

9 October 2018

The Manager  
ASX Market Announcements  
Australian Securities Exchange  
Exchange Centre  
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Sydney NSW 2000

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**Electronic Lodgement**

**Australian Foundation Investment Company Limited  
2018 Annual General Meeting Presentation**

Dear Sir / Madam

Please find attached a presentation that will be delivered to shareholders at the Company's Annual General Meeting to be held today.

Yours faithfully

A handwritten signature in grey ink, appearing to read 'M Rowe', is positioned above the typed name of the signatory.

Matthew Rowe  
Company Secretary



# Annual General Meeting 2018 Presentation

**AUSTRALIAN  
FOUNDATION  
INVESTMENT  
COMPANY**

**90** YEARS OF INVESTMENT  
EXPERIENCE

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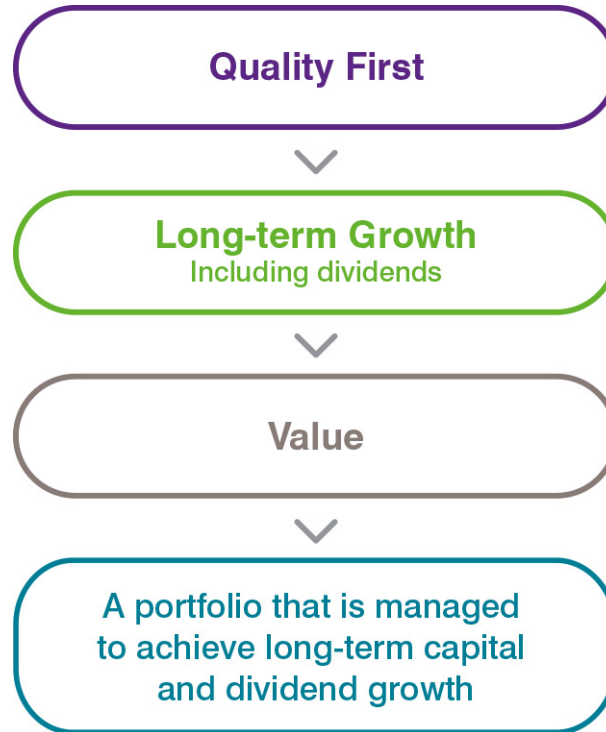
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## Our Investment Approach

# AFIC is a Long Term Investor in a Diversified Portfolio of Quality Companies

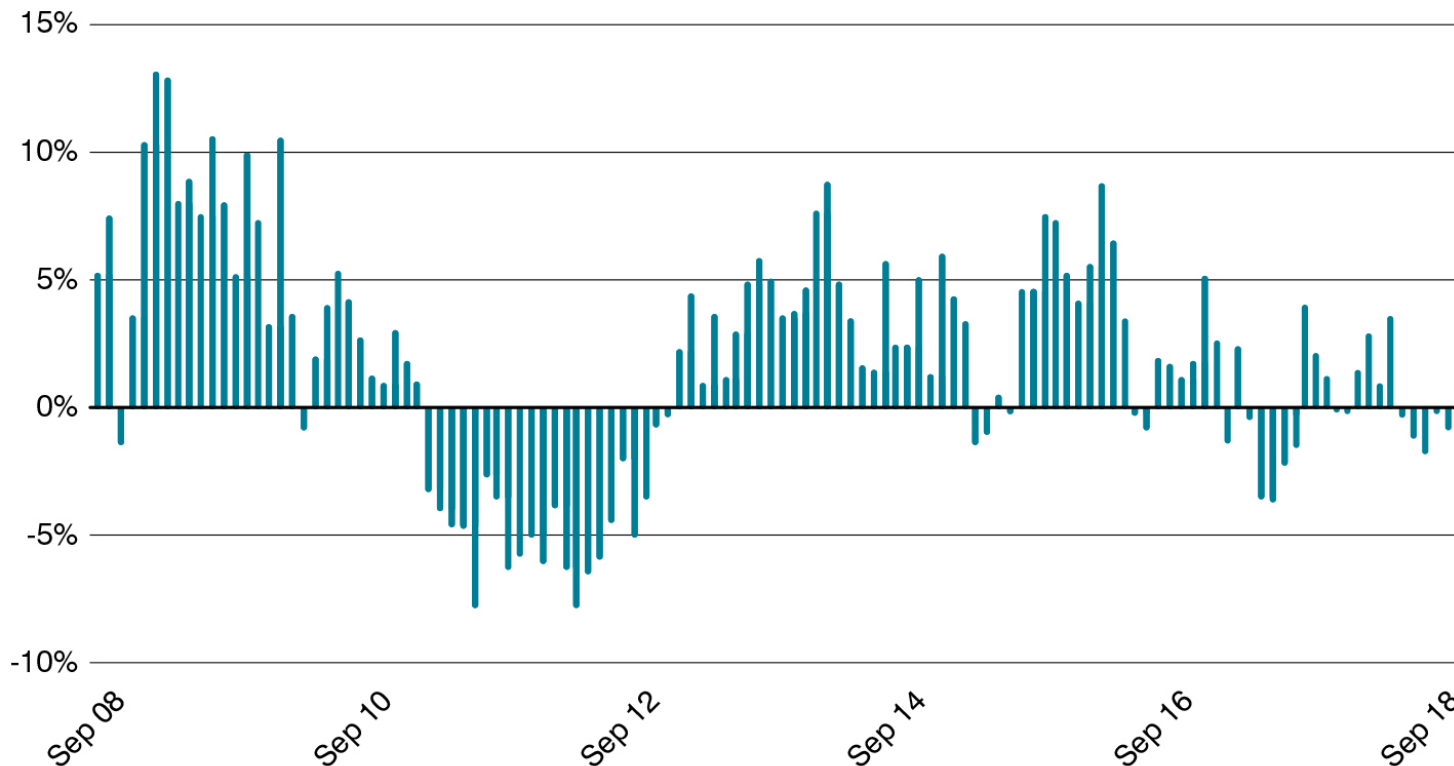


# Growth of a \$1,000 Investment in AFIC Shares (including benefit of franking) – 10 years to 30 September 2018



Assumes the reinvestment of AFIC dividends and an investor can take full advantage of the franking credits

# Share Price is trading at a very slight premium to Net Asset Backing







# Financial Results

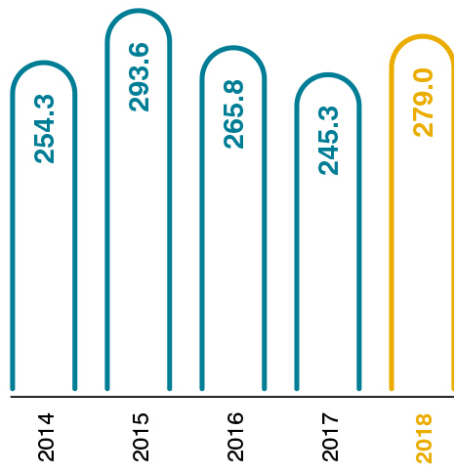
Annual General Meeting 2018

**AUSTRALIAN  
FOUNDATION  
INVESTMENT  
COMPANY**

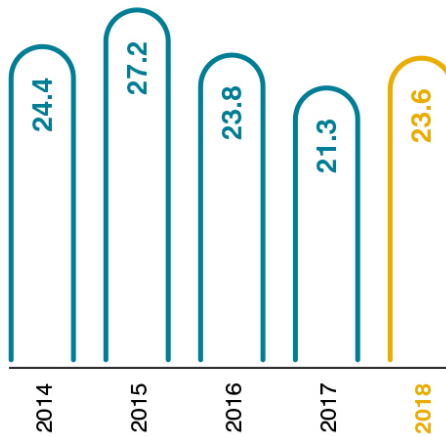


# Financial Results

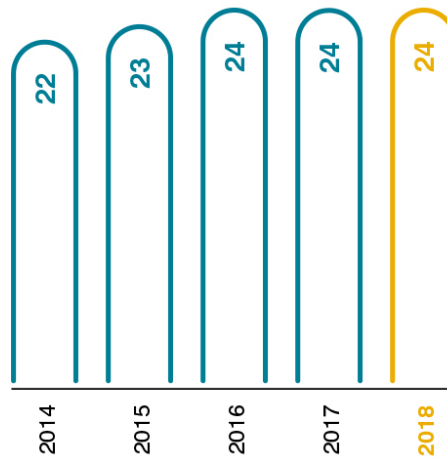
Net Profit After Tax (\$ Million)



Net Profit Per Share (Cents)



Dividends Per Share (Cents)



*Management expense ratio of 0.14%*

## Ending refundability of franking credits

- We are again highlighting that the Labor Party has announced that if elected it will stop excess franking credits being refunded to some shareholders.
- This will impact individuals and super funds – in particular, self-managed super funds.
- If an investor does not have sufficient other taxable income, they will have to pay 30% tax on their dividends.
- An income of \$50,000 per year in dividends (including franking credits) will be reduced to \$35,000.
- Low income earners and individuals in retirement will be very hard hit.

## Ending refundability of franking credits – our response

- AFIC has provided a template letter on its website for shareholders to write to their parliamentary representatives - **personal examples are likely to have the biggest impact on local members.**
- We have engaged through various industry groups to lobby on your behalf.
- Publicised where appropriate through the media.
- Submission by AFIC to the house economics committee.

Email: [economics.reps@aph.gov.au](mailto:economics.reps@aph.gov.au)

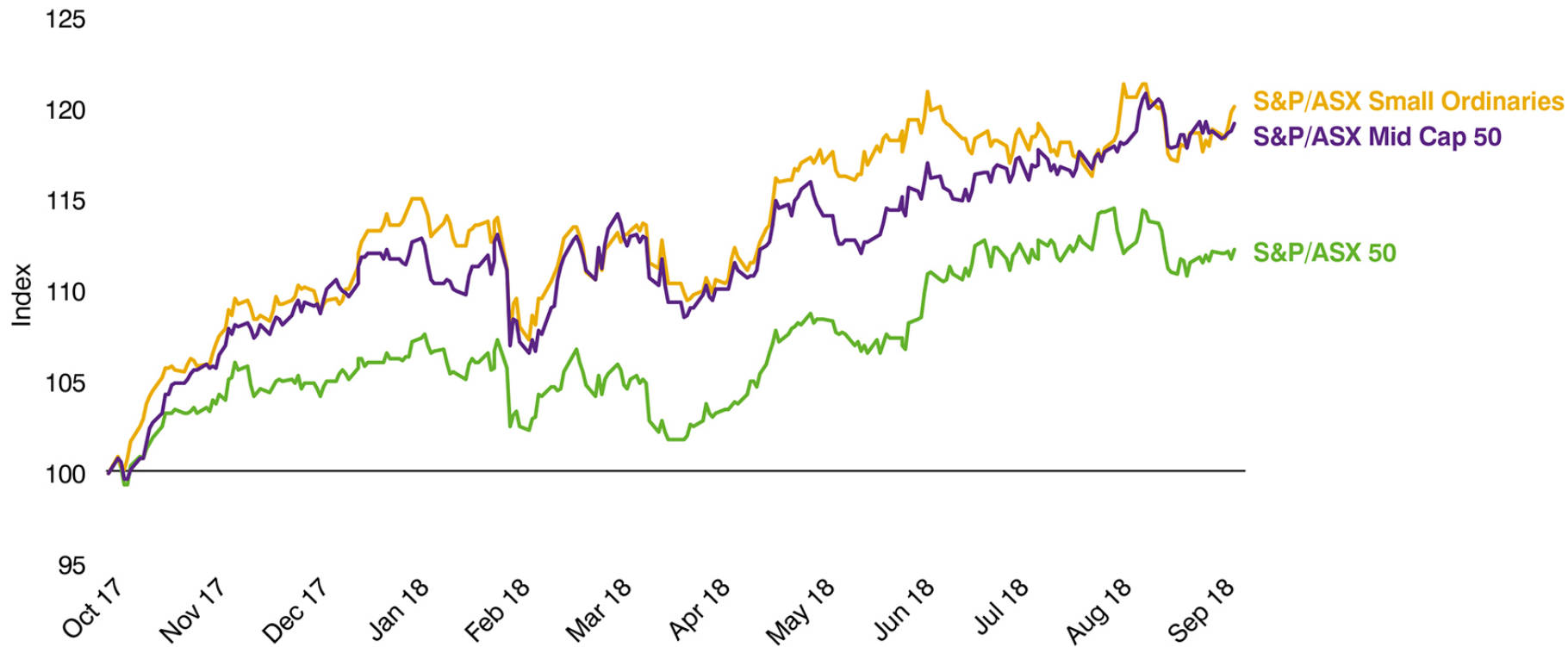
Mail: Committee Secretary  
Standing Committee on Economics  
PO Box 6021, Parliament House, Canberra ACT 2600





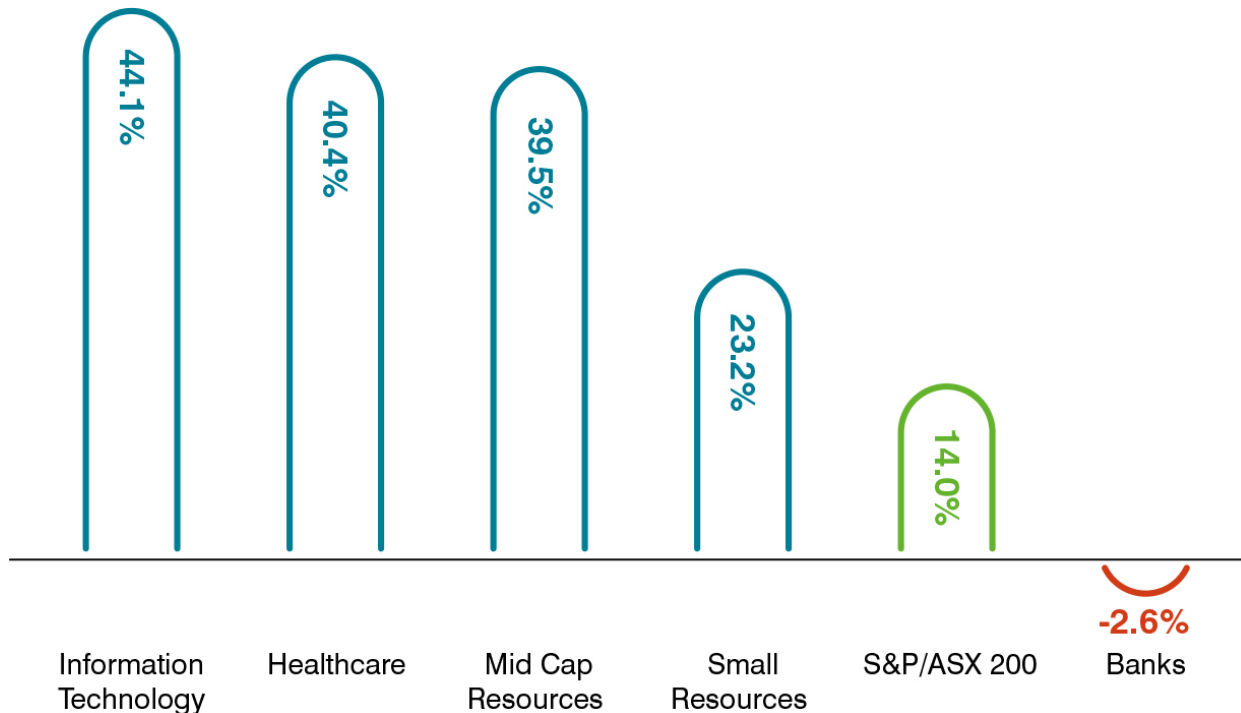
# Market Settings and the Portfolio

# Large companies have underperformed over the year to 30 September 2018



Source: FactSet

## With some growth sectors very strong and banks at the other extreme – returns to 30 September 2018

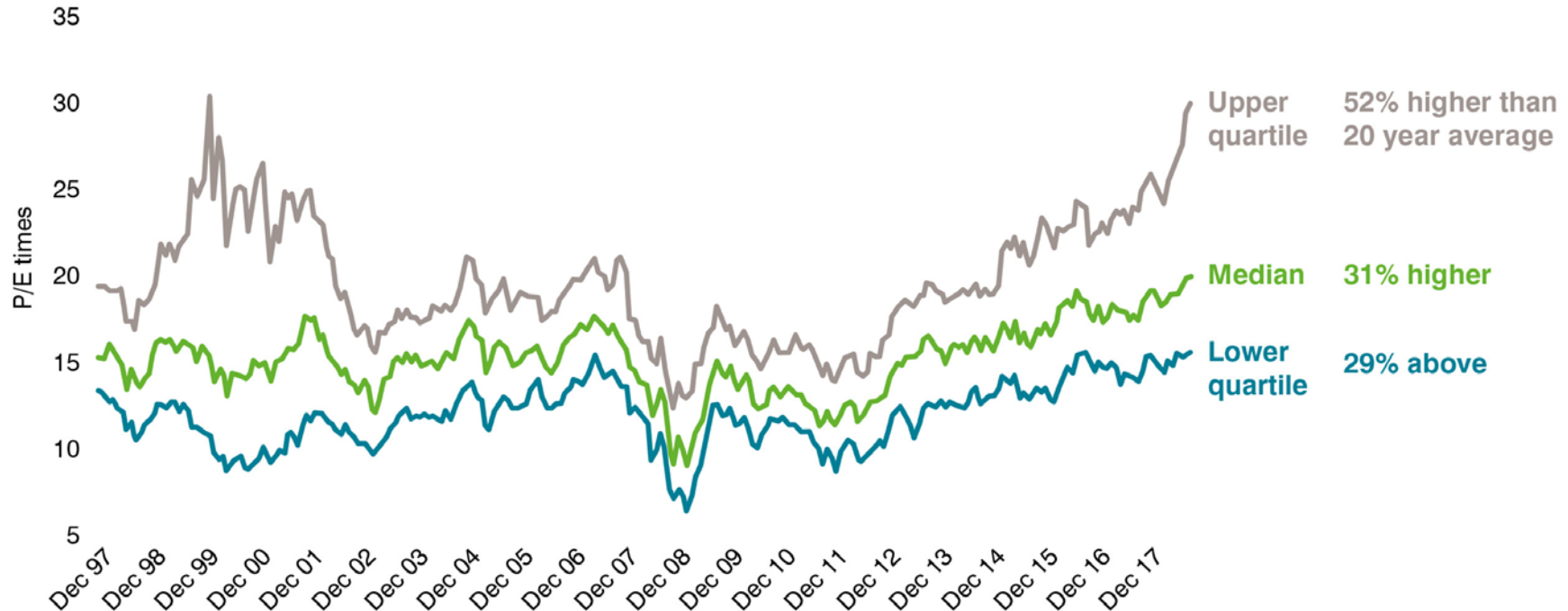


Returns include dividends



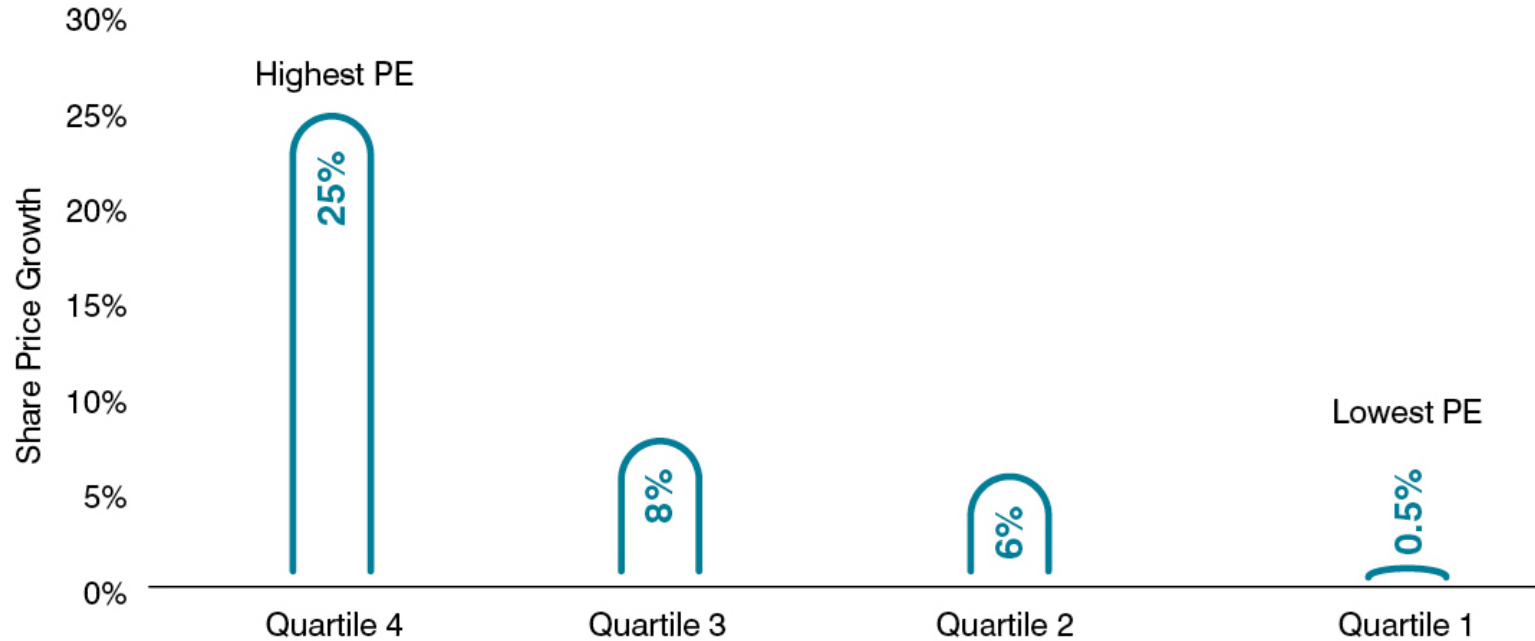
# High growth firms now trade above 30x forward P/E, in line with the peak of the dotcom bubble

ASX 200 Valuation dispersion



Source: FactSet, Goldman Sachs Global Investment Research.

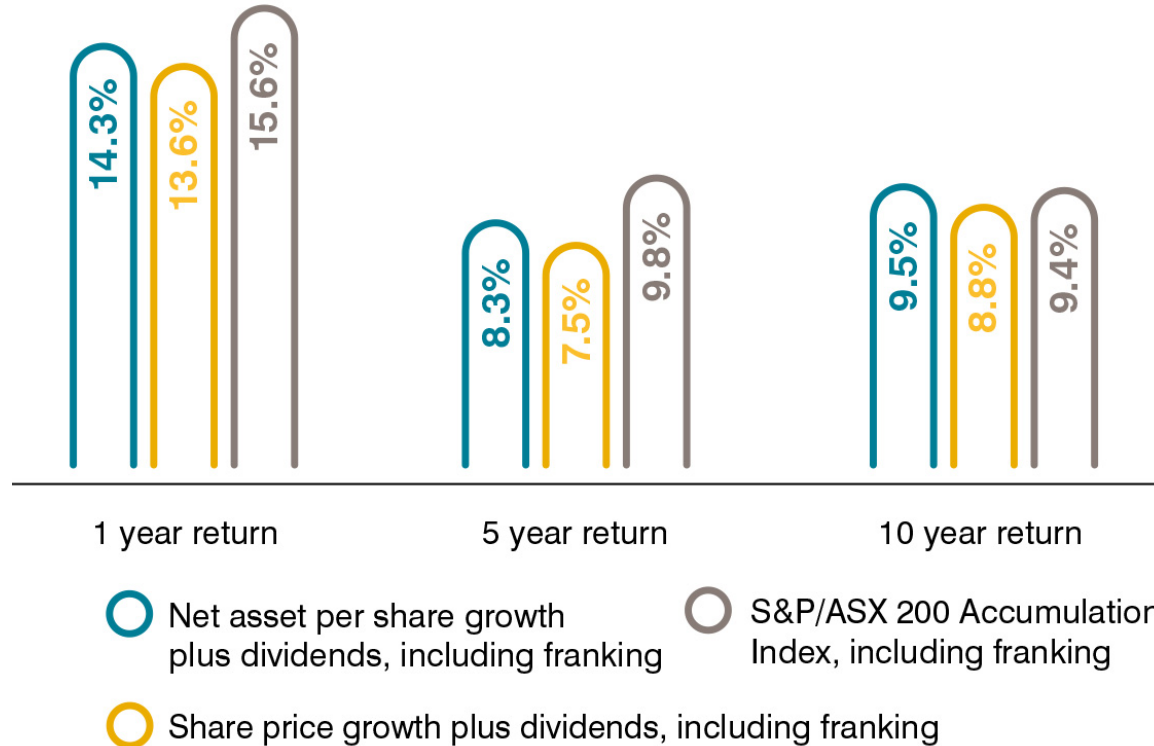
# High PE stocks have outperformed low PE names by 25% year to date



○ Performance by PE quartile at start of year (ASX 200 ex resources, market cap weighted).

Source: FactSet, UBS

# Relative Portfolio and Share Price Performance, including franking – Per Annum Returns to 30 September 2018



Assumes an investor can take full advantage of franking credits.



# Market moves as well as purchases/sales have changed the profile of the Portfolio – top 10 holdings 30 September 2018

| Rank | Company                                 | % of Portfolio | Major changes –<br>% as at Sept 2017 |      |
|------|---|----------------|--------------------------------------|------|
| 1    | Commonwealth Bank of Australia          | 7.7%           | ↓                                    | 8.9% |
| 2    | BHP                                     | 6.7%           | ↑                                    | 5.4% |
| 3    | Westpac Banking Corporation             | 5.9%           | ↓                                    | 7.4% |
| 4    | CSL                                     | 5.2%           | ↑                                    | 3.7% |
| 5    | Wesfarmers                              | 4.6%           |                                      |      |
| 6    | Rio Tinto                               | 3.6%           |                                      |      |
| 7    | Transurban Group*                       | 3.6%           |                                      |      |
| 8    | National Australia Bank                 | 3.5%           | ↓                                    | 4.7% |
| 9    | Australia and New Zealand Banking Group | 3.3%           | ↓                                    | 3.8% |
| 10   | Macquarie Group                         | 3.1%           | ↑                                    | 1.1% |

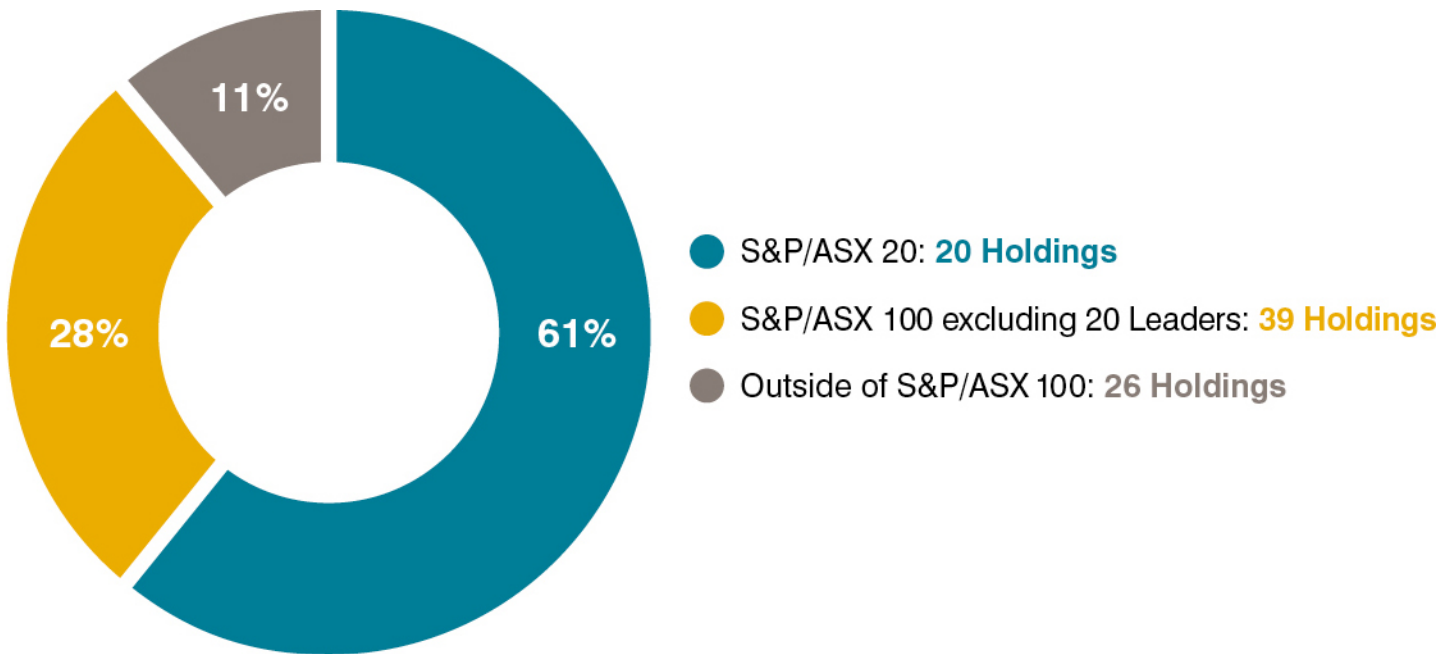
\* Options were outstanding against part of the holding.

# Market moves as well as purchases/sales have changed the profile of the Portfolio – next 10 holdings 30 September 2018

| Rank | Company                 | % of Portfolio | Major changes –<br>% as at Sept 2017 |               |
|------|-------------------------|----------------|--------------------------------------|---------------|
| 11   | Woolworths Group*       | 2.5%           | ↑                                    | 1.9%          |
| 12   | Amcor                   | 2.3%           |                                      |               |
| 13   | Oil Search              | 2.0%           |                                      |               |
| 14   | Woodside Petroleum*     | 2.0%           | ↑                                    | 1.4%          |
| 15   | Brambles                | 1.8%           |                                      |               |
| 16   | Telstra Corporation     | 1.7%           | ↓                                    | 2.7%          |
| 17   | Sydney Airport*         | 1.6%           | ↑                                    | Not in top 20 |
| 18   | James Hardie Industries | 1.3%           | ↑                                    | Not in top 20 |
| 19   | Qube Holdings           | 1.3%           |                                      |               |
| 20   | Treasury Wine Estates   | 1.3%           |                                      |               |

\* Options were outstanding against part of holding.

## Profile of the portfolio by size of company September 2018 – looking for growth opportunities some of which is outside of large companies



# The other interesting feature of the portfolio is the exposure to businesses with revenue generated from overseas – 43% of the portfolio

Key examples:

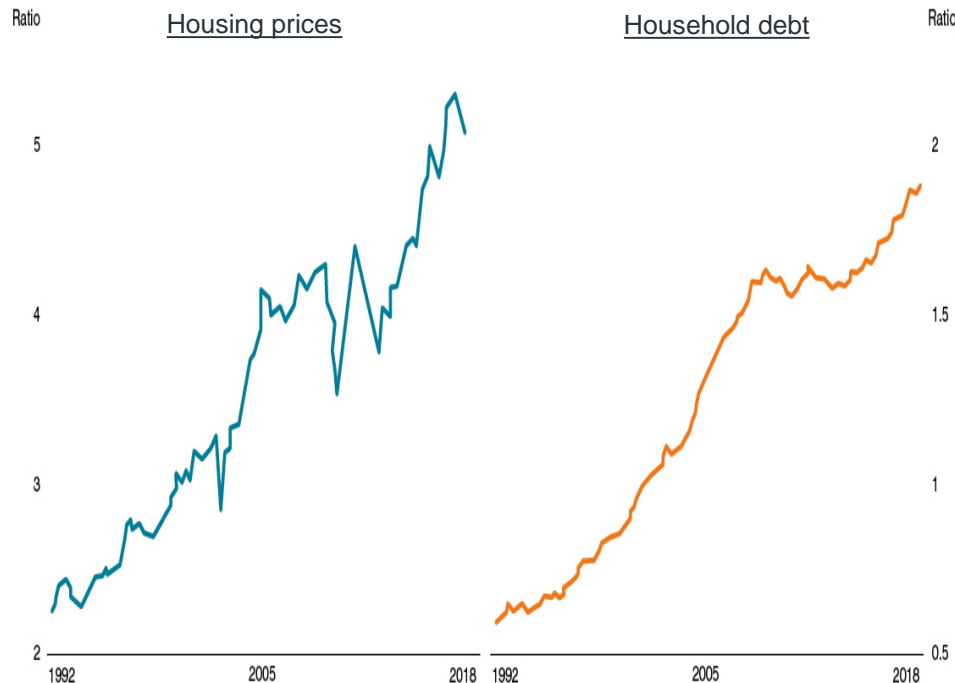
- BHP Billiton
- CSL
- Rio Tinto
- Amcor
- Oil Search
- Macquarie Group
- Woodside Petroleum
- Brambles
- James Hardie Industries
- Computershare
- Seek
- ResMed
- Fisher & Paykel Healthcare
- Mainfreight

Source: FactSet, AFIC.

# Australian Banks – growth in household debt has been a major tailwind

## Housing Prices and Household Debt

Ratio to annual household disposable income



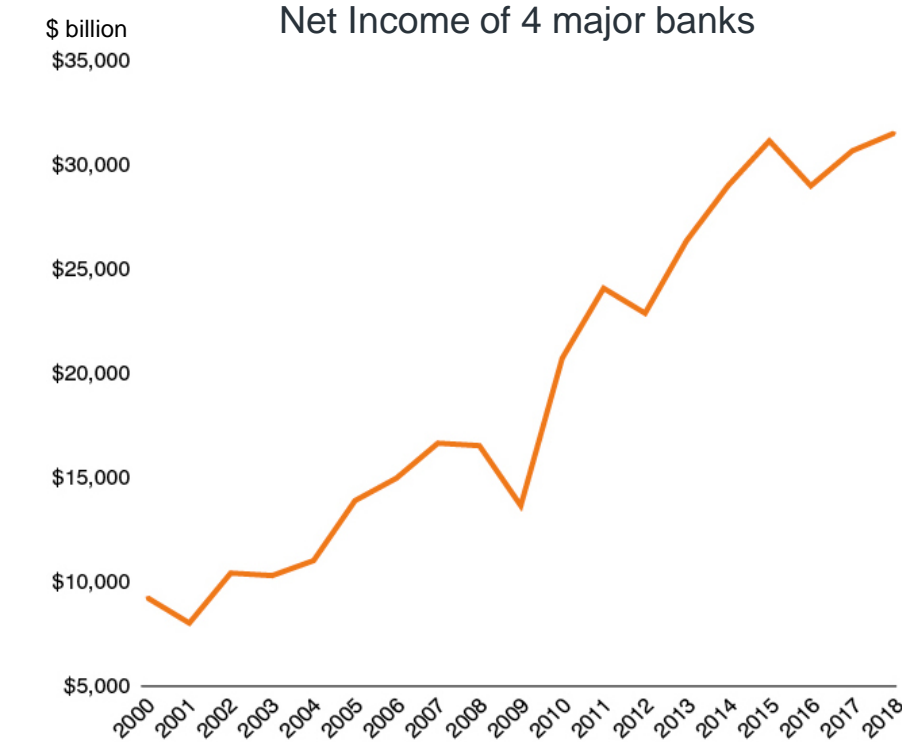
Sources: ABS; APM; APRA; Core Logic; RBA.

Upward trend in housing prices driven by increased household debt:

- Growing population, with immigration a key component.
- Supportive commodity cycle.
- Unbroken record of economic growth.
- Low interest rates post GFC.
- Easier credit standards.



# Australian Banks – Net Income growth has been strong on the back of these trends however going forward.....



Source: FactSet

## Credit growth likely to be more subdued:

- Lower income growth.
- Tighter lending standards:
  - APRA
  - Hayne Royal Commission
  - Slowing foreign investment in housing

## Impact on Bank Sector

- Lower balance sheet growth.
- Higher regulatory costs.
- Slowing housing market can be healthy.
- Banks will look to drive further costs out.
- Benign profit growth but dividends stable.

# Featured Holdings – Macquarie Group

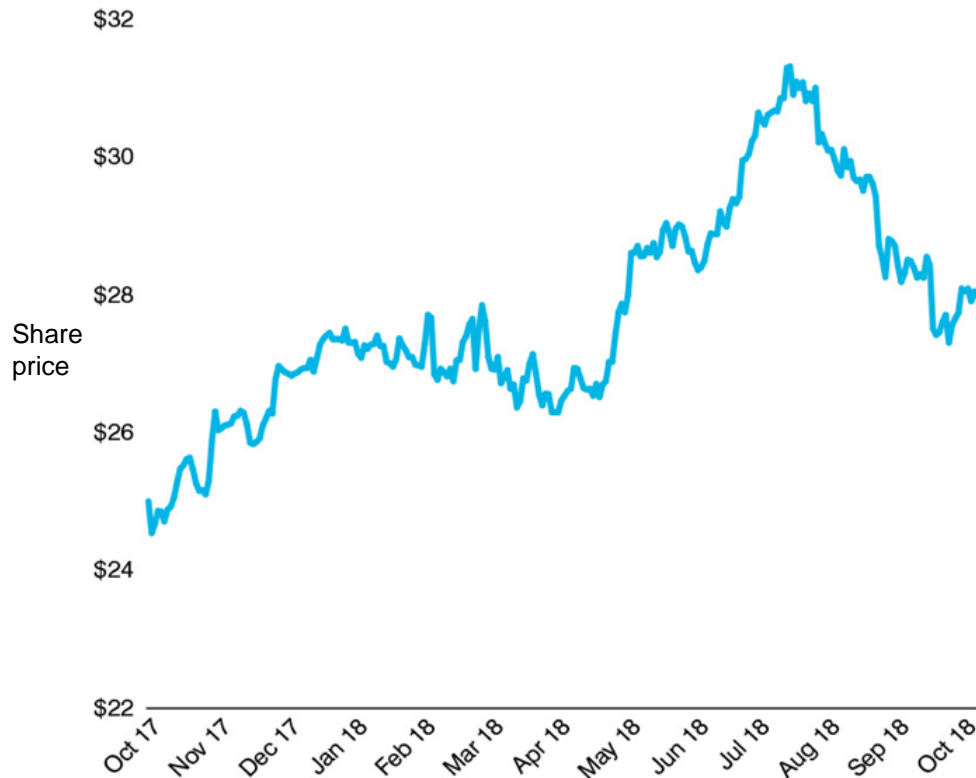


Source: FactSet.

What we like:

- Owner driver culture.
- Infrastructure exposure.
  - Energy (renewable)
  - Emerging markets
  - GDP/ population growth
- Technology exposure.

# Featured Holdings – Woolworths



Source: FactSet.

What we like:

- 'New' management with clear strategy.
- Progress on turnaround:
  - Australian supermarkets regained market leadership
  - IT Investment
  - Exit Masters
  - Simplify BigW
- Next phase: Ongoing investment opportunities.
- From here, maintain focus.
- Stable profit and dividend growth.

# Featured Holdings – Reliance Worldwide



Source: FactSet.

## What we like:

- Category leader in Push to Connect plumbing fittings market.
- Innovative company with R&D focus.
- Multiple growth drivers in North American and European markets.
- Self funding, cash generative business model.
- Strong balance sheet.
- Participated in rights issue.



# Closing Remarks



## Recent Company Reporting Season

- CBA, bank sector: struggling for earnings growth.
- Healthcare: very strong earnings growth but on high P/E's (Hospitals the exception).
- Resources: very strong cash generation, returning capital to shareholders.
- Energy sector: rising cash flows, strong oil price, new major projects moving forward.
- Telco's: evolving sector, NBN, competition, TPG/Vodafone merger.
- Industrials: Offshore earnings driving growth.
- Technology: Exhibiting strong growth but very expensive P/E's.

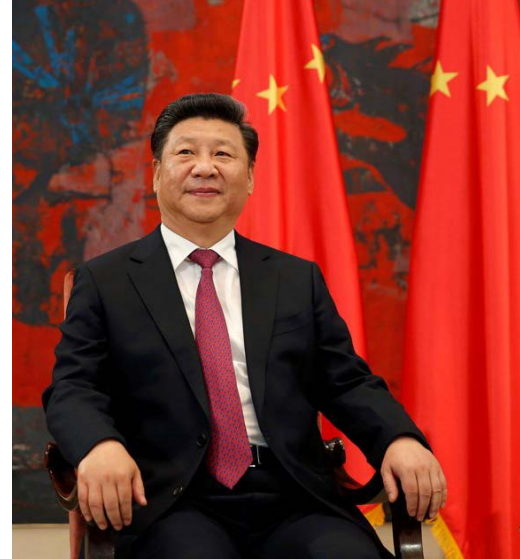
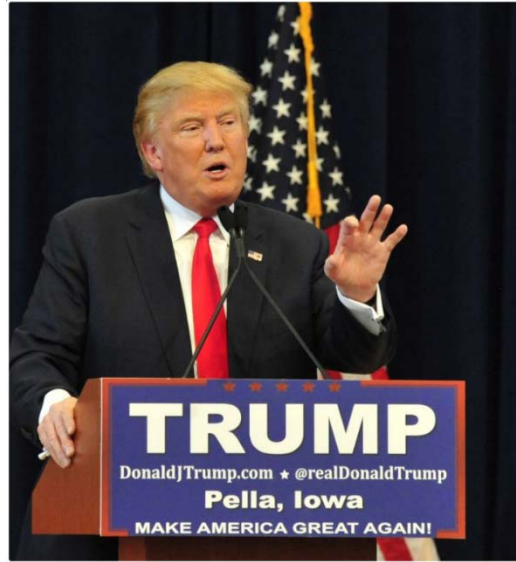
## Current Issues We Are Focusing On

- Met with 100+ companies in recent reporting season.
- Investment team visited UK/Europe/US in September and in November will be visiting China/HK.
- Themes:
  - Australian credit growth/ housing market – slowing.
  - Continued impact of technology on businesses, including emergence of new opportunities.
  - Finding value – expected long term growth versus what you have to currently pay.
  - Fallout from trade disputes.
  - Impact of rising interest rates in the US on equity markets.

## Last 10 years and next 10 years?

|                                     | Last 10 years   | Coming 10 years?        |
|-------------------------------------|-----------------|-------------------------|
| Interest Rates                      | Falling         | Rising                  |
| Wage Pressure                       | Benign          | Rising                  |
| Transport Costs                     | Benign          | Rising (US trucks, etc) |
| Excess Capacity (Industrial, other) | High            | Reducing                |
| US Corporate Profit Margins         | Rising          | Potential peak          |
| Investor Focus                      | Earnings growth | Valuation               |
| Corporate's use of capital          | Buybacks        | Investing               |
| Price earnings multiple             | Rising          | Falling?                |
| Inflation                           | Benign          | Rising?                 |

Other factors are still at play...



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