

Making money do good

Shareholder
Newsletter
August 2016



Celebrating 30 years

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Ahead of the curve for 30 years

This year Australian Ethical celebrated a significant milestone – we turned 30.

Over the past three decades, we've seen a significant shift in attitudes towards investments and super. Ethical investing is now part of the mainstream – or at least the enlightened mainstream. We are proud of the important part Australian Ethical has played in this journey. Our track record shows that investors do not have to compromise returns in order to do what's right. And the great news is, we continue to go from strength to strength.

In FY16, I'm thrilled to report we've increased our net flows by 78%, bringing our total funds under management (FUM) to more than \$1.5 billion. In addition, our net profit after tax was up 53% to \$3.0 million.

Many of our managed funds continue to outperform the market. Our Australian Shares Fund was in the top quartile for performance over FY16 and is the #1 best performing Australian Shares fund over the last 10 years (compared to both ethical and non-ethical funds).

Our superannuation membership also grew by 24% in FY16. Over 5,000 new members joined us in that period, with a high proportion opting to roll over their entire super balance to us.

Focused on clients, shareholders, employees and the community

There's a bit of an art to balancing the needs of various stakeholders in a values-based business. We believe in doing what's best not only for our shareholders, but also for employees, clients and the wider community.

On 30 June 2016, we lowered fees on our superannuation fund by 0.22%, which represents a total reduction of 1.3% – over half the fee for a member in our MySuper product – since 2013. As we grow, we will continue to share the benefits of scale with our clients and prospective new members.

Our share price has increased from \$58.80 on 30 June 2015 to \$81.11 on 30 June 2016, benefiting shareholders – even while we lower fees. In FY16, our total shareholder return was 43%.

None of this would be possible without our employees. In FY16, we launched an office expansion that aims to have our team working in a modern, collaborative environment and allow for growth. We also continue to support employees in their professional and personal lives, with the belief that these two areas are inextricably linked. To ensure that the goals of employees and the company are aligned, each employee is also a shareholder in the business.

Our grants program remains a source of immense pride for us. This year we supported 18 community projects – from animal welfare to environmental conservation to helping alleviate poverty. To date, we have donated over \$2 million to community projects, and our recently established Foundation will provide additional flexibility in how we support charitable organisations in the future.

Operating within the global investment landscape

The pressure to deliver short-term returns can drive companies to deplete the resource base (economic, natural and human) that underpins their own future prosperity. I've been pleased to see increasing discussion on how we can change this trend within international markets and focus capital markets more on the longer term.

At Australian Ethical we're committed to:

- focusing capital on delivering long-term value, and
- shifting financial markets towards a more responsible and sustainable footing.

Global capital is the most dominant force in the world today. Our purpose is to make sure that capital is used for the good of people and the planet. Through our ownership of companies, on behalf of our clients, we are recalibrating businesses to focus on creating sustainable, long-term value.

One of the biggest threats facing our world today is climate change. I'm proud to say that each day at Australian Ethical we're taking action to address this issue. By refusing to invest in environmentally damaging industries such as coal and logging, and by investing in clean energy solutions such as solar and wind, we're directing capital towards sustainable and future-driven industries. We're

doing this not only for the prosperity of our company and the nation's economy, but also for the prosperity of our planet.

Looking to the future

We have a clear vision for our business. We aim to be the financial services company of choice for conscious consumers. This year we've shown we're on track to achieve this vision, and remain a leader in the field of ethical investing.

We have a goal of reaching \$5 billion in FUM by 2020. Ambitious, sure – but we're committed to reaching it. We know this type of growth would allow us to:

- deliver broader services to our clients,
- have greater impact in society for positive change, and
- continue to deliver strong returns for our shareholders.

A 30-year milestone is a great opportunity to reflect. After three decades of ethical investing, we're stronger as a business than ever before. And our core priority – to make money do good for people and the planet – will allow us to operate a thriving, sustainable business well into the future.



Steve Gibbs
Chairman



Phil Vernon
Managing Director

Our year in numbers

Employee
engagement
2016:

77%²

#1

'BEST RESPONSIBLE
INVESTMENT
REPORT' 2015¹

26,000+
Super members
24% increase
since FY15

27%
RETURN ON
EQUITY

\$395,314
provisioned for
community
projects³

Emerging Companies Fund

AN INNOVATIVE NEW
PRODUCT LAUNCHED

- 1) Responsible Investor Reporting Awards
- 2) Externally benchmarked by AON Hewitt.
- 3) Some funds were held back in FY15 for investing in future projects.



\$23
million
revenue



\$3.00
DIVIDENDS



282c
earnings
per share



60,259
TONNES LESS CO₂⁴



OVER
\$1.5 billion
IN FUNDS UNDER
MANAGEMENT



\$3.0
million
profit after
tax

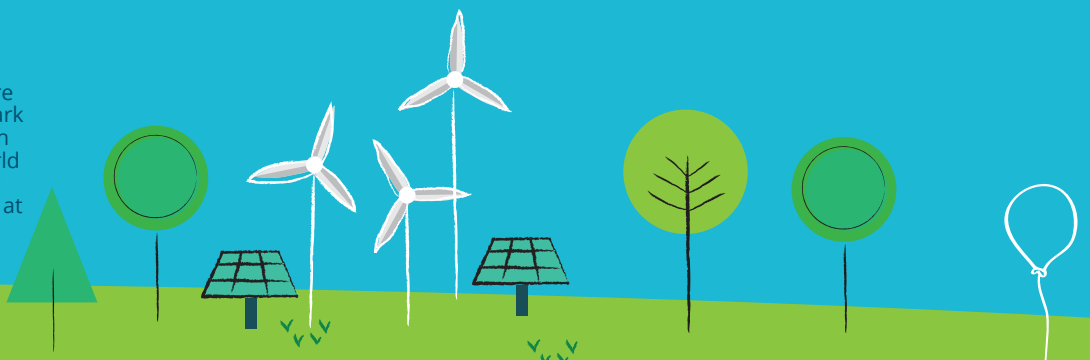


**Top quartile
for performance**

OUR AUSTRALIAN SHARES FUND
OVER THE PAST
12 MONTHS

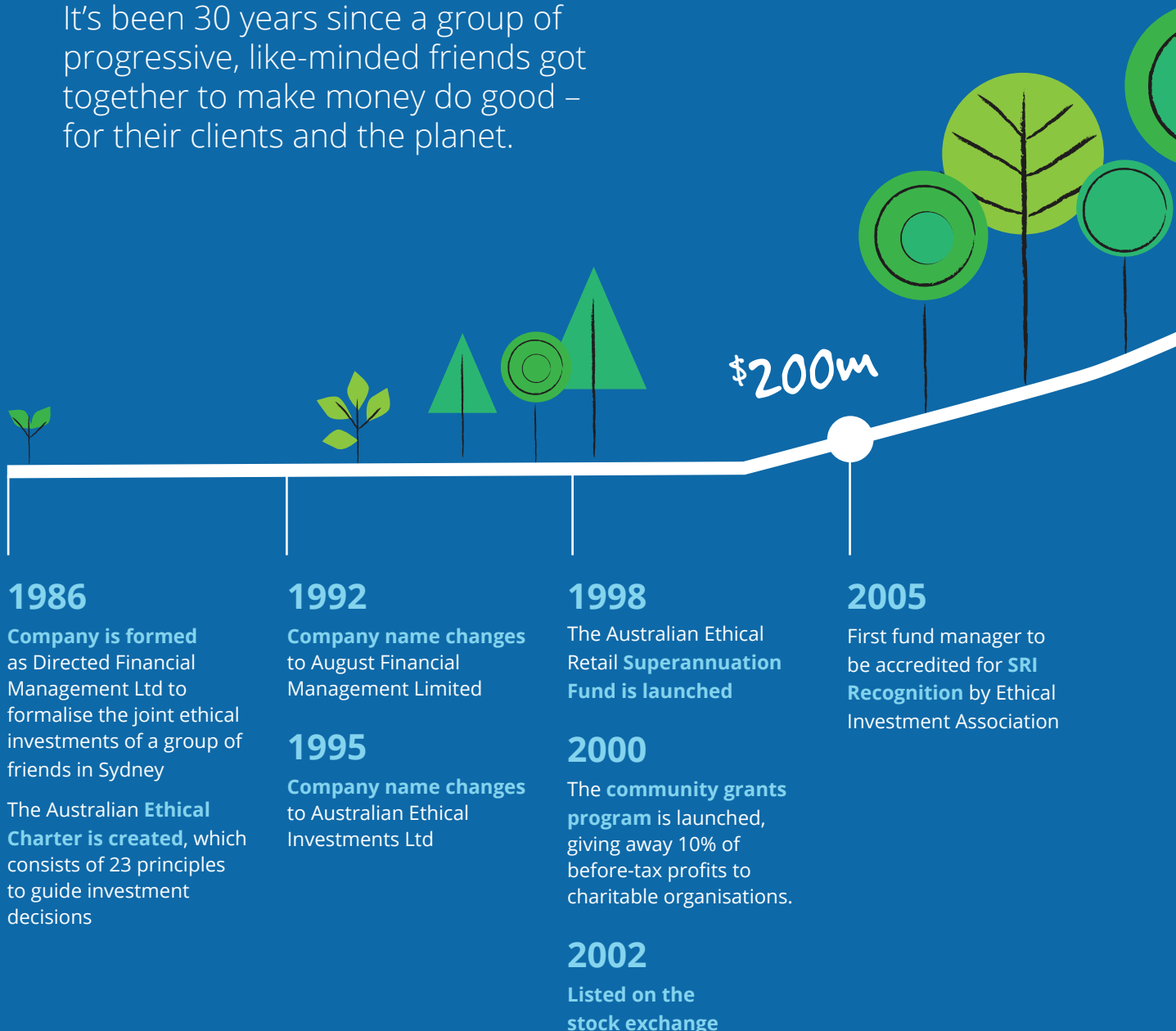
Mercer Survey, June 2016

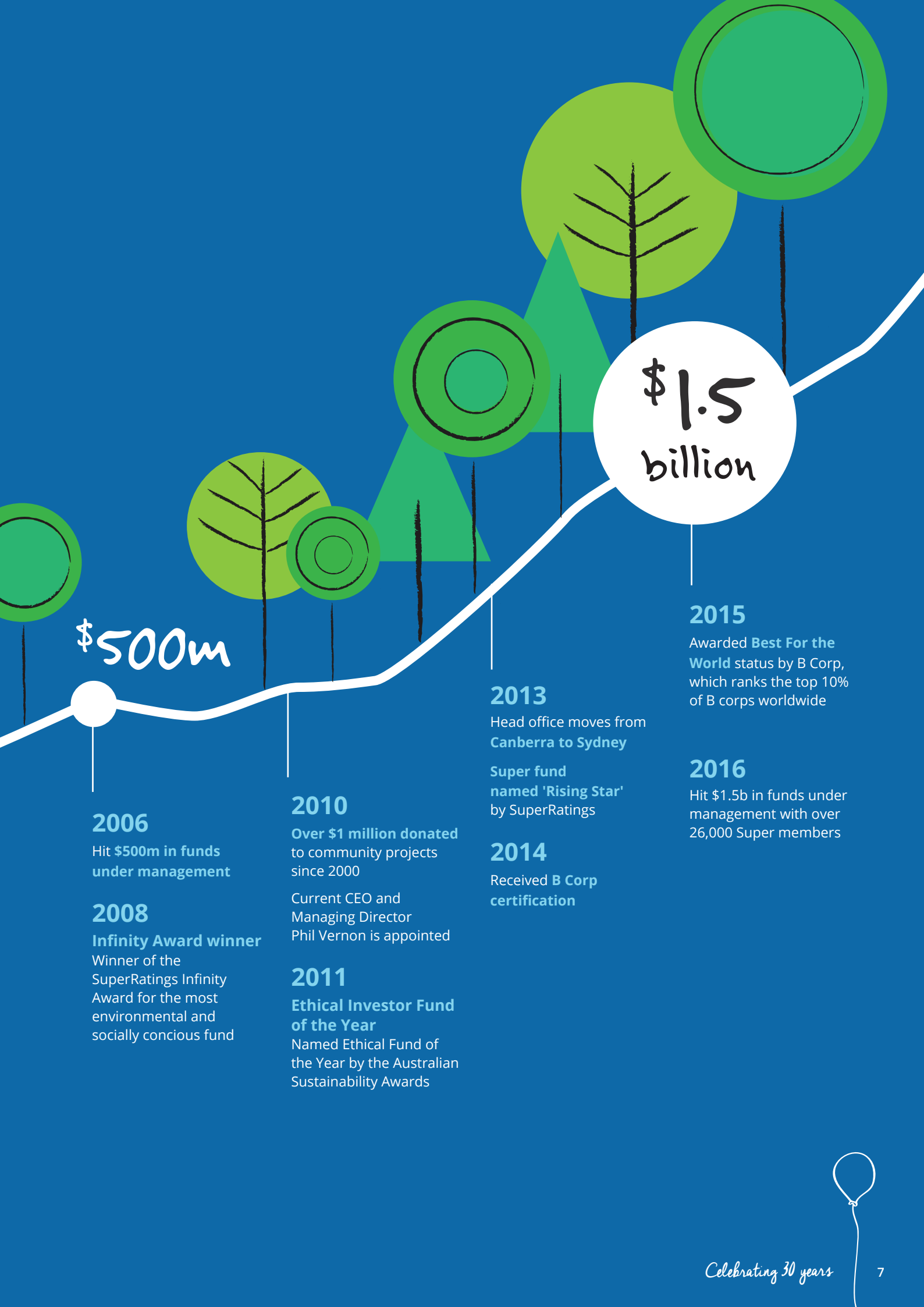
4) Emissions of Australian Ethical share investments compared to benchmark of S&P ASX 200 Index (for Australian share fund holdings) and MSCI World Index ex Australia (for international share fund holdings). Calculated as at 31 December 2015.



Our story

It's been 30 years since a group of progressive, like-minded friends got together to make money do good – for their clients and the planet.





\$500m

\$1.5 billion

2006

Hit \$500m in funds under management

2008

Infinity Award winner

Winner of the SuperRatings Infinity Award for the most environmental and socially conscious fund

2010

Over \$1 million donated to community projects since 2000

Current CEO and Managing Director Phil Vernon is appointed

2011

Ethical Investor Fund of the Year

Named Ethical Fund of the Year by the Australian Sustainability Awards

2013

Head office moves from Canberra to Sydney

Super fund named 'Rising Star' by SuperRatings

2014

Received B Corp certification

2015

Awarded **Best For the World** status by B Corp, which ranks the top 10% of B corps worldwide

2016

Hit \$1.5b in funds under management with over 26,000 Super members

Our commitment to the community

While ethical investing is our bread and butter, we know there are a lot of projects and organisations doing good that aren't traded on investment exchanges. These projects have a vital role to play in achieving a happy, healthy world, so each year we donate 10% of our pre-tax profits to organisations making a positive difference.

Since our community grants program began in 2000, we have donated over \$2 million to charitable organisations. In FY16, we received a total of 739 grant applications. These applications were reviewed internally for their ability to deliver

tangible outcomes that benefit the planet, people or animals. All our major stakeholder groups have a say in who receives a grant, employees and shareholders voting on the winner from a shortlist. This was the first year where even our clients had an opportunity to participate. In FY16, we distributed \$230,000 of community grants to 18 organisations through the Australian Ethical Foundation. The Foundation was granted charity registration with the Australian Charities and Not-for-profits Commission on 12 August 2015.

FY15 community grant recipients

\$20,000

grant recipients



Environmental Defenders Office Inc (NT)

Improving access to environmental justice in the Northern Territory
edont.org.au



Animal Aid Abroad

Improving the welfare of working donkeys in Afghanistan
animalaidabroad.org



Angel Place

Supporting homeless families through crisis accommodation in hotels
angelplaceproject.com



Green Connect

Providing jobs for young people and refugees and improving sustainability in the Illawarra, NSW
green-connect.com.au



Animalia Wildlife Shelter

Helping sick, injured and orphaned wildlife in Victoria
animaliawildlife.org.au

\$15,000

grant recipients



East Gippsland Rainforest Conservation Management Network

Protecting rainforests and providing Indigenous employment opportunities in Victoria

egrainforest.org.au



Abundant Water

Providing clean water filters and education programs to improve the lives of women in Laos

abundantwater.org

\$5,000

grant recipients

The Incredible Tip Shop

Providing jobs for disadvantaged job seekers in Mackay, Queensland

[facebook.com/
TheIncredibleTipShopMackay](https://facebook.com/TheIncredibleTipShopMackay)

A Girl & Her World

Supporting girls to stay in school and mothers to achieve financial independence in Fiji

agirlandherworld.org

\$10,000

grant recipients

Australian Red Cross with the Royal Flying Doctor Service

Providing healthy living programs for remote Aboriginal communities

redcross.org.au

Alternative Technology Association

Providing repairs for solar-power systems in villages in East Timor

ata.org.au/what-we-do/ipg

Assisi Aid Projects

Providing programs to help widowed women in rural India achieve financial independence

assisi.org.au

Indigo Foundation

Providing job opportunities and food for women in Indonesia through community gardens

indigofoundation.org

Wildlife Asia

Protecting the critically endangered Sumatran rhino

wildlifeasia.org.au/help-us/operation-Aceh

With Compassion & Soul

Caring for at-risk wildlife, including sun bears and orangutans, in Borneo

withcompassion.com.au

The Orangutan Project

Protecting orangutans against poachers and environmental threats

orangutan.org.au

Free to Shine

Providing school scholarships for girls at risk of sex-trafficking in Cambodia

freetoshine.org

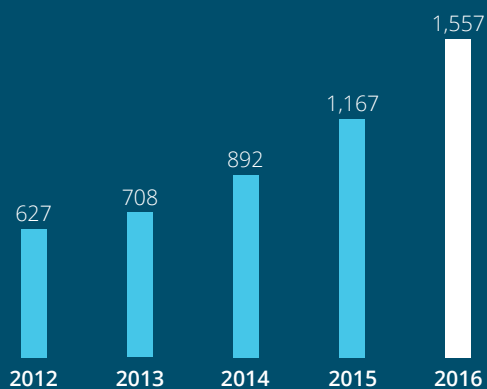
Sleepy Burrows

Helping sick, injured and orphaned wombats in NSW

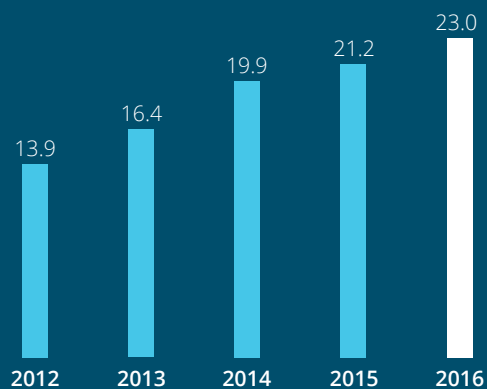
sleepyburrows.com.au

Financial summary

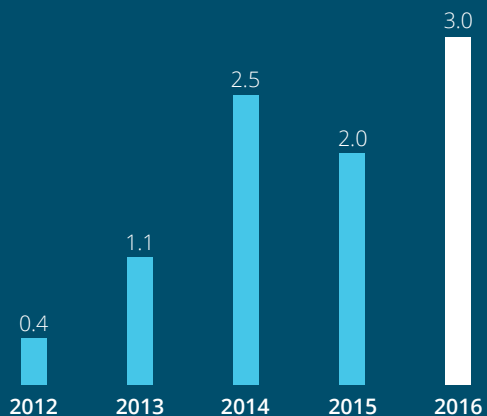
Funds Under Management (\$m)



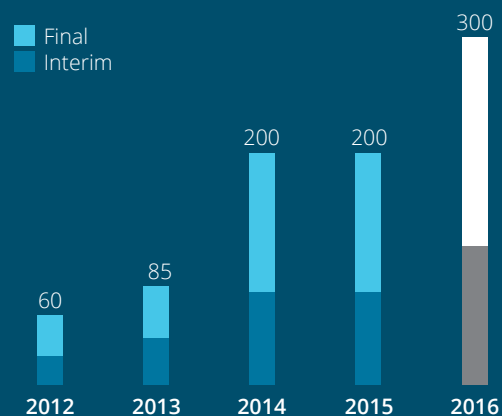
Revenue (\$m)



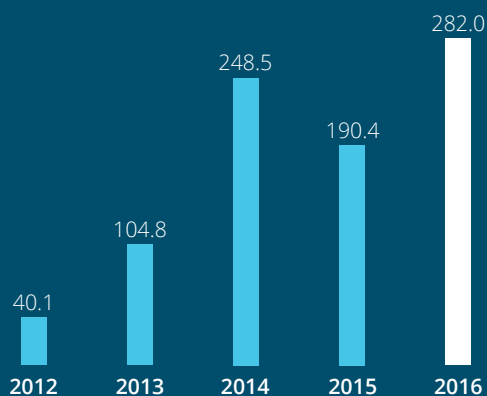
Profit After Tax (\$m)



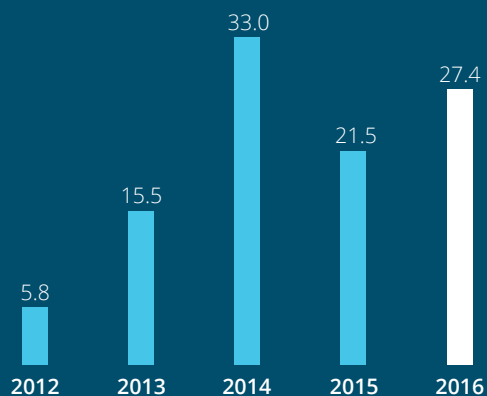
Dividends (cps)



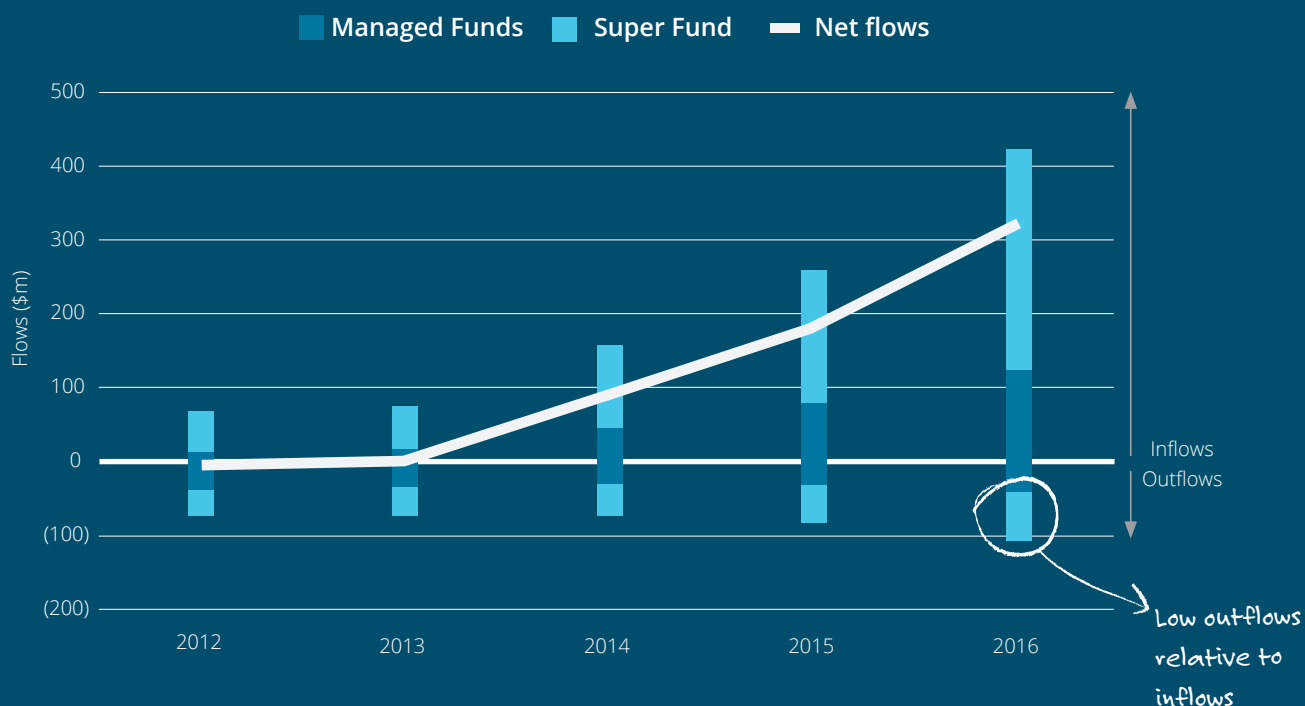
Basic Earnings Per Share (\$)



Return on Equity (%)



Net inflows



Financial results for the year to June 2016[^]

Key financials (A\$000s)	FY2016	FY2015	Change (YOY) %
Revenue	23,039	21,171	8.8
Expenses	(20,029)	(19,201)	(4.3)
Net Profit After Tax	3,010	1,970	53.0
Property impairment	181	484	63.0
Provision for remediation	900	0	n/a
Tax adjustment	(270)	0	n/a
Underlying Profit After Tax	3,821	2,454	55.7

Strong growth in our underlying earnings

[^] Underlying profit is provided to assist shareholders in understanding the Company's performance. Underlying profit excludes certain items, as determined by the Board and management, that are either significant by virtue of their size and impact on Net Profit After Tax, or are deemed to be outside normal operating activities. It reflects an assessment of the result for the ongoing business of the Group. This table has been prepared in accordance with the Australian Institute of Company Directors (AICD)/Finsia principles for reporting underlying profit and ASIC's Regulatory Guide 230 Disclosing non-IFRS financial information. Underlying profit after tax has not been reviewed or audited by our external auditors, however the adjustments to net profit have been extracted from the books and records that have been audited.

Delivering returns in a volatile market

In recent years, Australians have grown accustomed to the seesawing share market. Sharp falls in share prices, high private and public debt, monetary policy, increased government intervention in the economy, tax transparency measures and falling resource prices have all played a part in creating market volatility.

We understand the concern this causes our clients and remain committed to delivering competitive returns as the market plays out.

Our managed funds were some of the best performing during the Global Financial Crisis. Our Australian Shares Fund has returned an average of 10% per annum over the last twenty years. This year, we also outperformed the ASX 200 and the S&P500.

Financial returns

Our success in recent years has been underpinned by ethical leadership, strong investment performance and a clear retail distribution strategy.

In May 2016, we achieved two significant milestones. We passed \$1.5 billion in funds under management (FUM) for the Australian Ethical group, and \$1 billion in FUM in our superannuation fund. Since reaching these milestones, our FUM has continued to grow, hitting \$1.56 billion at 30 June 2016.

Not only that, this year our full-year profit increased by 53% to \$3.0 million. This increase is due to strong growth in our FUM, as a result of both strong flows and general market conditions.

Some other results that reflect our growth and performance are:

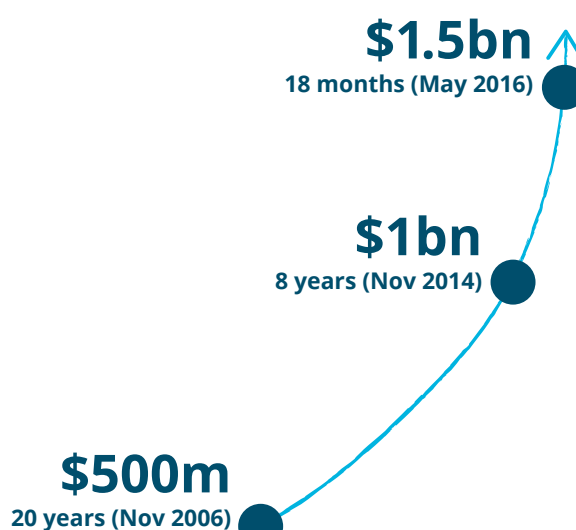
- superannuation membership at 26,342 (up 24% since last year);
- top quartile investment performance for a number of our funds; the Australian Shares Fund is the top ranked fund in its category over 10 years¹;
- over \$390,000 provisioned for community grants.

Net profit

Net profit after tax for the financial year to 30 June 2016 was \$3.0 million compared to \$2.0 million in the previous year.

The increase of 53% on the previous year was the result of increase in FUM from strong flows and market increase. The additional revenue from the FUM increase more than offset the fee reductions made in July 2015.

Our funds under management



¹ Mercer Survey, June 2016

Revenues

Revenue increased by 9% to \$23.0 million, up from \$21.2 million recorded for the previous year.

Net inflows increased by 78% to \$319 million for the year, compared to last year's net inflows of \$179 million.

FUM for the full year increased 33% to \$1.6 billion, up from \$1.2 billion in the previous corresponding period. This growth in FUM has been driven by a combination of new inflows and asset management performance.

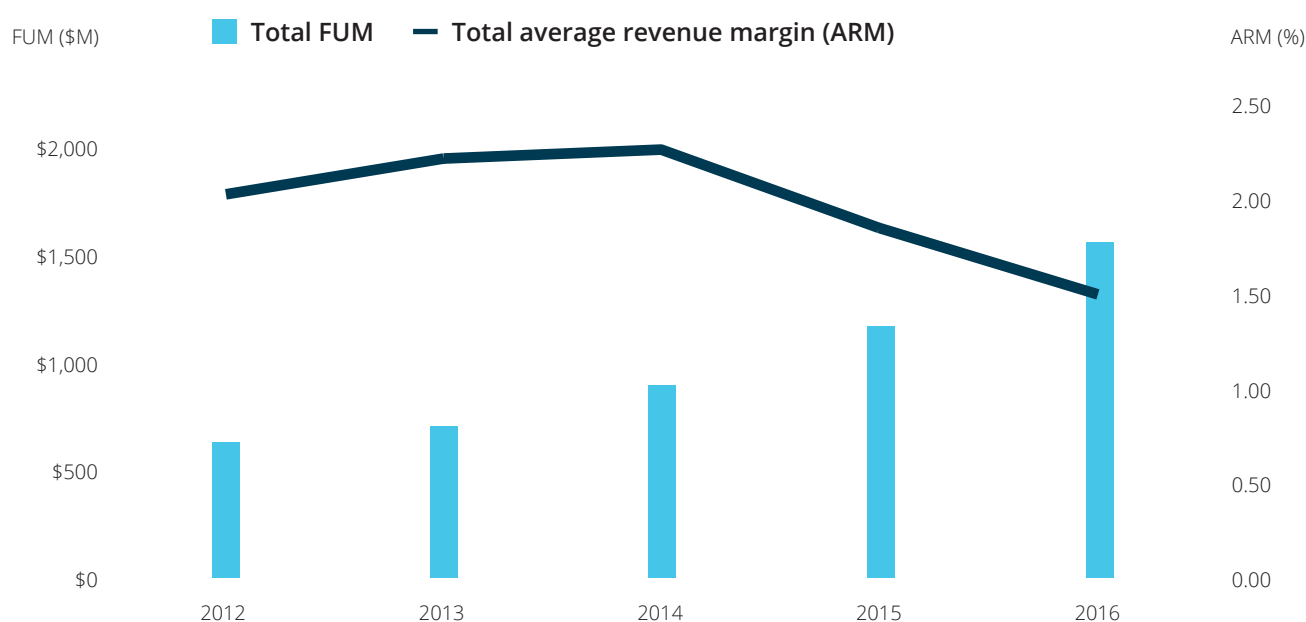
The impact of superannuation fee reductions at the end of the previous financial year was

offset by increases in net flows and growth of FUM this year. An additional fee reduction of 0.22%, reducing superannuation administration asset based fees to 0.41%, occurred on 30 June 2016¹. We continue our medium-term strategy to progressively reduce fees to a more competitive level, taking into account business needs and shareholder returns.

Fee reductions are one of a number of strategic initiatives to increase our competitiveness. The following table illustrates the potential impact of the most recent fee reduction. Revenue margins have been calculated as annualised FUM-based revenue divided by average FUM.

Products	Revenue margin based on 2015 fees (%)	Revenue margin based on 2016 fees (%)	Estimated Adjusted margin 2017 (%) ²
Managed funds	2.09	1.71	–
Superannuation	1.74	1.40	1.24
Overall	1.86	1.50	–

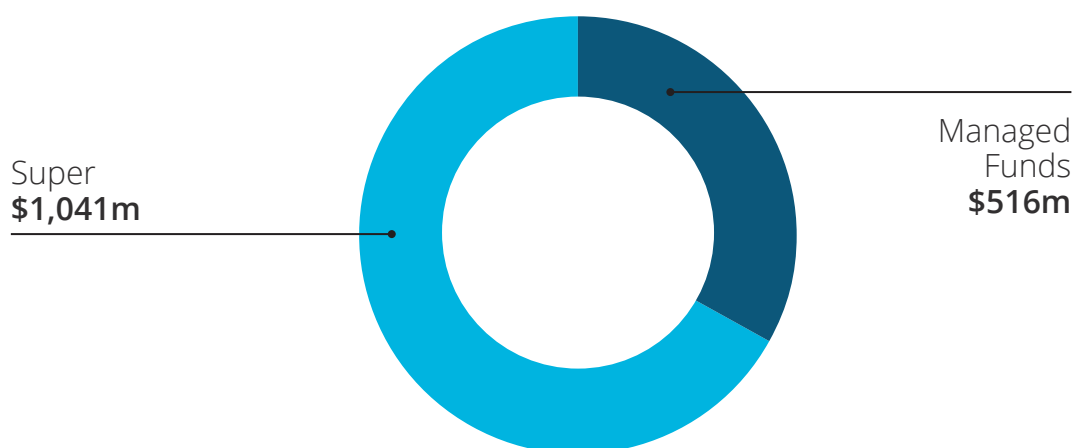
Our revenue margin has reduced over time due to planned fee reductions and increased flows into wholesale priced products. However, we have continued to substantially increase our FUM during the same time as highlighted in the graph below.



Average revenue margin is FUM-based revenue as a proportion of average FUM over the year. FUM-based revenue is one component of total revenue. Other revenue includes member and withdrawal fees, interest and rent. Details can be found in Note 2 of the Consolidated Financial Report 2016.

1 Fee reduction included a reduction in the reserve allocation of 0.07%.
 2 Revenue margin calculated as 2016 margin less fee reduction at 30 June 2016.

Funds Under Management



Final dividend

A fully franked final dividend of \$1.80 per share was declared for the full year ended 30 June 2016, bringing the total dividend for the year to \$3.00 per share. The record date for the dividend is 9 September 2016, with payment on 23 September 2016.

Expenses

Total expenses increased by \$0.8 million (4.3%). Expenses increased due to the following:

- **Marketing:** an increase in marketing activity drove the increase in flows with costs increasing by \$0.6 million over the previous year.
- **External services:** costs to outsource providers increased by \$0.1 million as a result of increased audit fees and platform fees. Fund-related costs increased by \$0.4 million due to increases in FUM and client numbers.
- **Income tax expense:** the effective tax rate was 36%, a decrease on the previous year's rate of 45%. Our effective tax rate is impacted by items that are not deductible for tax purposes, which are detailed in Note 4b of the Consolidated Financial Report 2016.
- **Property:** due to further weakening in the Canberra commercial property market our property in Canberra reduced in value by a further \$0.18m.
- **Provision for remediation:** A provision of \$0.9 million has been made in relation to remediating superannuation members for unit pricing errors with investigations continuing. The Group is committed to ensuring that members are not materially disadvantaged as a result of these errors and rectification is expected to be finalised in FY17.

The above expense increases were offset by:

- **Employee benefits expense:** costs have decreased by \$0.8 million or 9.2% over the previous year due to the prior year containing a number of transition impacts. There is one series of share performance rights remaining in respect of the employee incentive scheme (these share performance rights have been replaced by a different scheme referred to as deferred shares). Due to the increase in share price over the year expenses related to these rights were \$0.9m. Salary costs increased by \$0.1 million.

Financial position

We retain a strong balance sheet position with no debt. Net assets increased by \$1.7 million over the year to \$12.8 million. The majority of assets are held in cash to meet our Australian Financial Services Licence (AFSL) requirements. The only significant non-cash asset is a property held in Canberra, which is discussed in detail in Note 7 of the Consolidated Financial Report 2016. The assets held in excess of the licence requirements provide a buffer in the event of a sustained market downturn.

Over the year we achieved \$319 million in net flows, a 78% increase on the flows for the previous year of \$179 million. An increase in online marketing contributed to the improved flows, which were supported by strong investment performance.

“ Fish as a source of protein in Australia (and globally) is growing strongly. Aquaculture is essential to meet growing demand for fish as a source of protein as the world’s oceans are over fished.”

Ray Gin,
Australian Ethical Equities Analyst



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