


The Shield of Valuation

Defending your Retirement Wealth

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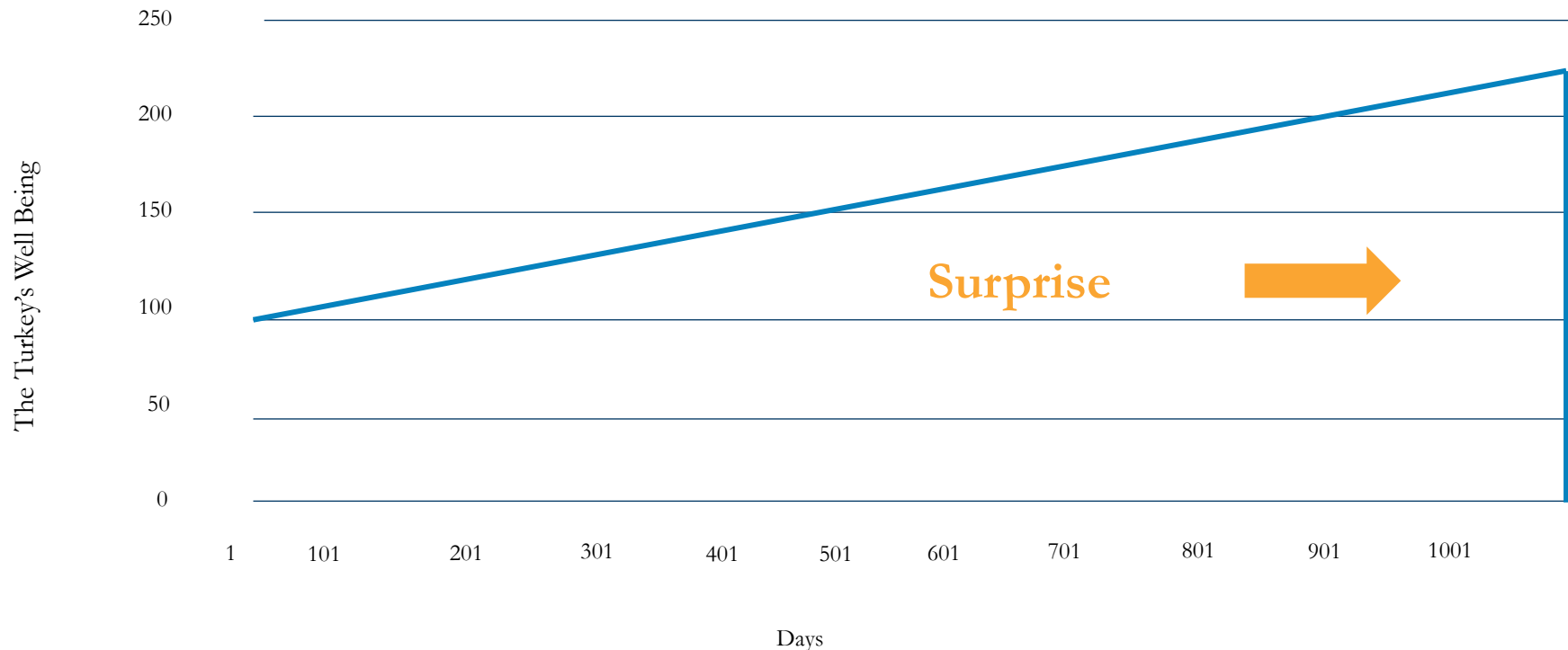


Valuation: Where are we and why does it matter?

What Benefits Can Valuation Awareness Bring to a Portfolio?

The Curse of Complacency

1001 Days in the Life of a Thanksgiving Turkey



Source: This example has been used previously by Nassim Nicholas Taleb.

To know where you're going, evaluate
where you are.

Rick Warren

If you don't know where you are going,
you'll end up someplace else.

Yogi Berra

The Importance of Cycle Adjusted Earnings

The **Cycle Adjusted Price to Earnings Ratio (CAPE)**

CAPE is today's price relative to the average earnings across the cycle in today's dollars. In order to average both booms and busts, a 10 year average is often used (CAPE10).

High Multiples on a Cycle Adjusted Basis

US 10 Year Cycle Adjusted P/E

P/E

50

40

30

20

10

0

1881

1901

1921

1941

1961

1981

2001

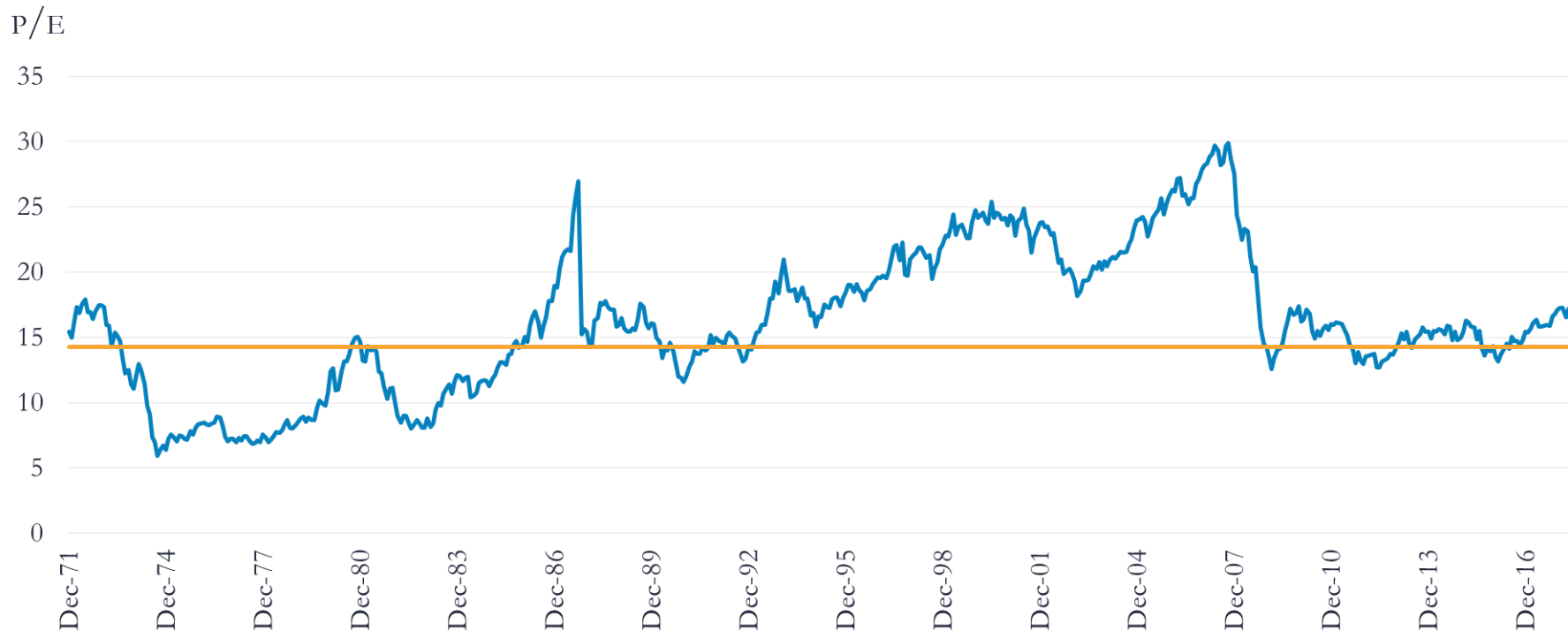
2018

US CAPE10 and Harmonic Mean (orange): Jan 1871 to May 2018. This information is for illustrative purposes only and does not represent any product or strategy managed by Lazard.

Source: Robert Shiller, <http://www.econ.yale.edu/~shiller/data.htm>

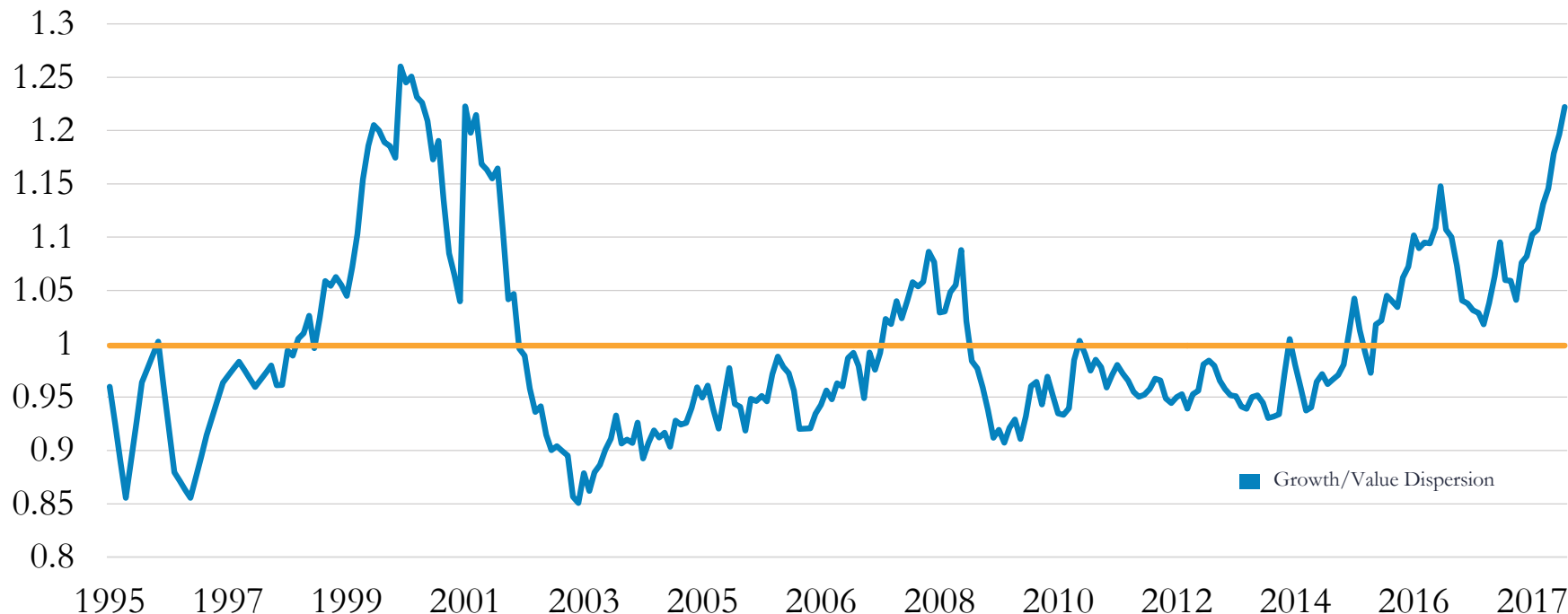
Australian CAPE Slightly Above Average

Australian 10 Year Cycle Adjusted P/E



Tech Boom Mark II: The Market is Getting Frothy

Value Opportunities



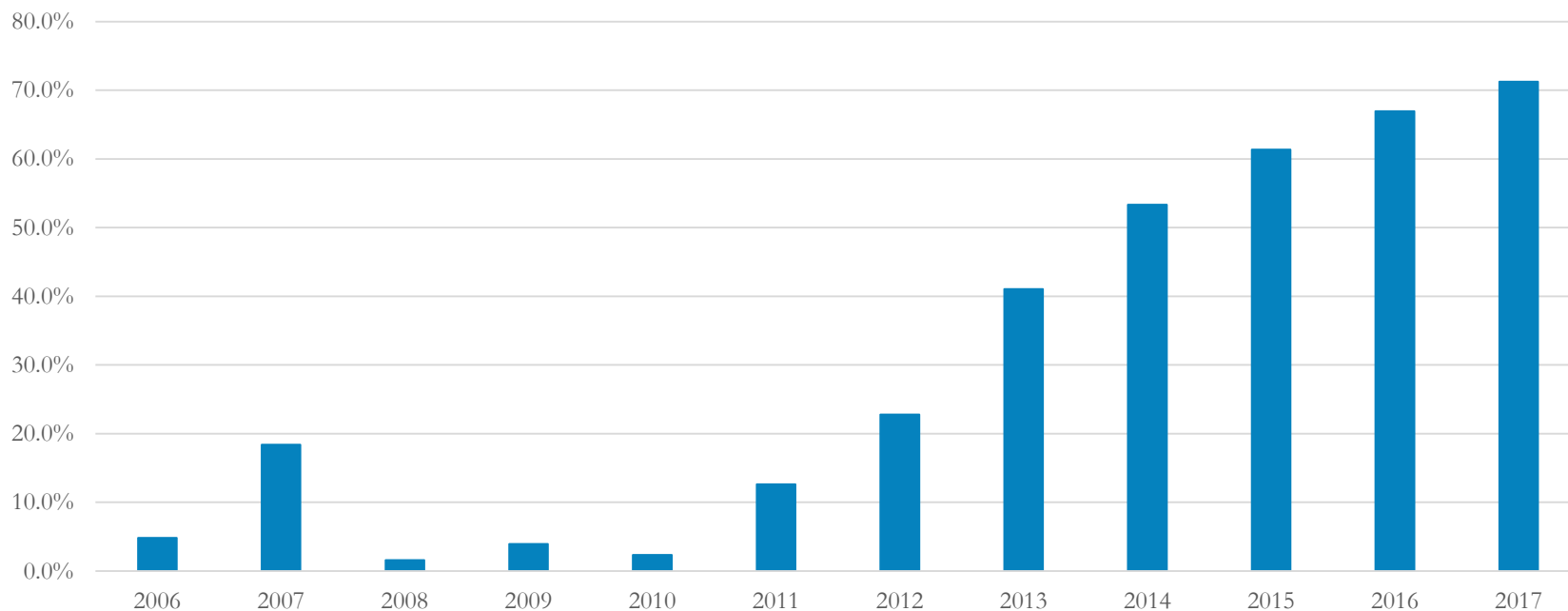
Source: Lazard Asset Management and Macquarie. As at 30 June 2018. Source: Average for normalised deviations from trend for six series. 1. Relative P/E multiple of top quintile growth firms (ASX200, GS). 2. Number of ASX200 stocks trading on >40x trailing P/E (GS). 3. Ratio of 20th to 80th percentile P/E (UBS, ASX200). 4. Ratio of P/E of highest quintile P/E stocks relative to Avg Industrial P/E (UBS, ASX200). 5. Relative P/E of Australian "Darling" stocks compared to average (CSFB definition of "Darlings" includes PE and price momentum, ASX200). 6. Lazard's weighted standard deviation of expected returns.

Interest Rates are not at Equilibrium Levels

	In this cycle rates reached a	Latest Change in CPI (yoy)	Inflation Target	Today's Cash Rate	Today's 10Yr Bond Yield
US	>220 yr low	2.9%	About 2%	1.75% - 2.00%	2.85%
Japan	>1,000 yr low	0.8%	2%	-0.10%	0.10%
Germany	>500 yr low	2.1%	Under 2%	0.00%	0.32%
UK	>500 yr low	2.4%	2%	0.75%	1.53%
Australia	>130 yr low	1.9%	2% to 3%	1.50%	2.58%

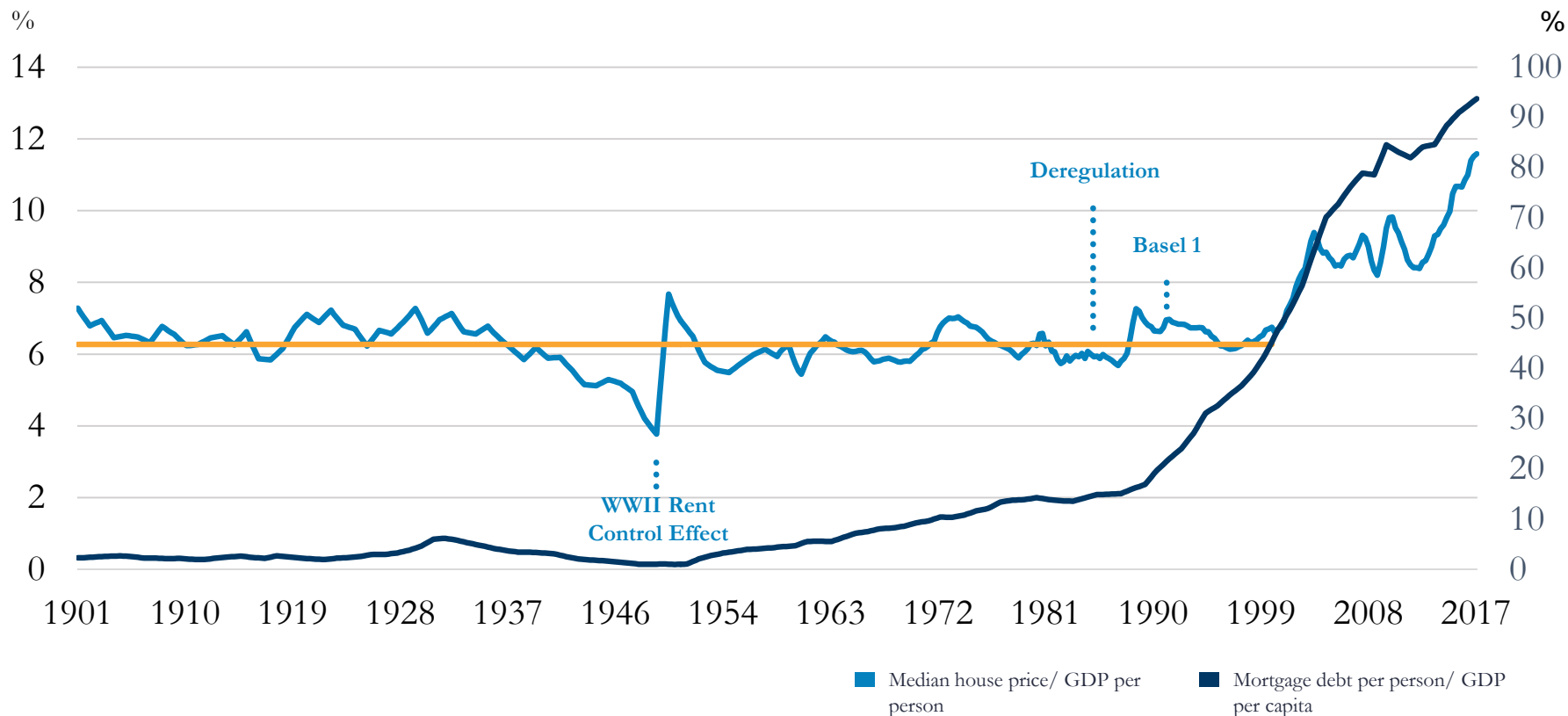
Corporate Credit Standards More Lax Than in 2007

Covenant Lite Lending (% of new loans, average of US and Europe)



Availability and Appetite for Debt has Driven House Prices

Aus. Median House Price/GDP per Capita (LHS) (1901-2000 Avg) and Mortgage Debt per Person/GDP per Capita (RHS)



A Comparison with the Stock Market

Valuation Analysis of Australian Residential Property Vs Other Asset Classes

Fully Equity Funded	Home	Unit
Gross Yield	3.1%	4.1%
Costs	1.1%	1.3%
Net Yield	2.0%	2.8%
Tax	0.6%	0.8%
NPAT Yield	1.4%	2.0%
P/E Ratio	70x	50x

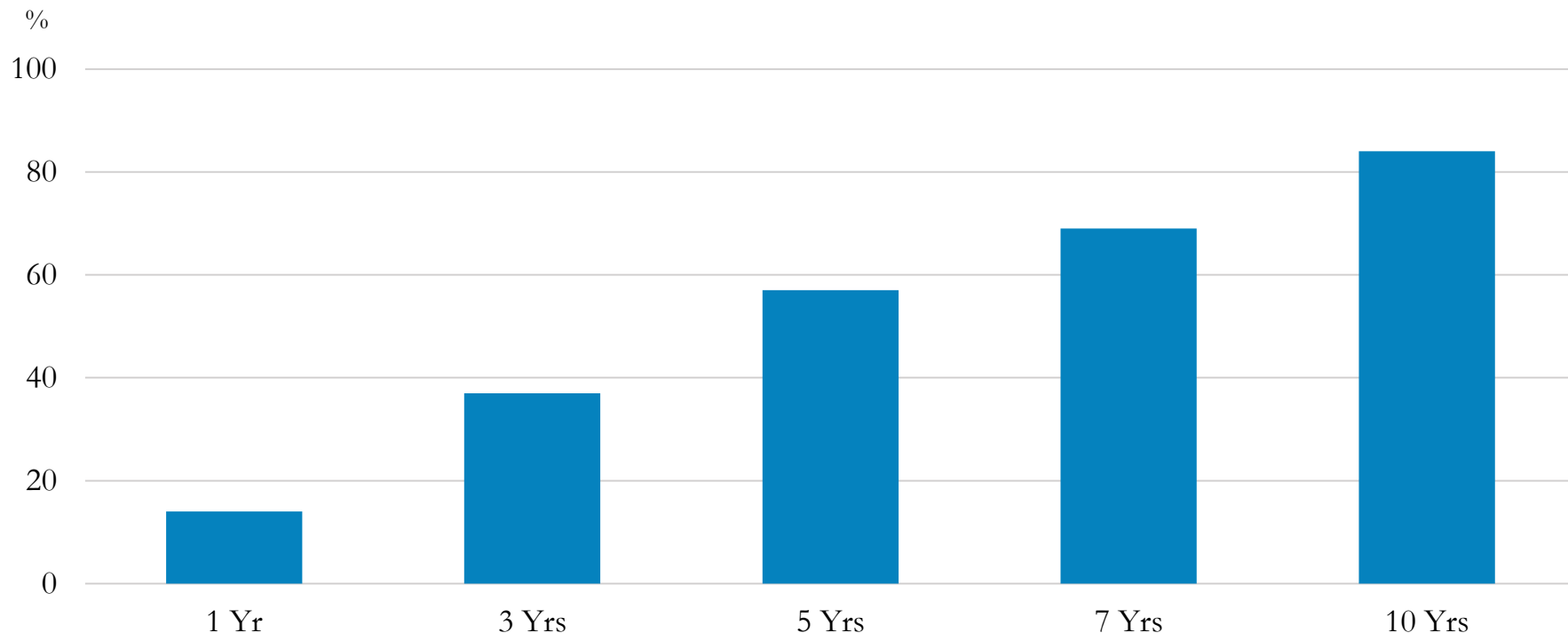
Net Yield	2001-17	2017
Prime Office	7.0%	5.6%
Prime Industrial	8.0%	6.2%
Retail	7.0%	5.6%
US Apartments	6.5%	5.4%
US Homes	7.3%	5.6%

After a long bull market in almost everything, assets are generally expensive



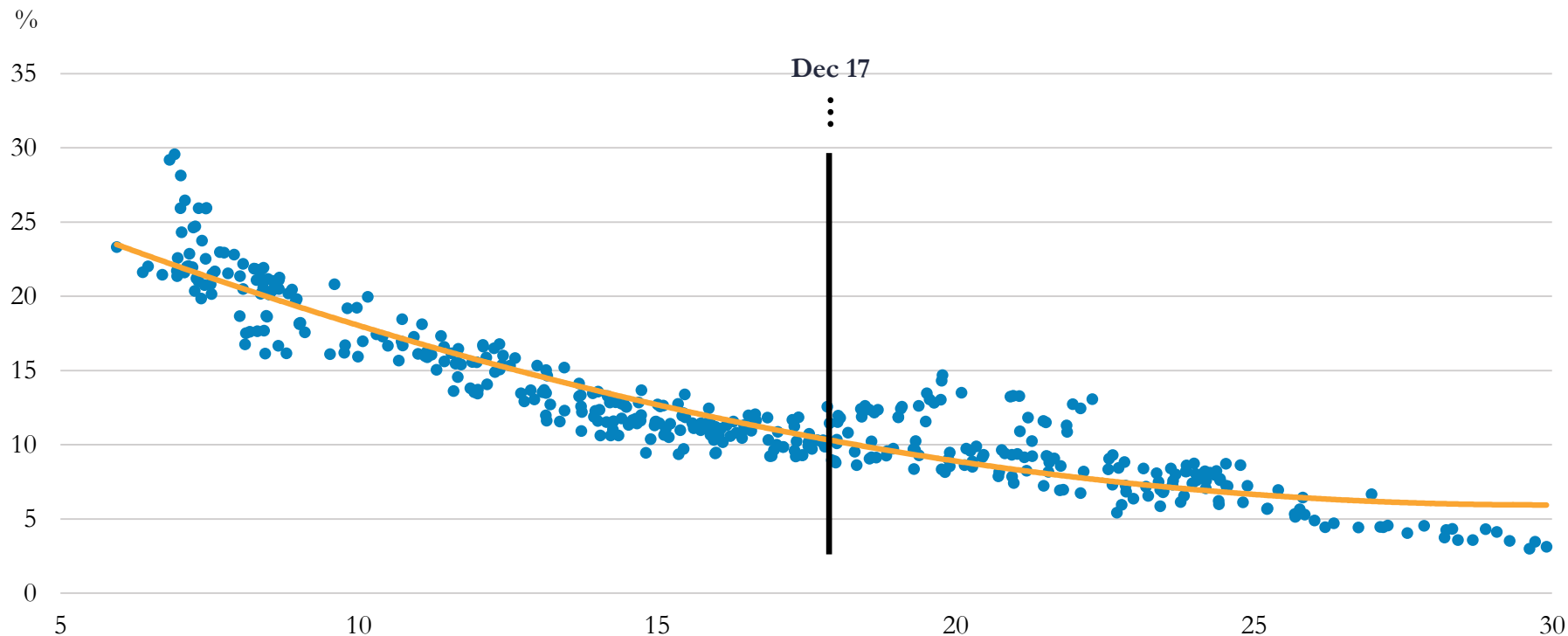
Valuation Matters Over the Long-Term

R-squared: Aus. CAPE10 and Subsequent 10 Year Total Returns over different return horizons

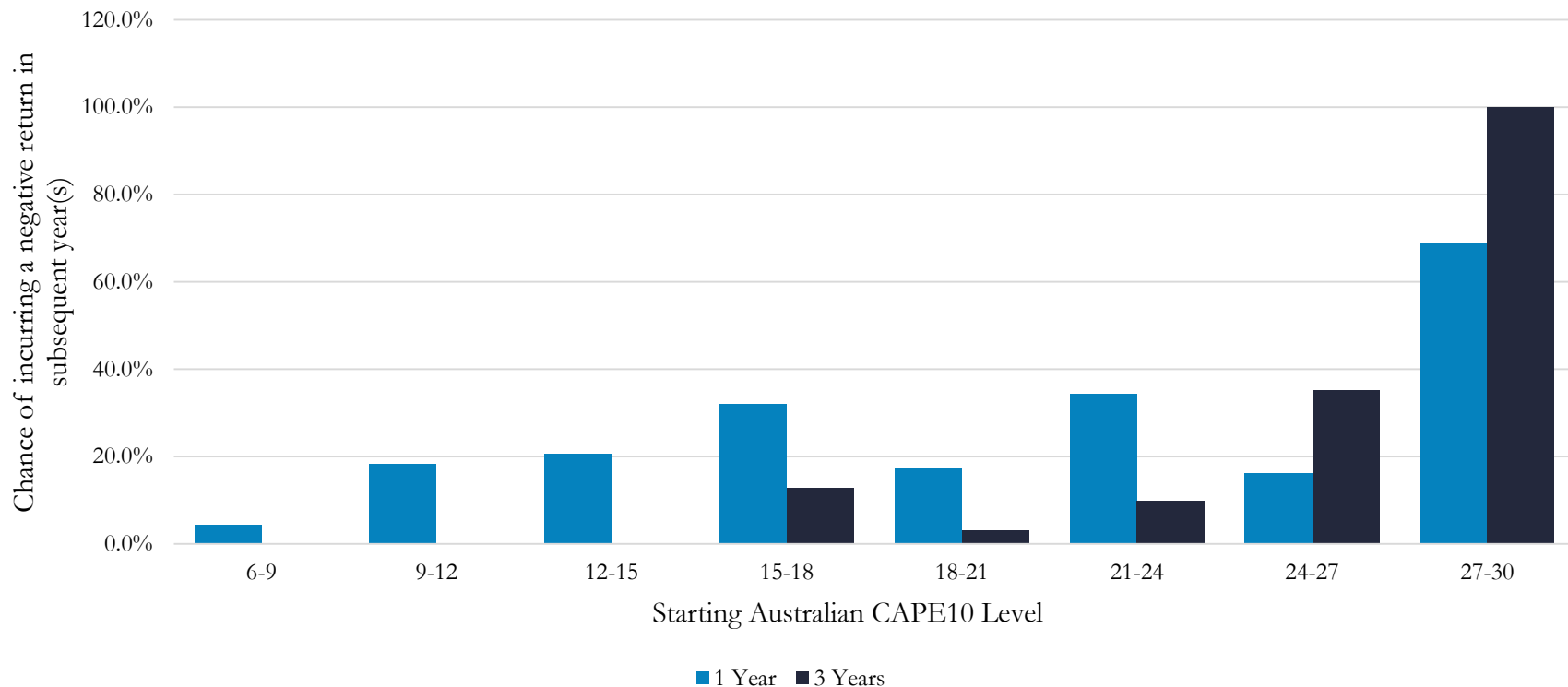


Valuation Matters Over the Long-Term

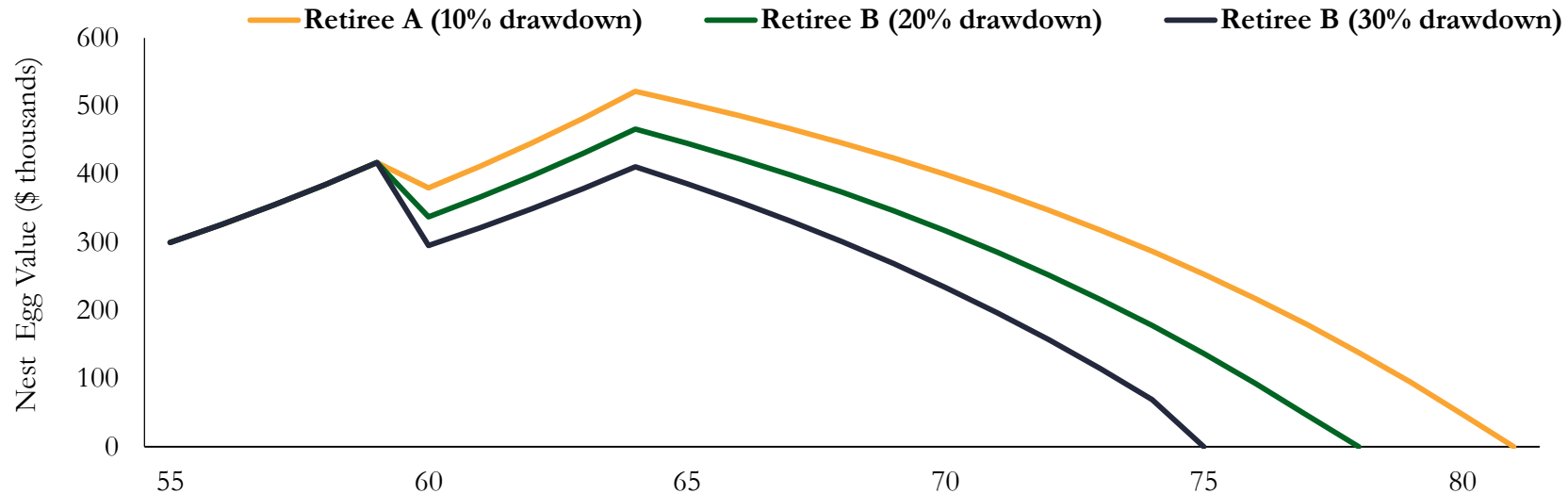
10Yr CAPE (x) and Subsequent 10 Year Nominal Returns (y)



High CAPE Increases Chance of a Negative Return



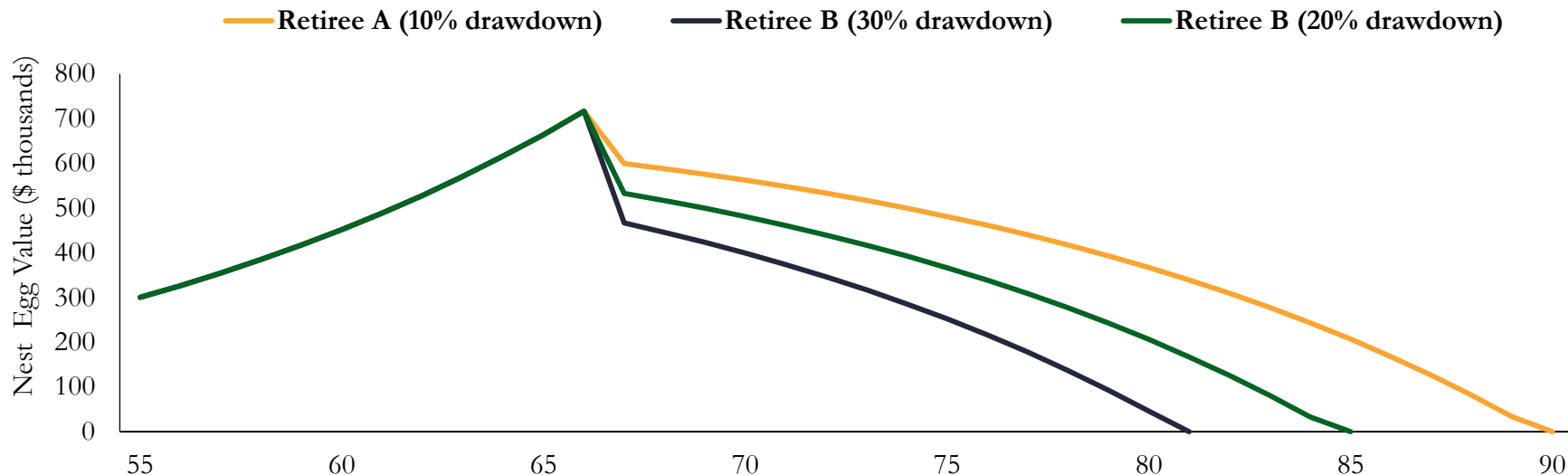
Defending During Accumulation Stage



- The Respective Drawdowns happen at age 59
- Assumes two retirees A and B who both contribute \$5,000 annually to their nest egg before retirement and then withdraw \$50,000 annually when they retire from 65 years of age
- Each of them are exposed to investment returns of 7% per annum

Limiting Drawdown Key to Wealth Preservation

Sequencing Risk




- The Respective Drawdowns happen at age 66
- Assumes two retirees A and B who both contribute \$5,000 annually to their nest egg before retirement and then withdraw \$50,000 annually when they retire from 65 years of age
- Each of them are exposed to investment returns of 7% per annum



Valuations matter and
markets look stretched.

Limiting drawdown is key
to defending retirement
wealth. Drawdown risk
increases as valuation
become more expensive.



Valuation: Where are we and why does it matter?

What Benefits Can Valuation Awareness Bring to a Portfolio

Lazard Defensive Australian Equity Fund – Our Objectives



Less draw down in negative markets

Reduced exposure to
S&P/ASX200
Accumulation Index
drawdowns



Total Return

A total return that
exceeds the Reserve
Bank of Australia
Cash Rate

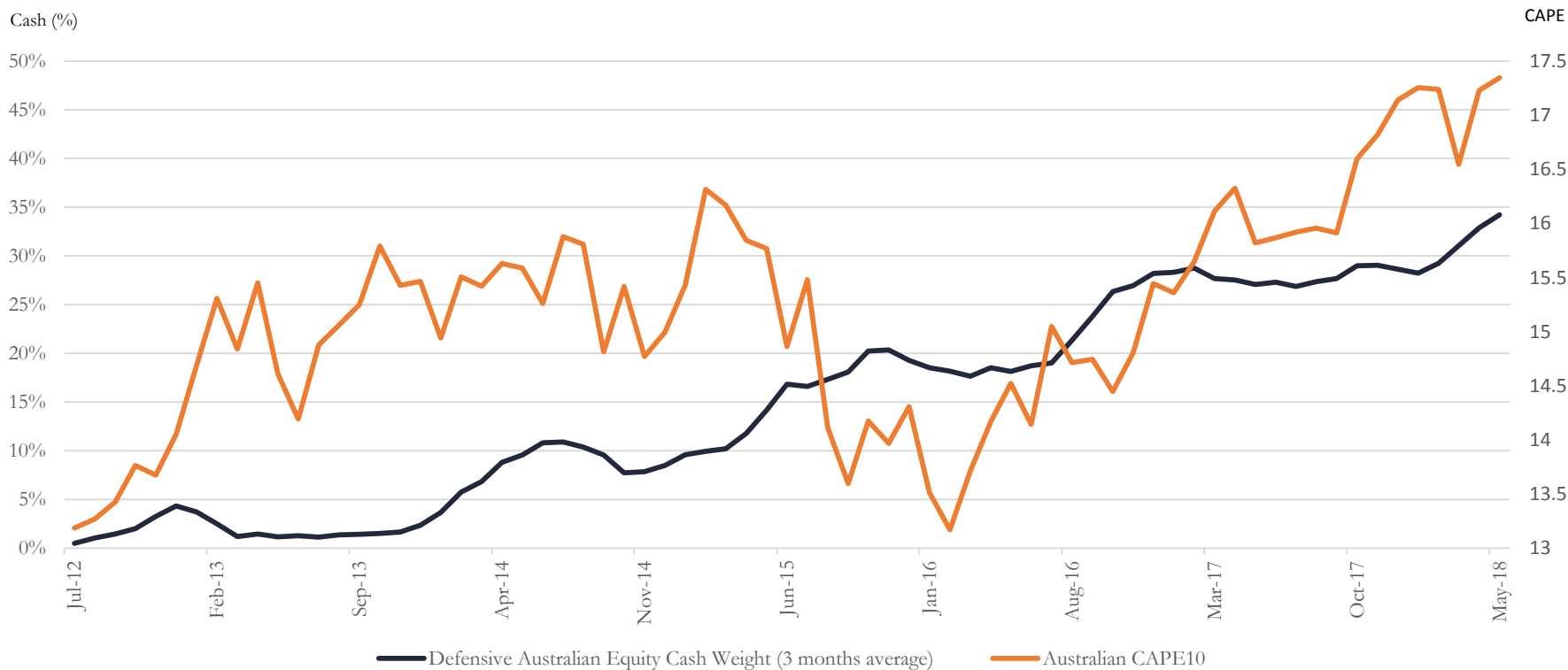


Sustainable and consistent income

An income return at a
premium to the
S&P/ASX200
Accumulation Index
dividend yield

Valuation Awareness in Practice

Cash Weight versus Australian CAPE10



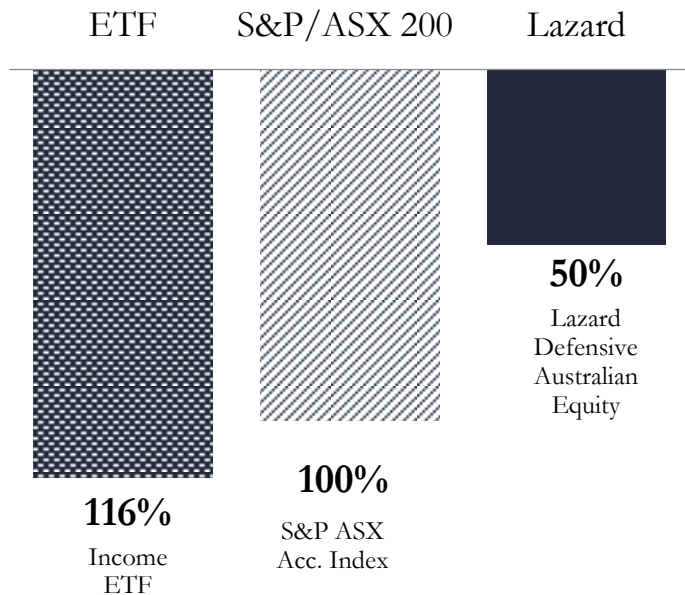
As at 30 September 2018.

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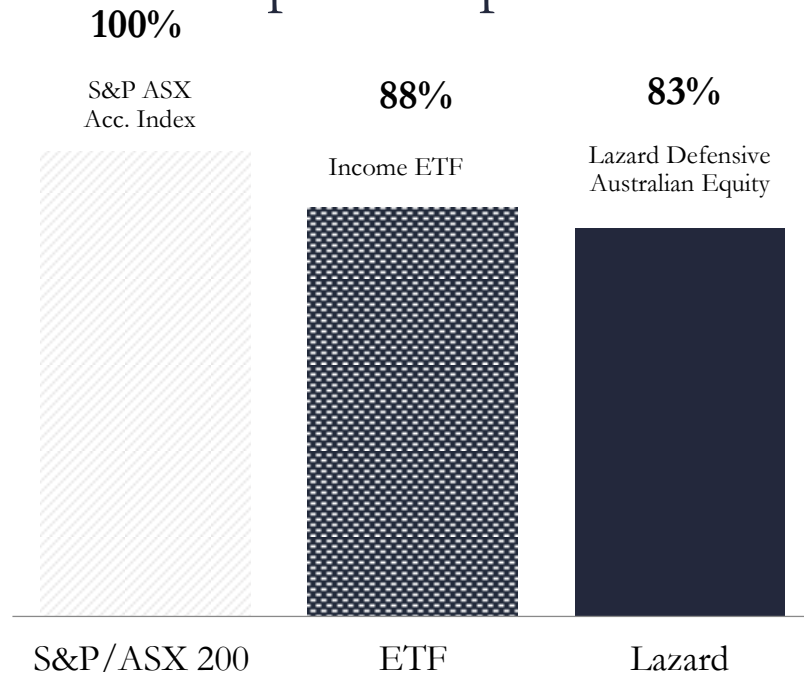
Source: Factset, Lazard Asset Management Pacific Co.

Performance in Different Markets

Downside Capture



Upside Capture

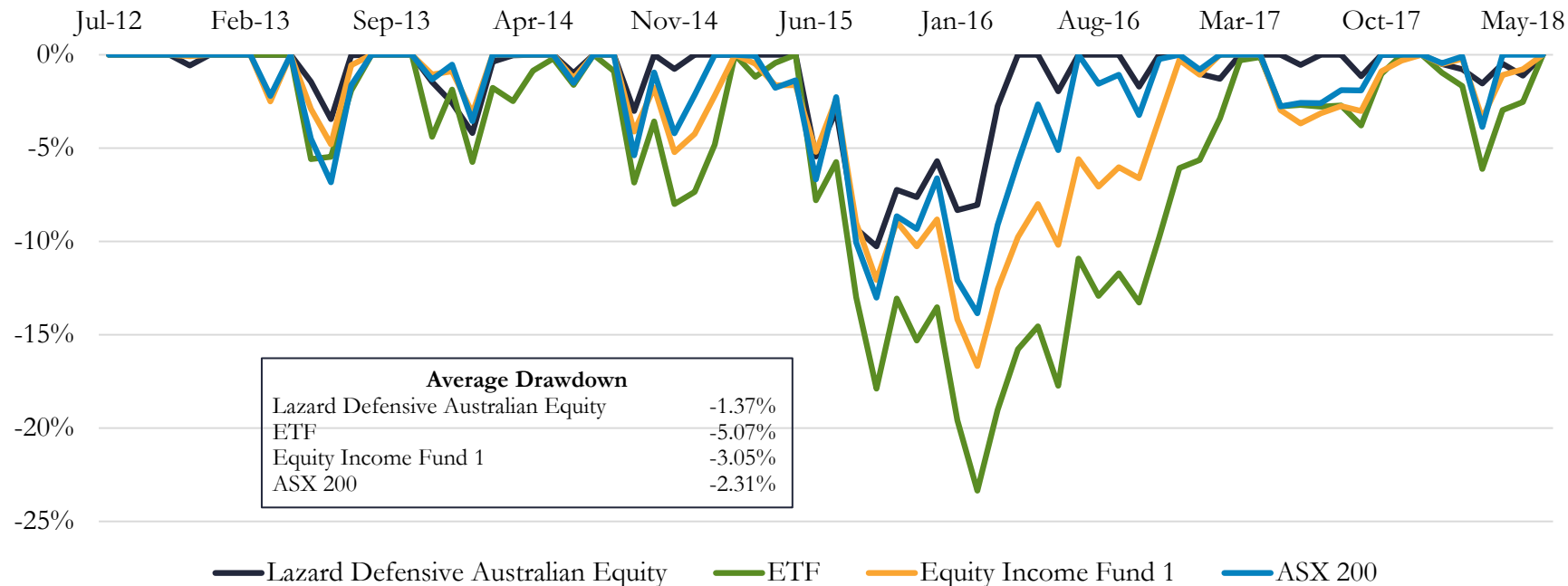


As of 30 June 2018. Upside Downside Capture for the period of August 2012 to June 2018. This information is for illustrative purposes only.

Historical Drawdown is calculated since inception and based on performance gross of all fees. Drawdown capture is a statistical measure of an investment manager's overall average performance in down markets, being calendar months where the [S&P/ASX 200 Accumulation Index] ("Index") experiences negative performance. A drawdown ratio (or percentage) of less than 100 (or 100%) reflects that the manager has outperformed the Index during such down markets.

Source: Lazard, Factset.

Cumulative Drawdown Since Inception



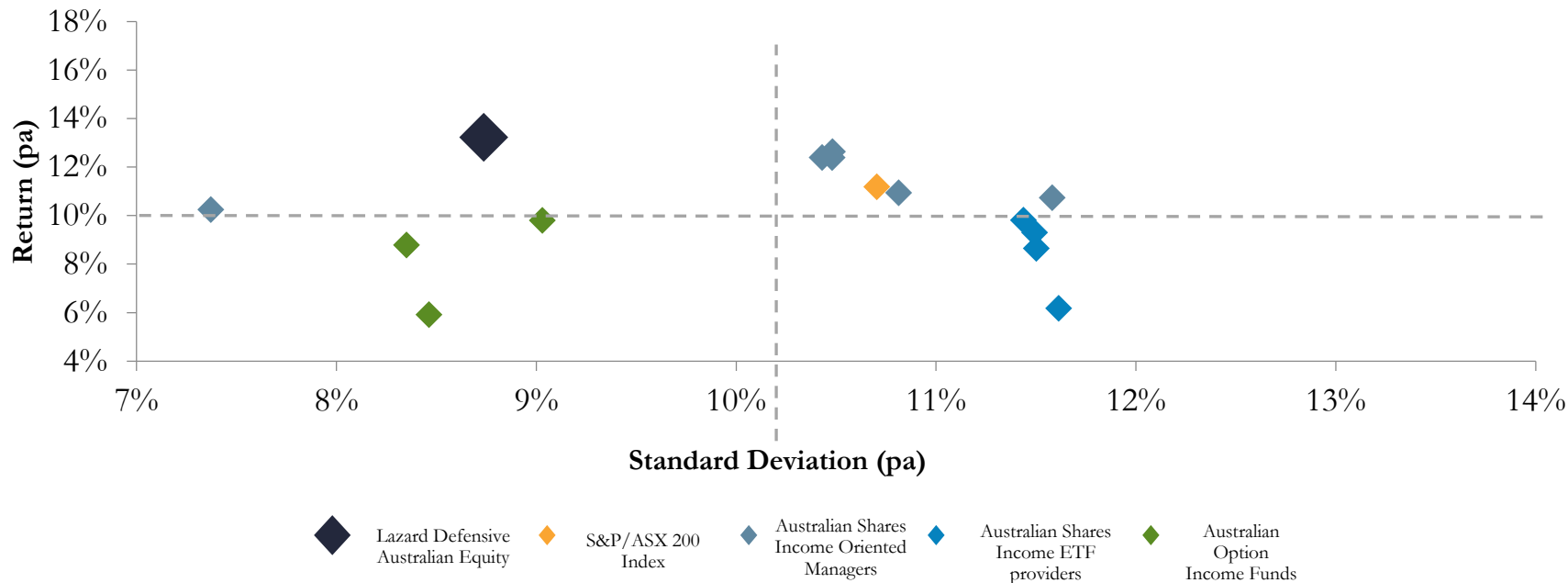
As of 30 June 2018.

Chart shows cumulative drawdown calculated from the first full month of performance, which is August 2012. Competitors have been defined by Lazard. Performance is calculated gross of fees. Past performance may not be indicative of future results. Historical Drawdown is calculated since inception and based on performance gross of all fees. Drawdown capture is a statistical measure of an investment manager's overall average performance in down markets, being calendar months where the [S&P/ASX 200 Accumulation Index] ("Index") experiences negative performance. A drawdown ratio (or percentage) of less than 100 (or 100%) reflects that the manager has outperformed the Index during such down markets

Source: Lazard Asset Management Pacific Co., Morningstar.

Peer Comparison

Return and Standard Deviation



Source: MercerInsight MPA, Morningstar, Factset, Lazard Asset Management Pacific Co
Return and Standard Deviation in \$A (before fees) over 6 years ending 30 September 2018 (monthly calculations)
Australian Shares Income Managers sourced from MercerInsightMPA Australian Shares (Income-oriented) universe
Income ETF data sourced from Factset
The performance quoted represents past performance. Past performance is not a reliable indicator of future results
Australian Option Income Funds sourced from Morningstar

Performance Summary

Lazard Defensive Australian Equity Fund

Income Return – as at 31 October 2018

	3 Months (%)	1 Year (%)	3 Year pa (%)	5 Year pa (%)	Since Inception pa (%) ^
Income Return	1.7	4.3	4.6	4.6	4.8
Franking Return	0.4	0.8	1.3	1.3	1.6
Grossed-up Income Return	2.1	5.1	5.9	5.9	6.4
Rolling RBA Cash Rate	0.4	1.5	1.6	1.9	2.1
Excess	+1.7	+3.6	+4.3	+4.0	+4.3

Total Return – as at 31 October 2018

	3 Months (%)	1 Year (%)	3 Year pa (%)	5 Year pa (%)	Since Inception pa (%) ^
Capital Gains	-3.4	-2.5	3.1	2.4	7.1
Total Return (gross of fees)	-1.1	3.4	9.8	9.1	14.3
S&P/ASX 200 Accumulation Index	-5.9	2.9	8.2	6.0	10.4
Excess	+4.8	+0.5	+1.6	+3.1	+3.9

* Performance is calculated gross of fees. Past performance may not be indicative of future results. Unless otherwise stated, Fund performance is gross of fees and assumes reinvestment of all distributions. Income return is calculated on an accruals basis rather than a cash receipts basis. Monthly franking return represents the yield from franking credits accrued over the month (calculated as a percentage of the Fund balance). Franking returns for periods greater than one month are calculated as the sum of the monthly franking returns. Total return for any period is calculated as the sum of the income return, the franking return and the capital gains.

Source: Lazard Asset Management Pacific Co., FactSet, ASX.

^ Since Inception is as of 3 July 2012



Valuation matters.

Paying attention to
valuation can lower
volatility, limit drawdown
and ultimately defend
retirement wealth.

Lazard Defensive Australian Equity

Independently Rated By:



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