

21 February 2020

The Manager  
ASX Market Announcements  
Australian Securities Exchange  
Exchange Centre  
Level 4  
20 Bridge Street  
Sydney NSW 2000

Australian Foundation  
Investment Company Limited  
ABN 56 004 147 120  
Level 21, 101 Collins St  
Melbourne VIC 3000  
T 03 9650 9911  
F 03 9650 9100  
invest@afi.com.au  
afi.com.au

**Electronic Lodgement**

**Australian Foundation Investment Company Limited  
Half Year Review to 31 December 2019**

Dear Sir / Madam

Please find attached the Half Year Review to 31 December 2019 that is being sent to shareholders.

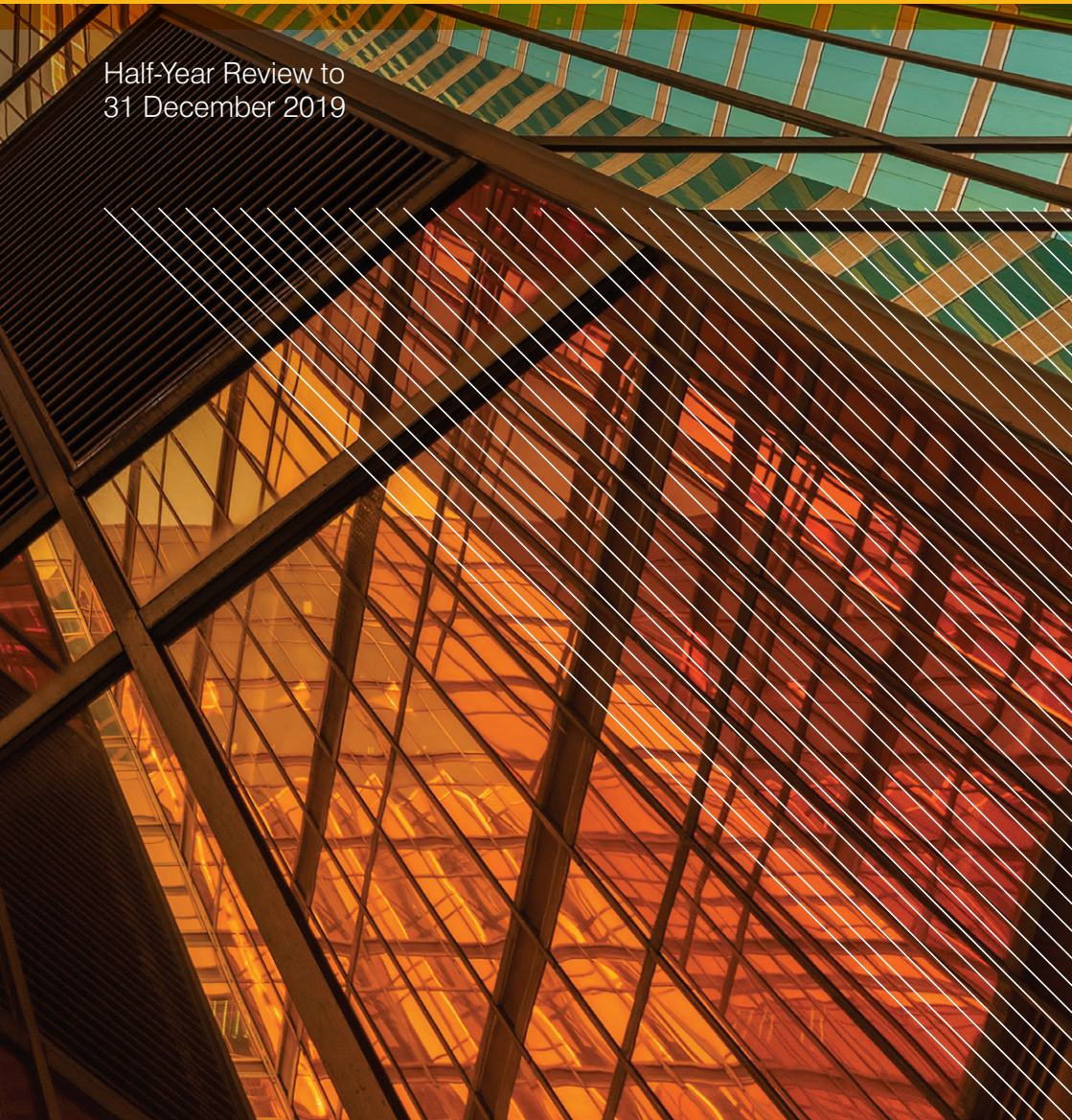
Yours faithfully



Matthew Rowe  
Company Secretary

Release authorised by Matthew Rowe, Company Secretary

Half-Year Review to  
31 December 2019



# Contents

- 1 Half-Year in Summary
- 2 About the Company
- 4 Review of Operations and Activities
- 11 Top 25 Investments
- 12 Income Statement
- 13 Balance Sheet
- 14 Summarised Statement of Changes in Equity
- 15 Holdings of Securities
- 19 Major Transactions in the Investment Portfolio
- 20 Company Particulars
- 21 Shareholder Meetings

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Australian Foundation Investment Company is a listed investment company investing in Australian and New Zealand equities.

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# Half-Year in Summary

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## Profit for the Half-Year

\$146.1m

Down 39.1% from 2018. Excluding one off items from 2018, down 1.6%

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## Share Price at 31 December 2019

\$7.11

\$6.00 in 2018

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## Fully Franked Interim Dividend

10¢

10 cents interim, 8 cents special, total 18 cents for 2018

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## Total 6 Month Shareholder Return

16.3%

Share price plus dividend

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## Net Asset Backing Per Share at 31 December 2019

\$6.63

\$5.69 in 2018

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## Management Expense Ratio

0.10% Annualised

0.11% last year

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## Total 6 Month Portfolio Return

5.4% Including franking\*

S&P/ASX 200 Accumulation Index return including franking\* 3.8%

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## Total Portfolio at 31 December 2019

\$8.0b Including cash

\$6.8 billion in 2018

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\* Assumes an investor can take full advantage of the franking credits.



# About the Company

## About the Company

Australian Foundation Investment Company (AFIC) is a listed investment company investing in Australian and New Zealand equities.

## Investment Objectives

The Company aims to provide shareholders with attractive investment returns through access to a growing stream of fully franked dividends and growth in capital invested.

The Company's primary investment goals are:

- to pay dividends which, over time, grow faster than the rate of inflation; and
- to provide attractive total returns over the medium to long term.

## Approach to Investing

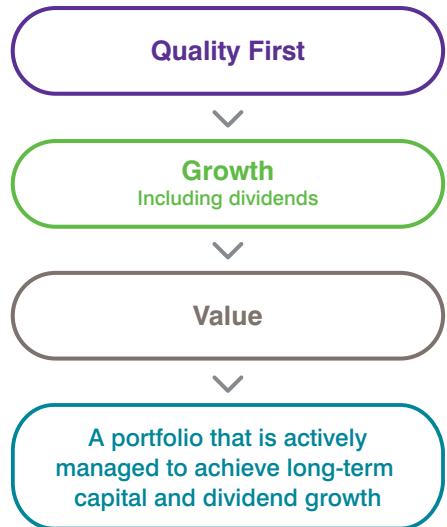
The investment philosophy is built on taking a medium to long-term view on companies in a diversified portfolio with an emphasis on identifying quality companies that are likely to sustainably grow their earnings and dividends over this time frame.

Quality in this context is an outcome of our assessment of the board and management as well as some key financial metrics. These include, the level of gearing in the balance sheet, margins and free cash flow. The structure of the industry and a company's competitive position in this industry is also an important indicator of quality. Linked to this assessment of quality is the ability of companies to grow earnings over time, which ultimately should produce good dividend growth.

Recognising value is also an important aspect of sound long-term investing. Short-term measures such as the price earnings ratio, price to book or price to sales may be of some value, but aren't necessarily strong predictors of future performance. Our assessment of value tries to capture the opportunity a business has to prosper and thrive over the medium to long term.

In building the investment portfolio in this way, we believe we can offer investors a well-diversified portfolio of high-quality companies that is intended to deliver total returns ahead of the Australian equity market and with less volatility over the long term.

## How AFIC Invests – What We Look For in Companies



The Company also uses options written against a small proportion of its investments and a small trading portfolio to generate additional income.

From time to time, some borrowings may be used where potential investment returns justify the use of debt. This is managed within very conservative limits, as determined by the Board.

AFIC is managed for the benefit of its shareholders with fees based on the recovery of costs rather than as a fixed percentage of the portfolio. There are no performance fees. As a result, the benefit of scale over time results in a very low expense ratio for investors. For the six months to 31 December 2019 this was 0.10 per cent (annualised), or 10 cents for each \$100 invested.



# Review of Operations and Activities

## Profit and Dividend

Profit for the half-year was \$146.1 million, down from \$239.8 million in the corresponding period last year. Excluding one-off items set out in the next paragraph, the half-year profit of \$146.1 million was down only 1.6 per cent from the underlying profit of \$148.5 million last half-year.

Investment income for the half-year was \$153.9 million, down from \$246.7 million in the last half-year. In the previous corresponding period, a number of one-off items increased investment income that were not repeated this half-year. This included participation in the Rio Tinto and BHP off-market share buy-backs and the receipt of a dividend because of the Coles demerger from Westfarmers.

Total interim dividend for the half-year is 10 cents per share, fully franked, versus 18 cents last half-year. The previous corresponding period included a special dividend of 8 cents per share, fully franked, which distributed the proceeds from the Company's participation in the Rio Tinto and BHP off-market share buy-backs. There is no special interim dividend this half-year.

## Portfolio Returns and Positioning

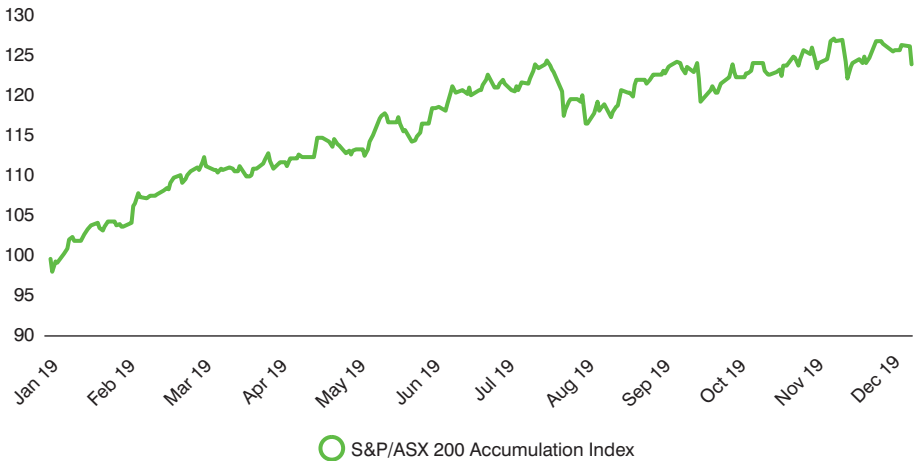
The Australian equity market, while slowing, continued to rise over the six months to 31 December 2019, despite concerns about trade tariffs, and low growth in many developed markets other than the United

States (Figure 1). AFIC has continued to adjust the portfolio, reducing the number of companies held to focus further on quality businesses with a competitive advantage, strong returns on invested capital and resilient balance sheets. This has delivered a very satisfactory portfolio performance despite not being in some of the more speculative sectors of the market.

It is also interesting to note the relative 12-month performance of some key sectors of the market (Figure 2) relevant to the overweight index positions AFIC holds in its portfolio. In particular, Healthcare (which includes CSL and Sonic Healthcare), Information Technology (which contains Xero) and Industrials (which contains Transurban, Sydney Airport and Brambles) were very strong. In comparison, most of the return for the 12-months from the major banks has been derived from their dividend yields.

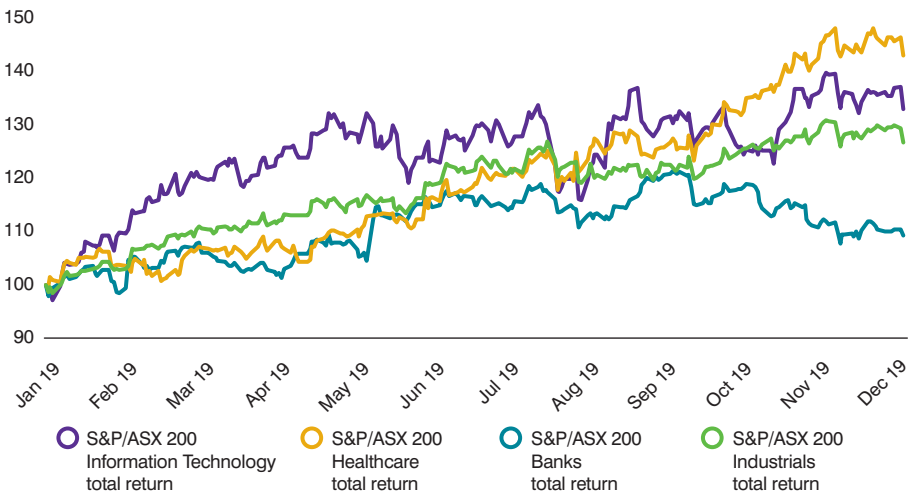
AFIC's portfolio was up 5.4 per cent for the six months to 31 December 2019 compared with the S&P/ASX 200 Accumulation Index, which was up 3.8 per cent over the same period. These figures include the benefit of franking credits, although AFIC's performance numbers are after costs. For the 12 months to 31 December 2019, the portfolio return, including franking, was 25.5 per cent. The return from the S&P/ASX 200 Accumulation Index over this period, including franking, was 25.4 per cent (Figure 3 on page 6).

**Figure 1: S&P/ASX 200 Total Return – 12 Months to 31 December 2019**



Source: FactSet

**Figure 2: Selected Sectors Total Return – 12 Months to 31 December 2019**

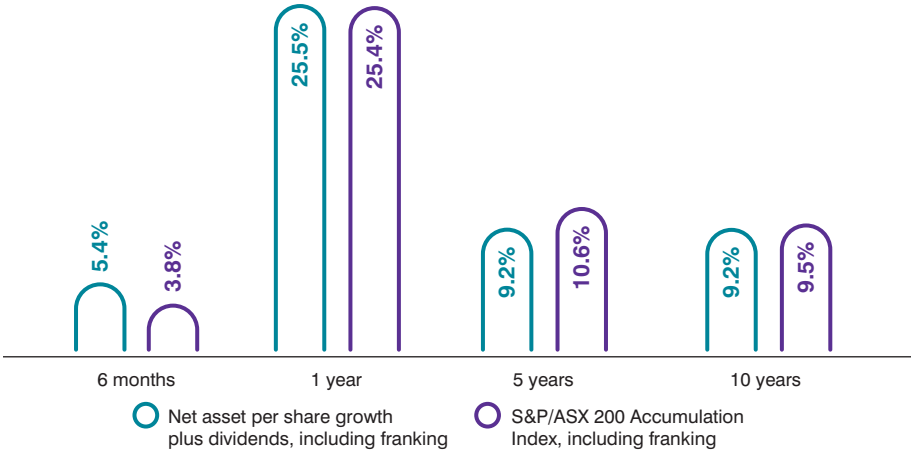


Source: FactSet



# Review of Operations and Activities continued

**Figure 3: Portfolio Performance to 31 December 2019, Including the Benefit of Franking\***



\* Assumes an investor can take full advantage of the franking credits.

Per annum returns other than six months. AFIC's performance numbers are after costs.

The portfolio approach has seen a lower proportion of the portfolio devoted to the major banks, given the competitive and regulatory issues this sector is facing. Significantly over the last four years, bank exposure has fallen from approximately 28 per cent to 19 per cent of the portfolio. AFIC has also reduced the relative exposure of the portfolio to resource companies (primarily from participation in their share buy-backs), which more recently, had benefited from strong commodity prices, particularly iron ore. In addition, holdings have been disposed of where the sustainable competitive advantage of the

business has come into question. Over a four-year period, the number of stocks in the portfolio has been reduced from 95 to 70. This has led to a reallocation of funds to preferred companies, generally into larger companies in the ASX 200 Index which have better growth prospects. The more recent effect of this repositioning when combined with a general upward move in the market has meant that the top 24 largest holdings in the portfolio (excluding the major banks and resources) have risen from 47.2 per cent to 51.4 per cent over the six-month period, and their value has gone from \$3.5 billion to \$4.1 billion.

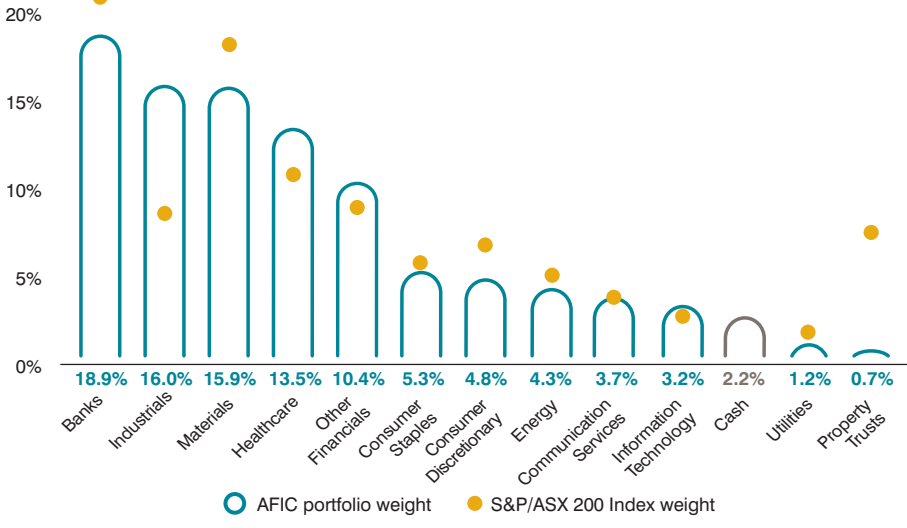


6-month Share Price  
Return

16.3%

# Review of Operations and Activities continued

**Figure 4: AFIC Investment by Sector versus the S&P/ASX 200 Index as at 31 December 2019**



It is also worth making some observations on the effect of the change in profile of the portfolio on AFIC’s more immediate income streams. The dividend cuts from three of the four major banks, combined with a reduction in the proportion of our portfolio in financials, has put a short term drag on our dividend income streams as many of our new investments have lower yields. We believe the move to stocks with a better growth profile should enhance the potential for dividend growth in the medium to long term, particularly as bank dividends are expected to remain stagnant.

## Portfolio Adjustments

As part of the move to build larger positions in quality companies with

a strong competitive advantage, further shares were purchased in Goodman Group, Macquarie Group and CSL. Major sales to fund these acquisitions included a small proportion of the holding in National Australia Bank (due to the exercise of call options through the six-month period at higher than current prices) and the complete sale of Perpetual, Boral, Orora, Link Administration, AMP and Iluka Resources. Dulux Group was sold because of a takeover.

Figure 4 highlights the profile of AFIC’s portfolio by the various sectors of the market at the end of the calendar year and how it differs from the Index.

## Share Price and Returns

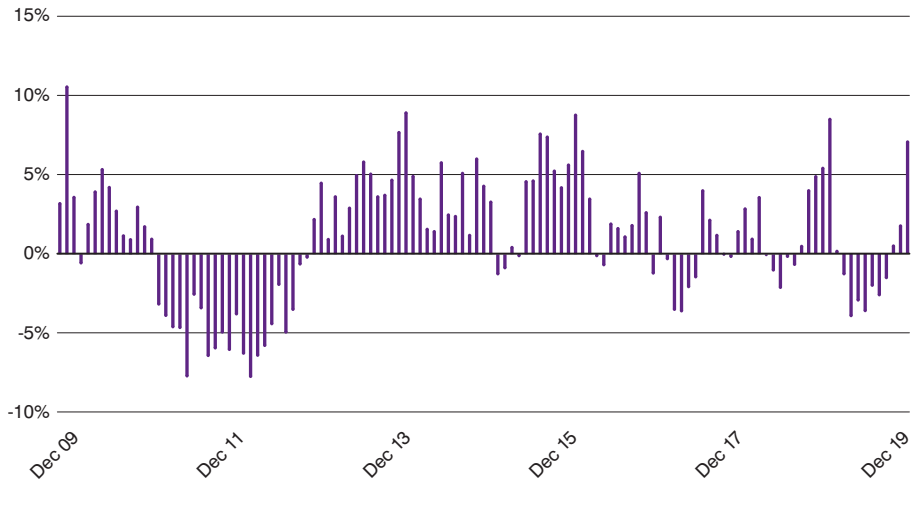
Figure 5 highlights where AFIC's share price was trading relative to the net asset backing at 31 December 2019. Over the six month period the share price has moved from a 4 per cent discount to a premium of 7 per cent to net asset backing.

This change from discount to premium is reflected in the recent strong share price return relative to the S&P/ASX 200 Accumulation Index for the six-month period to 31 December 2019 (Figure 6 on page 10). Importantly, the long term 10-year return is 7.7 per cent for the share price in comparison to 7.9 per cent for the Index. These figures do not include any benefit a shareholder can derive from the franking credits attached to the dividends paid.

## Going Forward

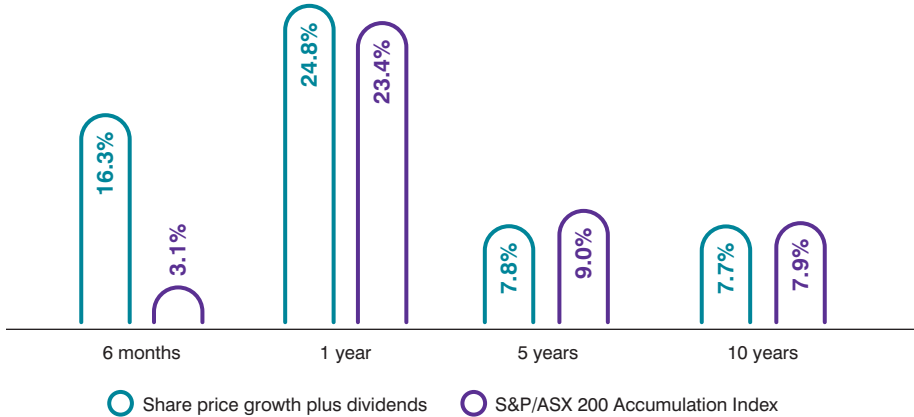
The United States and Australian equity markets are either at or close to all-time highs. With the price for many other asset classes also at or near extremes, we remain alert to the potential for increased volatility that is a reflection of the inherent risks in the market. These risks include equity market valuations (Figure 7 on page 10) that are pricing in very low interest rates, strong earnings growth and the apparent disregard of geopolitical events, such as trade disputes and potential conflict in the Middle East. We believe the portfolio is well positioned, including having sufficient funds available should good buying opportunities arise in the second half of the financial year from any increased market volatility.

**Figure 5: Share Price Relative to Net Asset Backing Per Share**



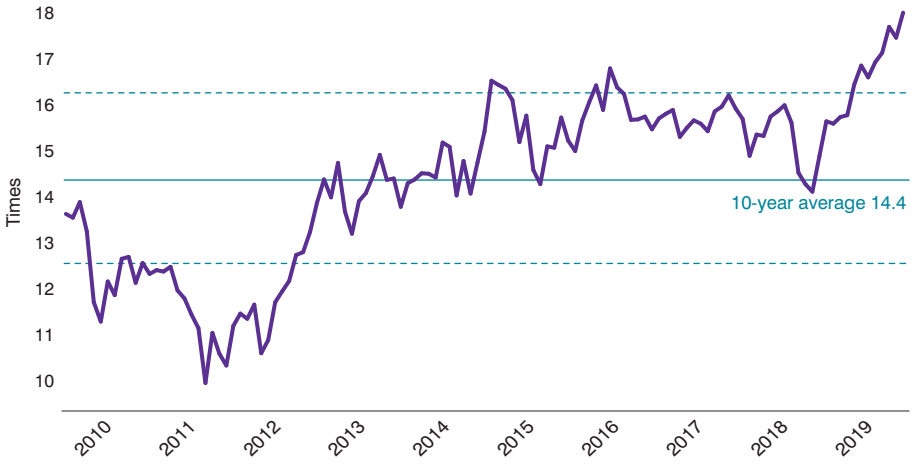
# Review of Operations and Activities continued

Figure 6: Share Price Return to 31 December 2019



Per annum returns other than six months.

Figure 7: Price Earnings Ratio (PE) of the S&P/ASX 200 Index



Source: FactSet



# Top 25 Investments

As at 31 December 2019

Includes investments held in both the investment and trading portfolios.

## Valued at Closing Prices at 31 December 2019

	Total Value \$ Million	% of Portfolio
1 Commonwealth Bank of Australia	631.2	8.0
2 CSL	584.7	7.5
3 BHP Group*	524.7	6.7
4 Westpac Banking Corporation*	387.3	4.9
5 Transurban Group	341.2	4.3
6 Macquarie Group	299.1	3.8
7 Wesfarmers	285.6	3.6
8 National Australia Bank*	267.9	3.4
9 Australia and New Zealand Banking Group	226.3	2.9
10 Woolworths Group	204.9	2.6
11 Rio Tinto	195.3	2.5
12 Amcor	195.0	2.5
13 James Hardie Industries	169.0	2.2
14 Sydney Airport	167.7	2.1
15 Telstra Corporation*	156.0	2.0
16 Woodside Petroleum*	153.0	1.9
17 Brambles	142.3	1.8
18 Mainfreight	133.3	1.7
19 Oil Search*	132.9	1.7
20 Ramsay Health Care	129.1	1.6
21 Sonic Healthcare	116.6	1.5
22 Qube Holdings	115.0	1.5
23 Coles Group*	105.6	1.3
24 Seek	99.7	1.3
25 Treasury Wine Estates	88.5	1.1
<b>Total</b>	<b>5,851.9</b>	

As percentage of total portfolio value (excludes cash)

74.6%

\* Indicates that options were outstanding against part of the holding.

# Income Statement

For the Half-Year Ended 31 December 2019

	<b>Half-Year 2019 \$'000</b>	Half-Year 2018 \$'000
Dividends and distributions	153,929	246,708
Revenue from deposits and bank bills	1,109	1,136
Net gains/(losses) on trading portfolio	6,628	4,187
Other revenue	21	-
<b>Total income</b>	<b>161,687</b>	252,031
Finance costs	(462)	(400)
Administration expenses	(3,874)	(3,850)
<b>Profit before income tax</b>	<b>157,351</b>	247,781
Income tax	(11,250)	(7,977)
<b>Profit for the half-year</b>	<b>146,101</b>	239,804
	<b>Cents</b>	Cents
Earnings per share	12.10	20.11

# Balance Sheet

As at 31 December 2019

	<b>31 Dec 2019 \$'000</b>	30 June 2019 \$'000
<b>Current assets</b>		
Cash	179,024	206,429
Receivables	13,276	40,128
<b>Total current assets</b>	<b>192,300</b>	<b>246,557</b>
<b>Non-current assets</b>		
Investment portfolio	7,847,853	7,572,640
Deferred tax assets	1,076	-
<b>Total non-current assets</b>	<b>7,848,929</b>	<b>7,572,640</b>
<b>Total assets</b>	<b>8,041,229</b>	<b>7,819,197</b>
<b>Current liabilities</b>		
Payables	4,777	932
Tax payable	27,024	17,052
Borrowings – bank debt	-	-
Trading portfolio	2,810	7,033
Provisions	3,412	4,114
<b>Total current liabilities</b>	<b>38,023</b>	<b>29,131</b>
<b>Non-current liabilities</b>	<b>1,064</b>	<b>1,471</b>
Provisions	-	100
Deferred tax liabilities – investment portfolio	1,210,069	1,163,749
<b>Total non-current liabilities</b>	<b>1,211,133</b>	<b>1,165,320</b>
<b>Total liabilities</b>	<b>1,249,156</b>	<b>1,194,451</b>
<b>Net assets</b>	<b>6,792,073</b>	<b>6,624,746</b>
<b>Shareholders' equity</b>		
Share capital	2,922,517	2,888,186
Revaluation reserve	2,717,547	2,561,314
Realised capital gains reserve	398,444	462,257
General reserve	23,637	23,637
Retained profits	729,928	689,352
<b>Total shareholders' equity (including minority interests)</b>	<b>6,792,073</b>	<b>6,624,746</b>

## Summarised Statement of Changes in Equity

For the Half-Year Ended 31 December 2019

	<b>Half-Year 2019 \$'000</b>	Half-Year 2018 \$'000
Total equity at the beginning of the half-year	<b>6,624,746</b>	6,339,260
Dividends paid	(164,150)	(162,800)
Dividend Reinvestment Plan	34,407	33,099
Other share capital adjustments	(76)	(65)
<b>Total transactions with shareholders</b>	<b>(129,819)</b>	(129,766)
Profit for the half-year	146,101	239,804
Revaluation of investment portfolio	219,411	(745,125)
Provision for tax on revaluation	(68,366)	215,197
Revaluation of investment portfolio (after tax)	151,045	(529,928)
<b>Total comprehensive income for the half-year</b>	<b>297,146</b>	(290,124)
Realised gains/(losses) on securities sold	16,857	71,462
Tax expense on realised gains/(losses) on securities sold	(22,045)	(24,803)
<b>Net realised gains/(losses) on securities sold</b>	<b>(5,188)</b>	46,659
Transfer from revaluation reserve to realised gains reserve	5,188	(46,659)
<b>Total equity at the end of the half-year</b>	<b>6,792,073</b>	5,919,370

A full set of AFIC's interim accounts are available on the Company's website.

# Holdings of Securities

As at 31 December 2019

Individual investments for the combined investment and trading portfolios as at 31 December 2019 are listed below. The list should not, however, be used to evaluate portfolio performance or to determine the net asset backing per share at other dates. Net asset backing is advised to the Australian Securities Exchange each month and is recorded on the toll free telephone service at 1800 780 784 and posted to AFIC's website [afi.com.au](http://afi.com.au)

Individual holdings in the portfolios may change during the course of the year. In addition, holdings which are part of the trading portfolio may be subject to call options or sale commitments by which they may be sold at a price significantly different from the market price prevailing at the time of the exercise or sale.

Code	Ordinary Shares, Trust Units or Stapled Securities	Number Held '000	Market Value \$'000
ABC	Adelaide Brighton	7,262	25,127
AGL	AGL Energy	1,100	22,583
AIA	Auckland International Airport	1,770	15,063
ALQ	ALS	7,542	69,237
AMC	Amcor	12,527	195,049
ANN	Ansell	1,284	37,271
ANZ	Australia and New Zealand Banking Group	9,188	226,293
APA*	APA Group	6,540	72,293
APE	AP Eagers	1,157	11,844
ARB	ARB Corporation	3,470	65,126
ASX	ASX	807	63,291
AUB	AUB Group	2,166	25,968
AWC*	Alumina	19,158	43,222
BHP*	BHP	13,482	524,707
BKW	Brickworks	1,854	34,626



## Holdings of Securities continued

As at 31 December 2019

Code	Ordinary Shares, Trust Units or Stapled Securities	Number Held '000	Market Value \$'000
BXB	Brambles	12,139	142,265
CAR	Carsales.com	4,191	69,613
CBA	Commonwealth Bank of Australia	7,900	631,210
COH	Cochlear	147	33,035
COL*	Coles Group	7,143	105,600
CPU	Computershare	4,660	78,195
CSL	CSL	2,120	584,697
CWY	Cleanaway	23,893	48,026
DJW	Djerriwarrh Investments	7,505	27,470
DUI	Diversified United Investment	12,030	59,910
EQT	EQT Holdings	1,322	40,640
EVT	Event Hospitality and Entertainment	1,030	14,012
FNP	Freedom Foods Group	5,162	26,326
FPH	Fisher & Paykel Healthcare Corporation	3,800	80,180
FRE	Freightways (NZX listed)	1,650	13,464
GMG	Goodman Group	5,958	79,658
IAG*	Insurance Australia Group	6,157	47,110
IRE	IRESS	5,472	71,349
IVC	InvoCare	1,920	25,320
JHX	James Hardie Industries	6,065	169,032
LIC	Lifestyle Communities	2,776	25,570

Code	Ordinary Shares, Trust Units or Stapled Securities	Number Held '000	Market Value \$'000
LLC	Lendlease	1,285	22,624
MFT	Mainfreight (NZX listed)	3,268	133,293
MIR	Mirrabooka Investments	8,728	23,565
MLT	Milton Corporation	10,841	53,557
MPL	Medibank Private	2,000	6,320
MQG	Macquarie Group	2,170	299,071
NAB*	National Australia Bank	10,885	267,907
NXT	NEXTDC	5,580	36,716
ORG	Origin Energy	6,500	54,925
ORI	Orica	1,970	43,301
OSH*	Oil Search	18,385	132,929
QUB	Qube Holdings	34,962	115,025
REA	REA Group	384	39,778
REH	Reece	6,227	71,360
RHC	Ramsay Health Care	1,780	129,103
RIO	Rio Tinto	1,946	195,330
RMD	ResMed	3,935	86,177
RWC	Reliance Worldwide Corporation	16,902	68,284
RYM	Ryman Healthcare (NZX listed)	855	13,391
S32	South32	16,741	45,201
SCG*	Scentre Group	14,450	55,299

## Holdings of Securities continued

As at 31 December 2019

Code	Ordinary Shares, Trust Units or Stapled Securities	Number Held '000	Market Value \$'000
SEK	Seek	4,420	99,663
SHL	Sonic Healthcare	4,054	116,559
SUN*	Suncorp Group	4,700	60,745
SYD	Sydney Airport	19,364	167,694
TCL	Transurban Group	22,887	341,242
TLS*	Telstra Corporation	44,075	155,961
TPM	TPG Telecom	2,500	16,775
TWE	Treasury Wine Estates	5,450	88,508
WBC*	Westpac Banking Corporation	15,985	387,286
WES	Wesfarmers	6,898	285,557
WOW	Woolworths	5,667	204,909
WPL*	Woodside Petroleum	4,460	152,972
XRO	Xero	871	69,640
<b>Total</b>			<b>7,845,043</b>

\* Part of the security was subject to call options written by the Company.

## Major Transactions in the Investment Portfolio

Acquisitions	Cost \$'000
Goodman Group	45,608
Macquarie Group	26,588
Cleanaway Waste Management	25,885
Lendlease Group*	21,624
CSL	17,737

\* New holding.

Disposals	Proceeds \$'000
National Australia Bank (due to the exercise of call options)	52,680
Dulux Group (Taken over by Nippon Paint)#	29,683
Perpetual#	23,212
Boral#	21,989
Orora#	19,322
Link Administration#	17,958
Lifestyle Communities	17,028
AMP#	15,913
Iluka Resources#	15,788

# Complete disposal from the portfolio.

### New Companies Added to the Investment Portfolio

Lendlease Group

Ryman Healthcare

# Company Particulars

**Australian Foundation Investment Company Limited (AFIC)**  
ABN 56 004 147 120

## Directors

John Paterson, Chairman  
Robert M Freeman, Managing Director  
Ross E Barker  
Rebecca Dee-Bradbury  
Graeme R Liebelt  
David A Peever  
Catherine M Walter AM  
Peter J Williams

## Company Secretaries

Matthew J Rowe  
Andrew JB Porter

## Auditor

PricewaterhouseCoopers  
Chartered Accountants

## Country of Incorporation

Australia

## Registered Office and Mailing Address

Level 21, 101 Collins Street  
Melbourne Victoria 3000

## Contact Details

Telephone (03) 9650 9911  
Facsimile (03) 9650 9100  
Website [afi.com.au](http://afi.com.au)  
Email [invest@afi.com.au](mailto:invest@afi.com.au)

For enquiries regarding net asset backing (as advised each month to the Australian Securities Exchange):

**Telephone** 1800 780 784 (toll free)

## Share Registrar

**Australia**  
Computershare Investor Services Pty Ltd  
Yarra Falls, 452 Johnston Street  
Abbotsford Victoria 3067

## New Zealand

Computershare Investor Services Limited  
159 Hurstmere Road  
Takapuna Auckland 0622

## Shareholder

**Enquiry Lines** 1300 662 270  
0800 333 501  
(within New Zealand)  
+61 3 9415 4373  
(from overseas)  
**Facsimile** (03) 9473 2500  
**Website** [investorcentre.com/au/contact](http://investorcentre.com/au/contact)

For all enquiries relating to shareholdings, noteholdings, dividends and related matters, please contact the share registrar as above.

## Australian and New Zealand Securities

### Exchange Codes

**AFI** Ordinary shares (ASX and NZX)



# Shareholder Meetings

## Melbourne Shareholder Meeting

**Time** 10.00am  
**Date** Tuesday 17 March 2020  
**Venue** ZINC Federation Square  
**Location** Corner of Swanston Street and Flinders Street  
Melbourne

## Sydney Shareholder Meeting

**Time** 10.00am  
**Date** Friday 20 March 2020  
**Venue** Wesley Conference Centre  
**Location** 220 Pitt Street  
Sydney

## Canberra Shareholder Meeting

**Time** 10.00am  
**Date** Monday 23 March 2020  
**Venue** Hyatt Hotel Canberra  
**Location** 120 Commonwealth Avenue  
Yarralumla

## Adelaide Shareholder Meeting

**Time** 10.00am  
**Date** Friday 27 March 2020  
**Venue** Adelaide Convention Centre  
**Location** Panorama Rooms, North Terrace  
Adelaide

## Perth Shareholder Meeting

**Time** 10.00am  
**Date** Tuesday 31 March 2020  
**Venue** Pan Pacific Perth  
**Location** 207 Adelaide Terrace  
Perth

