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Woodhall's 2017 Investment Strategy

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We continue to favour a healthy tilt to currency hedging.

We are 76% currency hedged in our S&P 500 exposure in main portfolio
We continue to be about 50:50 re the ASX 200 and the S&P 500
We are most overweight in the ASX in 1) Financials; 2) Materials; 3) Industrials

The forecasts

In the companion document on this site, 'Woodhall's 2017 Year Ahead, we set out 12 forecasts that guide our strategy.

The consequence of setting out reasonable lower bounds for the prices of oil and iron ore is our view that our dollar will not depreciate by a material amount and may well rise into the end of 2017.

We also produce model portfolios each month of Australian direct equities using broker forecasts of dividends and earnings together with proprietary software for producing volatility forecasts and optimisation of sector weights.

We plan to rebalance the portfolio between six and 12 months from the last rebalance date (on 3rd October 2016). The timing of the next rebalance depends on a variety of forecasts including a comparison between the stocks, weights and consensus recommendations in the legacy portfolio and those in each monthly potential update.

Minor adjustments to portfolios may be made from time to time. Proprietary timing measures may be used to go to cash when the market – or specified sectors – seems precariously overpriced. The same mispricing measures are to be used to get back into equities when it is deemed appropriate.

Hedging

We have hedged our currency exposure in our 'ungeared portfolio' by holding a hedged ETF (IHVV) at 76% and an unhedged ETF (IVV) at 24%. Both ETFs track the S&P 500.

The hedging ratio for our geared strategy (see the Weekly for details) is 63%. We choose to take on more risk in this strategy than the one designed to produce a pension.

If our dollar stays above 70c (as we predict) we do not plan to change the hedging ratio until it starts to rise above 75c. At that point, we plan to make progressive steps to increase the hedging ratio. If it falls below 70c we will start to take on more hedging if the dollar starts to rise again. Since we don't actively manage currencies, we implicitly have a channel of 70c-75c that we see as being consistent with our current hedging ratio.

We have a significant cash holding (8%) in our ungeared portfolio which may be used to buy IHVV so as to increase the hedging ratio and the US exposure as deemed appropriate.

Foreign exposure

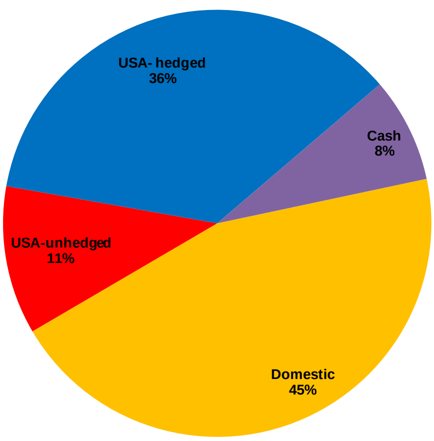
At this point we only consider the S&P 500 ETFs for our foreign exposure.

The foreign exposure naturally changes over time through price movements as we do not actively manage this exposure.

The last rebalance was made when some of the domestic exposure was set to cash at the October 3rd rebalance with a view to looking for opportunities a little later. As the Presidential election took hold, it was decided to keep the cash specifically to exploit any perceived mispricing due to volatility flowing from the polling and the election results.

Two parcels of IVV (unhedged) were bought on the Friday (4th November) before and the Wednesday (9th November) of the election. That increased our foreign exposure to 51% - excluding assigning the cash allocation of 8% - by the end of 2016 as shown in Chart 1.

Chart 1: Asset allocation



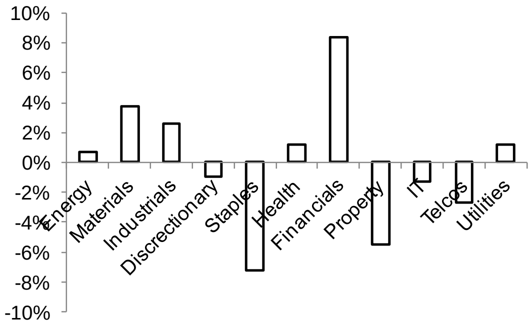
Our geared strategy was 50% the ASX 200 and 50% in the S&P 500.

The large cash holding is designed to allow us take advantage of any volatility in January and early February due to the Presidential Inauguration on January 20th and the FOMC meeting few days later on January 31st – February 1st. At this point, the plan is to reduce cash to about 3% in February by placing this cash in the S&P 500 ETFs as we forecast much stronger capital gains in that market.

Sectoral tilts

The sectoral tilts in our ASX 200 direct equity portfolios in Chart 2 show large over-weight exposures to Financials, Materials and Industrials. The defensive sectors of Staples, Property and Telcos are the most underweight.

Chart 2: Sectoral tilts



The Materials' position (+3.7 percentage points) was largely due to the weights produced in the optimisation process for the October 3rd rebalance.

The Financials' position (+8.4% percentage points) was also materially affected by a purchase from cash of CBA on November 29th which then became the largest stock holding. This play was opportunistic based on changes in the Reuters data we use and the rhetoric around Trump's possible policies.

Stock holdings

The component stocks are shown in the Chart 3. There were 22 stocks held at eoy 2016. A small portion of the 8% is planned to be used to take up the Santos (STO) offer in January.

Chart 3: Stock holdings