Magellan Global Equities Fund (Managed Fund)

ARSN: 603 395 302

ASX code: MGE

Fund Facts

Portfolio Manager	Hamish Douglass
Structure	ASX-quoted Global Equities Fund
Inception Date	2 March 2015
Management & Administration Fee[1]	1.35% per annum
Fund Size	AUD $768.2 million
Distribution Frequency	Annually at 30 June
Performance Fee[1]	10.0% of the excess return of the units of the Fund above the higher of the Index Relative Hurdle (MSCI World Net Total Return Index (AUD)) and the Absolute Return Hurdle (the yield of 10-year Australian Government Bonds). Additionally, the Performance Fees are subject to a high water mark.

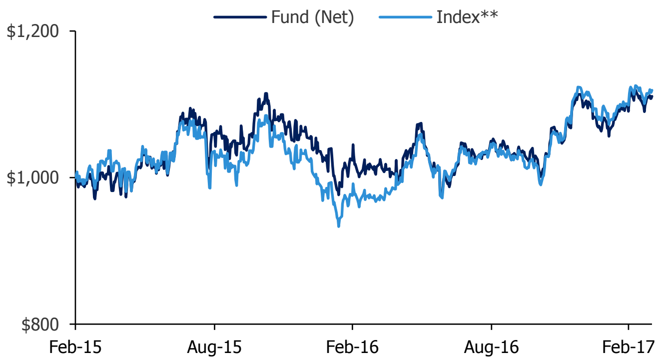
iNAV tickers			
	Bloomberg	MGE AU Equity	MGEIV Index
	Thomson Reuters	MGE.AX	MGEin.IDCC
	IRESS	MGE.AXW	MGENAV.ETF

[1]All fees are inclusive of the net effect of GST

Fund Features

- ASX quoted version of Magellan Global Fund.
- Fund is actively managed
- Minimum administration for investors; no paperwork needed to trade
- Units can be bought or sold on the ASX like any other listed security
- Efficient and live pricing
- Provision of liquidity by the Fund
- Settlement via CHESS
- Magellan has significant investment alongside unit holders.

Performance Chart growth of AUD $1,000*



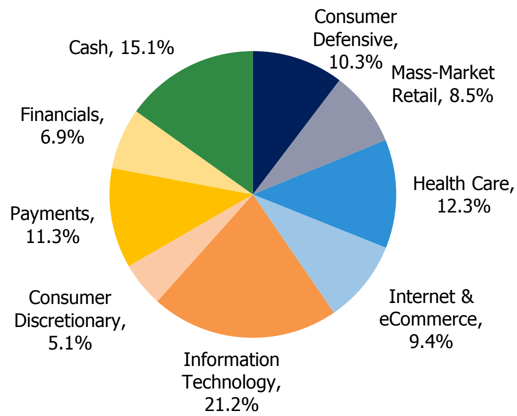
Fund Performance*

	Fund (%)	Index (%)**	Excess (%)
1 Month	1.9	1.9	0.0
3 Months	1.4	1.0	0.4
6 Months	7.5	8.7	-1.2
1 Year	10.6	15.7	-5.1
2 Years (% p.a.)	5.6	5.3	0.3
Since Inception (% p.a.)	5.2	5.6	-0.4

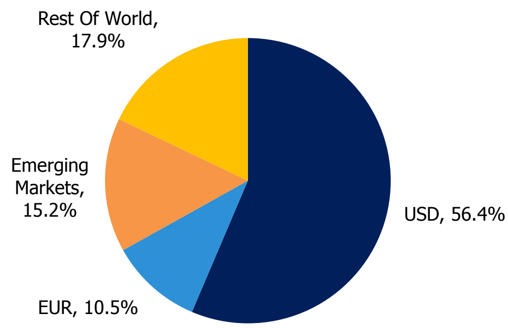
Top 10 Holdings

	Sector	%
Apple Inc	Information Technology	7.6
Alphabet Inc	Internet & eCommerce	5.4
Visa Inc	Payments	5.1
Lowe's Co Inc	Consumer Discretionary	5.1
Microsoft Corp	Information Technology	4.5
Wells Fargo & Co	Financials	4.3
eBay Inc	Internet & eCommerce	4.0
Facebook Inc-A	Information Technology	3.8
Oracle Corp	Information Technology	3.8
Nestle SA	Consumer Defensive	3.6
	TOTAL:	47.2

Sector Exposure by Source of Revenues#



Geographical Exposure by Source of Revenues#



* Calculations are based on the monthly ASX released net asset value with distributions reinvested, after ongoing fees and expenses but excluding individual tax, member fees and entry fees (if applicable). Fund Inception 2 March 2015.
** MSCI World Net Total Return Index (AUD).
# Sectors are internally defined. Geographical exposure is calculated on a look through basis based on underlying revenue exposure of individual companies held within the portfolio.

Market Commentary

Global stocks hit record highs as they rose for a fourth consecutive quarter during the first three months of 2017 as US companies posted higher-than-expected earnings, President Donald Trump's proposed pro-growth policies fanned optimism about the US economy and mainstream parties held off populists in the elections in the Netherlands.

US stocks rose as companies overall reported that higher revenue had boosted earnings-per-share growth. In March, the Fed raised the US cash rate by a quarter point for the third time since the 2007-09 recession (to between 0.75% and 1%). Among observations released over the quarter were that the US economy expanded at an annualised pace of 2.1% in the fourth quarter as consumer spending surged at a 3.5% rate. Others showed that the economy added 628,000 jobs in the three months to February, when the jobless rate stood at 4.7%. The S&P 500 Index rose 5.5%.

European stocks advanced as companies posted solid earnings growth and incumbent Dutch Prime Minister Mark Rutte thwarted a challenge from anti-EU populist Geert Wilders's Freedom Party. Reports over the quarter showed that loose monetary policy, a lower euro and an easing of fiscal austerity have perked up the eurozone economy. Reports showed the eurozone economy expanded 1.7% in 2016, consumer prices rose 1.5% in the 12 months to March and the jobless rate fell to an eight-year low of 9.6% in January. The Stoxx Europe 600 Index added 5.5%.

At an industry level within the benchmark, IT, healthcare and consumer-discretionary stocks advanced the most while energy, due to a 6% drop in the oil price, was the only sector to decline.

Fund Commentary

The portfolio recorded a positive return for the quarter where the largest contributors to performance were the investments in Apple, Facebook and Lowe's.

Apple rose 24.5% over the quarter on a better-than-expected first-quarter update that showed iPhone popularity remains high as the installed base is growing at double-digit rates and the company is seeing record numbers of people switching from Android devices. Engagement with the IOS ecosystem is increasing as App store sales grew 43% in the quarter to an all-time high. Facebook increased 23.5% after fourth-quarter revenue exceeded expectations with 51% growth. Facebook's users and engagement is growing and this is being successfully monetised via advertising revenue, particularly via mobile. Lowe's climbed 16.1% after fourth-quarter results saw strong comparable store growth of 5%, driven by buoyant housing and home-improvement spending.

Over the quarter, the stocks that detracted from returns included investments in Target, Tesco and Qualcomm.

Target declined 26.5% following the release of the company's fourth-quarter earnings that showed comparative sales were negative over the holiday period and the company's management announced significant downgrades to earnings expectations. This was due to implementation of a strategic initiatives that will entail resetting profitability to contend with a more competitive retail environment. Tesco fell 10.3% after the release of mixed trading statements from the company and the announcement of its intention to acquire UK-based food wholesaler Booker added to business complexity compared with the increased simplicity of recent years. Qualcomm slid 11.3% after Apple joined those launching legal action against the company based on claims of unfair royalty practices regarding its baseband chips.

Movements in the S&P 500 and Stoxx Europe 600 indices and stocks are in local currency.

Key Stock in Focus - Facebook

Facebook is the world's leading social network and is now worth over US$400 billion by market cap thanks to a more than tripling in revenue over the past three years. The company's competitive advantages point to more success ahead.

Facebook has built a position as the world's core social platform by attracting 1.9 billion users each month, about 30% of the world's population it can reach given that the company's network has been banned in China since 2009. Of this number, 1.2 billion people visit the core Facebook property each day. Facebook's other properties – WhatsApp, Messenger, and Instagram – have 1.2 billion, 1 billion and 600 million users each month respectively.

The scale and pervasiveness of Facebook's platform is unique and we believe non-replicable. The company benefits from a strong network effect, which means the more people join the more valuable the network becomes to all users. Facebook users stay loyal because they can spend years building their online social community, participating with countless posts, photos, comments, 'likes' and events on the platform. The 'news feed' is unique for each user, filled with relevant content from friends and other connections. The last direct challenge to Facebook was in 2011 with the launch of Google+ but it was already too late. Even with the might of Google behind it and arguably Google+'s better functionality, the network effect had already made Facebook uncatchable. Such victories highlight how Facebook is a uniquely advantaged global digital platform.

Facebook could always fall short of expectations, of course. The amount of time users spend on Facebook may not grow as fast as expected and with it reduce the growth in advertising that Facebook can display to users. One way this could happen is if alternative platforms improve their ability to deliver interesting third-party content to users. Improved artificially intelligent assistants, like Siri or Google Assistant, may deliver competitive personalised content that takes time share from Facebook's news feed. Another potential downside is that research and development costs and investments in non-core ventures could erode Facebook's margins. But Facebook appears well positioned to overcome any challenges.

Highly engaged users

Two attributes in particular indicate a bright future for Facebook. The first is that Facebook users are highly engaged. In April 2016, Facebook revealed that the average user spends 50 minutes per day between Facebook, Instagram and Messenger, dwarfing competing social platforms, and that this number is growing at double-digit rates.

Another way to look at Facebook's engagement is the share of its users who visit daily. Even as the number of its monthly active users has grown from 600 million in 2010 to 1.9 billion in 2016, the share of these users who visit its properties daily has increased from 54% to 66%. That means more users are visiting more often.

Facebook competes for people's time and engagement with all other media, including TV, print, radio, messaging platforms and YouTube and yet time spent on Facebook properties keeps growing. New social networks, such as Snapchat, and messaging services, such as Line, have threatened engagement on Facebook as they have expanded and added functionality. However, despite the fresh competition, Facebook's engagement keeps rising.

Advantaged in advertising

The second reason we are confident about Facebook's outlook is that the company is skilled at exploiting its network for advertising in three ways. Facebook's big advantage in advertising is that its ad-targeting capabilities are best in class. By participating on the social network, users provide to Facebook a stream of information about themselves, others, issues and brands with whom they interact, their location and their intentions. This data is only available to Facebook and is valuable to advertisers. Armed with this exclusive data, marketers can pinpoint advertising campaigns. A wedding planner, for example, might only want to show ads to women who are engaged living in the Gosford area. To target the same audience on TV the wedding planner might need to reach all women aged 20 to 50 across regional New South Wales. Facebook's ability to target such niches for advertisers will improve over time as technology advances and its collects more and richer data.

The next advantage with advertising, which admittedly is generic to all internet-based media, is that Facebook has a better ability to measure ad performance than offline media like TV, radio and print. Online advertising better measures the effectiveness of advertising by monitoring the clicks that follow online ad exposures, and by monitoring offline store visits. Providing evidence of the return of money spent on advertising campaigns on Facebook gives marketers the confidence to increase their spending on the platform, often by reallocating it from traditional media.

Facebook's other advantage with advertising is that it (and Google) are well positioned for the shift to mobile advertising such that in fiscal 2016 when 97% of Facebook's revenue of US$27.6 billion was generated from selling advertising, primarily on user news feeds, 84% was delivered on a mobile device. Mobile has grown to an estimated 20%[1] of people's media time (in the US); however, the smaller screen size has made effective advertising challenging on the devices. While few companies have found a solution, Facebook's news feed ads and Google's search ads work well. The result is that Facebook now boasts a share of about 32% of US mobile advertising spend compared with 6% on desktop[2].

Long runway

We expect Facebook's core business to grow at high rates. The number of Facebook users will likely increase, particularly in emerging markets, assisted by increasing smartphone penetration and better connectivity in these areas.

We anticipate engagement of users on the core Facebook properties will rise as Facebook optimises its services. Facebook's primary service, its news feed, aggregates socially targeted content – both user-generated and professional. Based on individual interaction with this content – clicks, comments and 'likes' etc. – Facebook tailors a unique experience for each user aimed at optimising engagement. It is constantly testing content and tweaking its placement algorithms.

Facebook contains some valuable stakes in nascent businesses that augur well for future profits. Its messaging platforms, Messenger and WhatsApp, each have over one billion monthly users yet currently generate no sales, while similar messaging platforms in Asia are already earning vast revenue. Facebook has invested early into virtual reality to shape the evolution of a new content format. Finally, advertising to targeted searches of its unique social database could prove extremely valuable to marketers, particularly when complemented by expected developments in artificial intelligence and Facebook's digital assistant, M.

Facebook's core business alone presents an attractive investment. These additional businesses provide the potential for material additional upside as Facebook offers more and better services to its billions of engaged users.

[1] Source: CFO Sandberg on Q1'15 earnings call.
[2] Source: Company filings, MagnaGlobal estimates, Magellan estimates.