We believe this is sensible and if done well will provide a useful growth opportunity.

The **ASX** had three pieces of important news over the quarter.

The first was disappointing in that the CEO, Mr Funke Kupper resigned due to controversy from his previous CEO role at Tabcorp. We feel that he made a very strong contribution to the ASX in his four and a half years in the role and his decision to resign avoids the ASX being embroiled in a controversial issue. Fortunately the ASX has a strong leadership team and the momentum in the business should continue while they search for a new CEO.

The second piece of news was that the Treasurer announced the Government's response to the review of equities clearing by the Council of Financial Regulators. The ASX is the sole clearer of equities trades in Australia and the Government said it is prepared to open clearing to competition, however it is also very clear that it wants to maintain a safe system with capital backing the domestic clearing system to be held in Australia. While this announcement puts some risk around revenue of one of the ASX businesses it is by no means certain that a competitor will emerge.

The third piece of news is that the Government will change the ownership restrictions on the ASX to be consistent with ownership restrictions of banks. Currently an Act of Parliament is needed before a shareholder can own more than 15% of the ASX, in future the Treasurer will have the power to approve a shareholder owning more than 15% of the ASX.

Caltex completed a discounted buy back of $270m of its shares to be undertaken in April. The majority of the buyback price was done through a fully franked dividend and as such is particularly attractive for tax payers with a zero tax rate such as those in pension phase and charities.

Retirement Incomes

During March we attended the Post Retirement Conference run by Conexus Financial in Sydney. The conference ran over two days with the first day involving large superannuation funds and the second day involving financial advisers. The main topics discussed were what portfolio strategies and products are appropriate for retirees and how advisers can help people who are approaching retirement or have retired.

The discussions were heavily influenced by the recommendations of the 2014 Financial System Inquiry (FSI) relating to superannuation and retirement incomes and the Government response to those recommendations.

In summary the FSI concluded that:

- superannuation assets are not being efficiently converted into retirement incomes;
- the clear objective for the superannuation system should be "to provide income in retirement to substitute or supplement the Age Pension";
- superannuation funds should provide a comprehensive income product for retirement (CIPR).

The Government broadly endorsed the recommendations on superannuation and retirement incomes.

The industry has been working away at progressing its thinking and approach to the issues raised and the recommendations. With this background it is not surprising there was a very large attendance at the conference and a lot of interest in developments in the industry and how funds and advisers are thinking.

There were a number of themes and issues on which speakers seemed to broadly agree.

Many speakers said that developing a financial plan for retirement is much more difficult and complex than developing a plan for the accumulation stage.

There are a myriad of unknowns that need to be considered during retirement including:

- How much income do we need?
- How long will we live?
- How could inflation affect living standards?
- What is the tolerance to volatility in asset markets?
- How does superannuation income mix with the Age Pension?
- How will we pay for higher medical expenses later in life?
- What about the children's inheritance?
- Is the home a source of income in retirement?

One way of expressing this is that investment in accumulation is managed in a relatively homogenous way, whereas retirement is a very individualistic issue and therefore it is impossible to create a one size fits all product for producing retirement incomes.

Another issue is that measurement of the effectiveness of the retirement plan is more difficult than measurement of progress during accumulation. During accumulation the main objective is to accumulate as many assets as possible, measurement is relatively easy by comparing returns against well-established benchmarks and peers. In retirement the objective that counts is to have sufficient income to experience a satisfactory retirement without running out of money. Given the myriad of uncertainties mentioned above, the retirement plan is much harder to assess. We think the industry needs to develop more measures to assess the performance rather than continuing to rely solely on the portfolios return to an index benchmark.

There seemed to be a general agreement that most retirees should include some equities in their investment portfolios, this is mainly because many retirees can expect to live for a further twenty or thirty years and equities should provide some protection against inflation and some growth in income. More practically, with very low interest rates it is difficult for fixed income portfolios to provide a decent income for long periods of time.

There was also a view that retirees have a lower tolerance of investment volatility than younger people. This creates a challenge when equities are a significant portion of assets in retirement. There is well-established research that shows investment losses hurt emotionally about twice as much as gains benefit emotionally. One speaker said that for older people this two to one relationship between feelings about losses and gains, increases to five to one. In other words, investment volatility becomes a bigger consideration in retirement.

Another generally agreed view was that receiving financial advice is much more important approaching and in retirement than it is in the accumulation phase. Topics that receive more attention in retirement include family dynamics, wills, retirement living accommodation and aged care. One problem is that many people do not want to pay for advice and another is that there are not enough advisers in Australia to provide face-to-face advice to all retirees. One telling statistic showed that retirees who receive advice feel more settled and confident and are more likely to avoid selling assets after prices have fallen.

For many retirees the family home is their most valuable asset however in Australia very few people receive income from their home at the moment. A number of speakers said that the home is the biggest untapped resource for retirees. At present most financial institutions do not actively promote products that can release income from the home. This is surprising given the fact that housing is a very expensive asset class and selling some of the home at a high price seems to make sense.

Conferences such as this provide a good forum for everyone involved in the provision of services to the retirement sector to interact and discuss developments and new approaches that will lead to better outcomes for retirees.