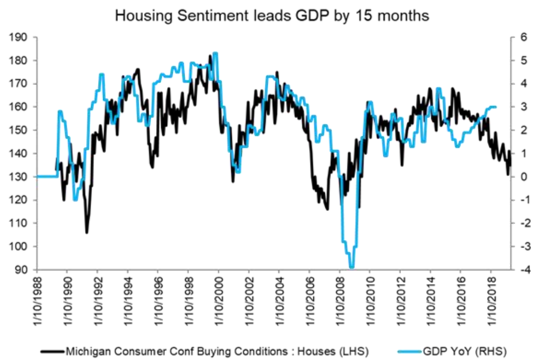
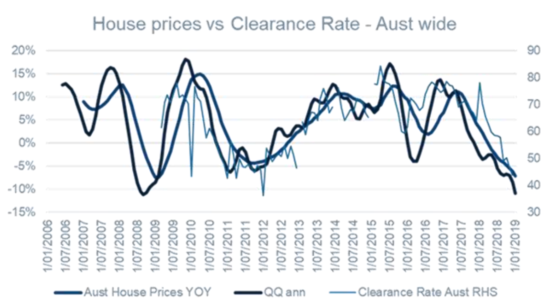
ATRIUM QUARTERLY INVESTMENT INSIGHTS

We have recently completed a series of client events around the country where our Chief Investment Officer - Tony Edwards presented our current views on economic activity and investment markets, portfolio positioning and the outlook for returns. We thought a summary of these points might be useful. We have highlighted these below.

Current view on the economic activity and markets over the past 6 months

- There has been a significant and rapid deterioration in global economic data since the last quarter of last year. A broad range of economic indicators (which often provide a reasonable lead as to the future trajectory of markets) started to move sharply lower at the same time that the outlook for bond yields has been rising. These moves appear to be at odds with each other. Examples of these (seen below in some of the charts) include manufacturing orders and intentions, consumer sentiment, property clearance rates and retail sales. While the outlook for economic growth is moving lower, we don't believe a recession either in the US or Australia is inevitable in the near term, but there are indications that expectations of future economic growth and corporate profitability will need to be tempered.

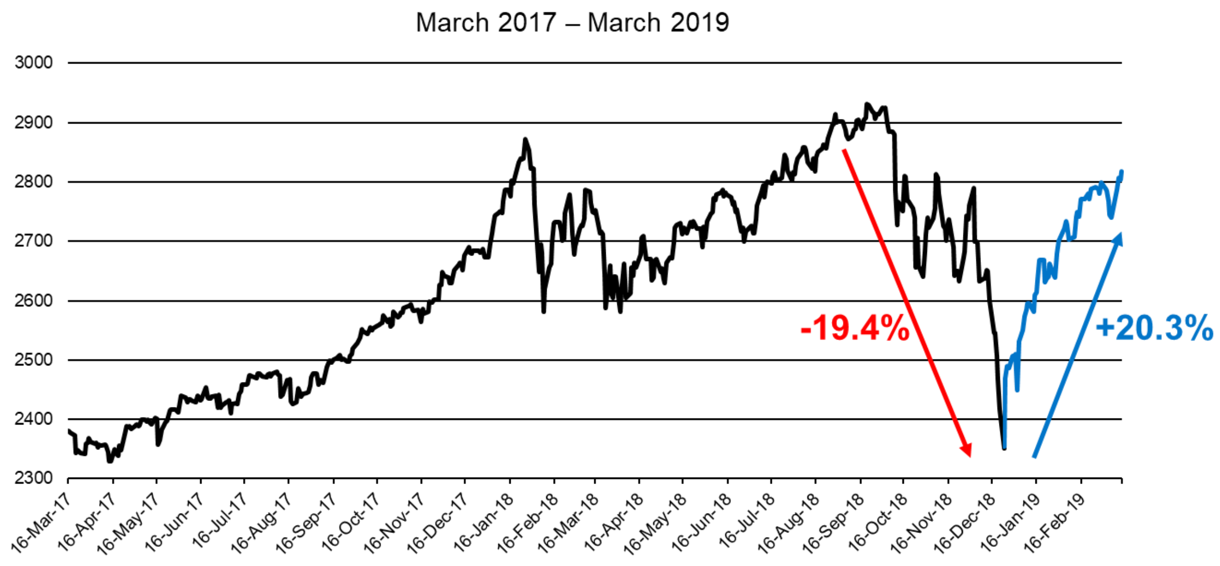




Source: Bloomberg, Atrium, NAB. Data as at 31 January 2019. Past performance is not a reliable indicator of future performance.

- In addition, during 2018 we saw central banks (the Fed in particular) gradually withdrawing stimulus by raising cash rates and winding back policies of asset purchases (quantitative easing) that were in place to inject liquidity into investment markets. Central banks have bought billions of dollars of government bonds, commercial paper, mortgage backed securities and equities since the GFC. This has had the effect of reducing interest rates to all-time lows which has had a material and positive impact on the valuations for asset classes such as property, bonds and equities.
- In the last quarter of 2018, we saw a significant drawdown for equity markets (down just below 20% for US shares at the lows). Markets became concerned that central banks would over-tighten monetary conditions – which a slowing economy could not sustain. The yield curve flattened – meaning that the yield or return for assets of a longer-term duration was actually expected to be no better (or even worse) than the return for short term assets. If rising short term rates become higher than longer term rates (yield curve inversion), then there is little incentive for investors to fund longer term investment, this leads to lower economic growth, lower earnings and hence lower company valuations.
- Central banks decided to act in January. They made comments to the effect that they would be patient on the path of liquidity withdrawal and that they would pause on interest rate rises. Markets rewarded this by buying risky assets (in particular equities). Suddenly, we were off to the races again. Equity markets have subsequently recovered during the quarter with the S&P 500 and S&P/ASX 200 indices up 13% and 9.5% respectively.

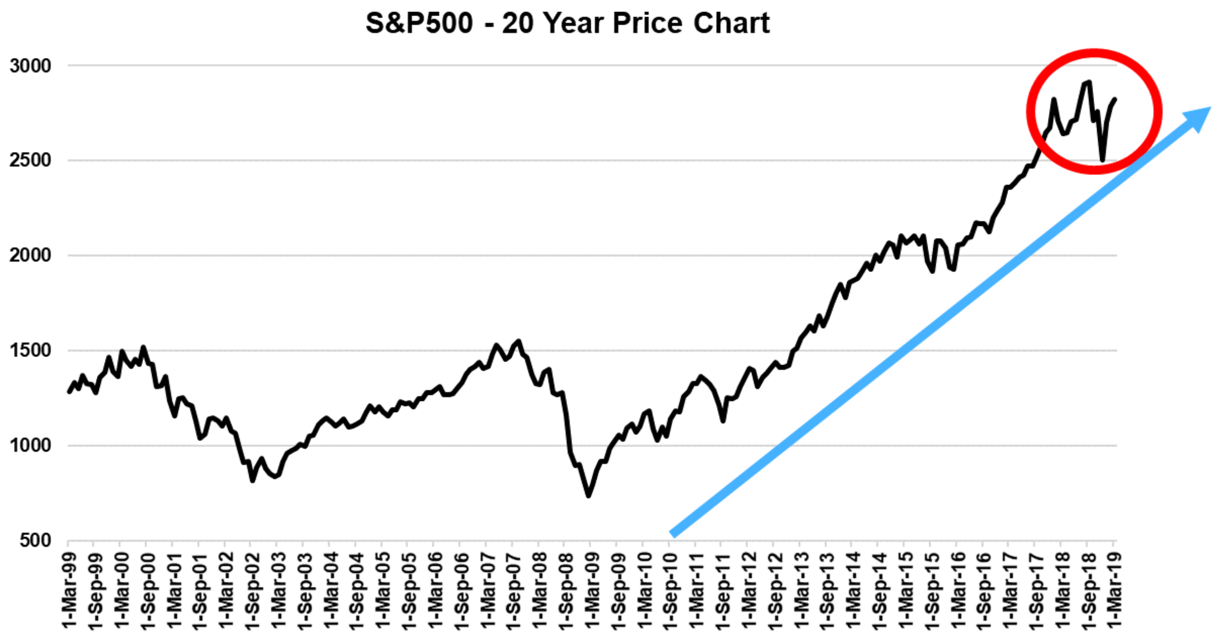
S&P500 – 'Lost' 2 Years of returns in 3 months…before Rebounding



Source: Bloomberg. Performance figures actual as at 28 February 2019. Past performance is not a reliable indicator of future performance.

Portfolio positioning and portfolio activity – A longer term context is relevant and insightful

- Markets have clearly had a good run over the past 5-10 years since the GFC. While it might not feel like a boom time as asset prices have moved much higher than wages, believe it or not we are now in the longest bull run in history, outstripping the early 1900's, the tech boom as well as the pre-GFC boom.



Source: Bloomberg. Performance figures actual as at 26 February 2019. Past performance is not a reliable indicator of future performance.

- When it comes to investing, there is a time to be greedy and a time to be prudent. In our view, the time to be greedy was in the early years of this bull market run, and while the latter stages of a bull market can continue to be prosperous for investors for some time, it is prudent to diversify risk to a more balanced stance ahead of the end of a bull market.
- The portfolios continue to be invested actively in a range of preserving, diversifying and growth assets. In recent times we have been active across the portfolio in a range of areas. We highlight some of these active decisions below:
    1. Post the market sell-off in late December, we topped up our equity positions particularly in the banks and a few key holdings. This proved to be a good decision, with markets now up over 20% since this point. We had subsequently taken some profits as the market recovered.
    2. When central banks highlighted their intentions to pause their interest rate normalisation program in the near term, we took the opportunity to lengthen the duration of the bond portfolio. It was our view that markets would see this as an opportunity to purchase bonds and push yields even lower.
    3. We added to our Alternatives managers in our Evolution Series, adding Two Sigma – a multi-asset long/short manager to the portfolios. Two Sigma has built into one of the preeminent quantitative alternative managers with an enviable track record, having delivered 16 consecutive years of positive active returns. We exited our positions in Latigo and Alphadyne.
    4. For those clients invested in Real Assets, either via the Atrium Evolution Series or the Atrium Real Assets Fund, we have also been active in this part of the portfolio. The

Fund made an investment into a portfolio of presold townhouse projects in the ACT, to provide a predictable exposure to the long-term requirement for housing and office/retail property in the ACT. This is one of a number of transactions we have undertaken in Real Assets in the past twelve months and this asset class continues to diversify.

- We've also been active in reviewing our managers and attending company meetings:
  1. We met with a range of managers during the quarter including:
     - Antipodes (global equities)
     - SG Hiscock ICE (Australian equities)
     - Bennelong (liquid alternatives)
     - JP Morgan (rates & credit)
     - One River (liquid alternatives)
     - GMO (liquid alternatives)
  2. We also visited several companies in the quarter including:
     - Challenger
     - Woolworths
     - EML Payments
     - Sydney Airport
     - James Hardie
     - Carsales
     - Lifestyle Communities
     - Small-cap tech companies

  We exited Super Cheap Auto, RIO Tinto and MYOB (Takeover) over the quarter. We added to our positions in Treasury Wine Estates and Ramsay Healthcare.

Outlook

- There has been a shift in the outlook for investment markets driven by globally co-ordinated central bank actions that reconfirm the view of lower interest rates for longer – effectively extending the cycle and underpinning higher valuations for a range of assets.
- This has resulted in a bounce in global equity markets over the quarter that has been quite extraordinary with the MSCI World Index returning over 11% to the end of March. In our view, valuations are not cheap relative to historical levels and are stretched in some asset classes (such as in bond markets) as a result of low interest rates on a global basis, and we are likely to see further market volatility as a result.
- We believe that the Australian dollar is likely to continue to face headwinds as the domestic economy adjusts to an environment of lower growth.
- Given our positioning over the past quarter, we are more than comfortable with the return profile of the portfolios over this period. It has been an environment where taking risk has been rewarded, so to deliver robust returns as we have with measurably lower risk than equity markets has been in-line with our philosophy of delivering strong risk adjusted returns over the long term.
- Of note, we have highlighted the importance of timeframes when investing. Areas like Alternatives have over the longer term provided important contribution to overall returns but can be subject to shorter-term changes in market conditions (as occurred in Q4 2018). We are extremely pleased with the rebound in performance in this sector in the first quarter of 2019 and we remain confident in the line up of managers which make up this strategy.
- Risks abound globally, the negative 'wealth effect' on sentiment in Australia from falling house prices, slowing Chinese growth, trade wars, debt levels, Brexit and the rise of populism. A robust investment process with a focus on value and asset quality helps us to navigate through the noise and assess markets over a longer timeframe for our investors, while being alert to risks and opportunities in the short-term.

Important Information

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