Monthly Report – April 2021
Alphinity Concentrated Australian Share Fund

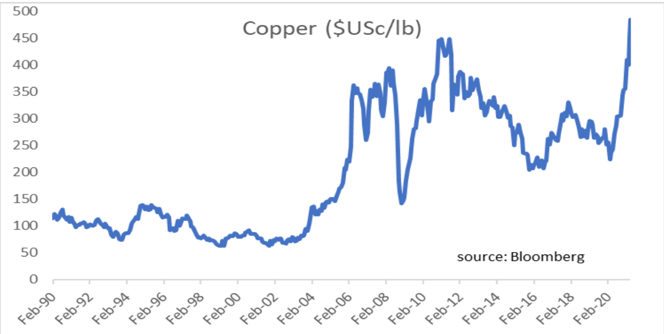
Off to the Races

Market comment

April saw an almost 4% rise in the market (ASX300 including dividends), bringing the year-to-date market increase to 8%; the positions in the Fund have added further to that, bringing year-to-date returns approaching 10%. It continues to feel a bit surreal, after all the headwinds and challenges that the world has thrown at us over the past year or so, but when you look at the other asset classes you have to choose from, equities obviously look to many like the least worst option.

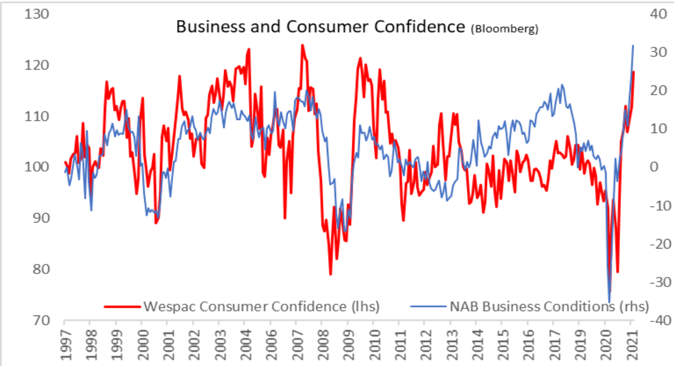
Australian shares did well compared to most global markets despite a stronger $A. While it lagged the 5-6% rises in a couple of European markets and Brazil, the ASX matched the US market and did better than the rest. China and Japan both experienced modest falls and the rest were flat to up a couple of percent. An incredible 18% rise in the price of Iron Ore was behind much of our strength (and Brazil's) and most base metals also did well; precious metals however were relatively flat. The price of oil was up about 4% over the month.

Copper rose by 12% in $US terms (10% in $A) in April alone. Demand for Copper is seen as an indicator of future global growth as it is such an essential input to so much of economic activity. This is particularly the case at present as the world moves towards renewable energy: changes in the grid and increased electrification of transport require a lot of copper. The price of copper finished at an all-time high in April and, with the degree of demand foreseeable, it could easily go higher from here. The Fund is well exposed to the copper thematic.



The Australian economy continues to rebound with alacrity from its Covid-slump of last year. Unemployment continues to fall, much more quickly than economists expected, and with a federal election due within a year we can't help feeling that the pump will continue to be primed as much as is needed to keep the recovery on track.

Inflation announced in April for the first quarter of the calendar year showed an encouraging tick-up in what has been stubbornly low. Business and consumer sentiment, as measured by two of the big banks, are both at extremely high levels; for business it is the highest on record. Now that we can't leave the country, the money we're saving on overseas travel seems to be flowing into the shops, and until something changes, probably will stay there until the country can open its borders again.



Portfolio comment

The Fund outperformed the strong market in April. It benefitted from holdings in several different sectors, including waste management company Cleanaway, steel maker Bluescope, health care device manufacturer Fisher and Paykel, health insurer Medibank Private and iron ore miner BHP. On the other side of the ledger our position in supermarket operator Woolworths and not owning consumer finance operator Afterpay nor iron ore exposures Rio Tinto or Fortescue all cost a small amount of performance.

Performance*	1 Month %	Quarter %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception^ % p.a.
Fund return (net)	3.6	9.3	30.7	9.3	11.6	9.9	10.6
S&P/ASX 200 Accumulation Index	3.5	7.5	30.8	9.5	10.3	8.3	9.0

*Returns are calculated after fees have been deducted, assuming reinvestment of distributions. No allowance is made for tax. Past performance is not a reliable indicator of future performance. **Source: Fidante Partners Limited, 30 April 2021.**

^The Fund changed investment manager and investment methodology on 12 July 2010, at which time Alphinity Investment Management commenced managing the Fund and started the transitioning of the portfolios to a structure consistent with Alphinity's investment views. The transition was completed on 31 August 2010. The inception date for the returns for the Fund is 1 September 2010. For performance relating to previous periods, please contact the Fidante Partners Investor Services team on 13 51 53 during Sydney business hours.

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Market outlook

Strong corporate earnings and stable to lower bond yields, following their sharp rise in the March quarter, have combined to continue to propel equity markets even higher. With robust consumer demand and a remarkably empty global supply chain in everything from cars to steel and most things in between, corporate earnings, especially in cyclical sectors, look set to continue to beat market expectations in the next few months. At some point demand will slow and the supply chain will catch up. When that happens the impact could be quite abrupt but that looks like a concern for later in the year.

What bond yields will do is more difficult to predict as inflation concerns seem to be wax and wane on almost a weekly basis, but in our view they remain too low and are the key risk to equity markets. Considering the abundance of earnings growth and still-lofty valuations for many growth sectors, epecially Australian technology stocks, we expect that cyclical sectors will continue to be favoured by investors even though some more defensive, lower growth companies such as Consumer Staples, which have been left behind in the rally, are looking increasingly attractive from a valuation perspective.

The February reporting season covering trading in the period up to the end of December gave us an early indication that the shape and pace of the earnings recovery for some of the "Covid losers", such as travel related companies, looked too optimistic. At the same time the longevity of the tailwinds for some of the "Covid winners", such as consumer goods companies, had been underappreciated by market participants.

More recent company updates regarding earnings thus far in calendar year 2021 have reinforced this view. Although too early to tell for sure, it wouldn't surprise us if those trends remain in place even in the medium term. While we are all looking forward to the end of restrictions on travel and social interaction, and returning to life in general as we used to know it, corporates, employees and consumers have all learned new ways of doing things and new things to enjoy. Life will surely be better after Covid is done with than at present, but it will not necessarily ever be the same as before.

Top five active overweight positions as at 30 Apr 2021	Index weight %	Active weight %
BHP Group Limited	7.1	5.4
Commonwealth Bank Of Australia	8.0	2.6
National Australia Bank Limited	4.5	2.5
Woolworths Group Ltd	2.5	2.3
Cleanaway Waste Management Ltd	0.3	2.1

Source: Fidante Partners Limited, 30 April 2021.

Portfolio Outlook

Pleasing momentum following on from the February reporting season was evident in April with a number of our portfolio holdings making further positive earnings announcements in recent weeks, and this helped to drive outperformance in April. Strong trading updates by steel manufacturer Bluescope and metal recycler Sims as well as retailer Super Retail Group and plumbing parts manufacturer Reliance Worldwide were all well-received by investors and reflect the strong manufacturing and consumer enviroment which has been building since the middle of last year.

The Banks' interim earnings announcements added further evidence of the strong domestic economic recovery with last year's fear of an imminent sharp increase in bad debts looking increasingly misplaced. We remain comfortable with our current modest overweight to the sector and would potentially look to increase our exposure further if earnings momentum also improved at the underlying operating level (i.e. excluding movements in bad debts provisions). Improving credit growth also has the potential to provide further upside surprise for the sector.

In the Insurance sector, insurance broker Steadfast and general insurer QBE are both making the most of a strong pricing environment while private health insurer Medibank Private looks well poised to benefit from market share gains and a benign claims environment. In the packaging sector Amcor reported another strong quarterly result and raised its full year guidance for the third time this financial year. While most of the market's focus remains on cyclical companies, strong operational performance by this group of more defensive companies, that are less driven by the economic cycle, is important and, in our view, will become even more so as the momentum in the economic recovery inevitably slows.

The Technology sector remains one of the largest underweights for the portfolio relative to its benchmark. This sector looks increasingly vulnerable to overly-optimistic earnings expectations and also hard-to-justify valuations.

Overall, we believe that the portfolio remains well positioned to continue to capitalise on the evolving earnings leadership.

Asset allocation	30 Apr 2021 %	Range %
Securities	98.9	90-100
Cash	1.1	0-10

Source: Fidante Partners Limited, 30 April 2021.

BTW

A topic not discussed much among Bitcoin speculators, but which should increasingly be, is that the process of generating Bitcoin is bad for the environment and could even be killing people. Why do we say this?

We've reported on these pages previously that "mining" Bitcoin and its ilk consumes an enormous amount of electricity. In fact it is on track to use as much as the whole of Australia in 2021. If that electricity were being generated by renewables we might be less concerned but the fact is, it's not. A substantial amount of the world's crypto activity takes place in China where electricity is cheap and, despite that country making some strides towards renewables recently, ~70% is generated by burning Coal. And even if the Bitcoin mines were all powered by renewables, unless the miners had built their own supplies it would just consume the renewable energy that other electricity users would have consumed doing something useful.

Adding to that, the trade war China is waging against Australia has meant that it won't allow Thermal Coal from Australia into the country. This has caused great suffering to seafarers, mostly from poor countries, stuck on ships off the coast of China for months on end, and to the shipping companies whose ships are effectively being held hostage. It also caused power shortages in some provinces during the depth of winter and increased demand for Chinese thermal coal substantially which has spurred on miners there to produce more.

We're not fans of thermal coal, in fact this Fund will not invest in companies with anything more than an immaterial exposure to the mining of thermal coal. But two things we know are (a) the thermal coal produced in Australia is mostly of high quality and produces a lower amount of non-carbon pollution than coal from most other countries; and (b) the safety standards in Australian mines are generally pretty good and the number of injuries and deaths are low in global terms.

These are two things that can't be said about the coal mined in China. Much of its thermal coal has higher ash and lower energy content than ours which means they need to burn more of it to produce the same amount of electricity. It also means there is more CO_2 emitted and more residue left over. While it would be better not to burn coal at all, if you were forced to you would use Australian coal over Chinese coal every time. Unless of course you were an authoritarian regime which feels that teaching a smaller nation not to stick up for its own interests or raise awkward subjects is more important than mine workers' safety, the environment, and the cost and/or availability of energy to its own citizens.

The safety aspect is easy to observe. Bloomberg published an article in April linking the high coal price in China with its mining companies prioritising output ahead of safety resulting in accidents that had caused a number of deaths. It reported a huge rescue operation which was underway at the time to save 21 miners trapped underground in the troubled Xinjiang province in Western China; this was after a further 12 people had died in mining accidents in Guizhou and Shanxi provinces earlier in the month.

The energy considerations of Bitcoin is even starting to cause concern among some crypto newbies. While longer-term operators are obviously happy to just make money (when it goes up), we saw a story during the month about a minor celebrity in the US, new to the crypto space, who was recently rapped over the knuckles by the social media police for not buying green coins; he is now an evangelist for green coins. A green coin is one that has been mined only using renewable energy; all the others apparently are blood coins: bought on the secondary market or mined using electricity generated by dirty fossil fuels.

Two firms with vested interests in cryptocurrencies however hit back in April with this rather glass-almost-full white paper about how mining wasn't really that bad for the environment, it could be its saviour! It appears to us to rely on some optimistic, unrealistic, and often contradictory assumptions, and imputes a degree of altruism and coordination to the crypto world we haven't thus far noticed. It contains some fairly scary numbers about the potential energy use of the industry as Bitcoin heads towards its absolute limit of 21m coins. This white paper has since been reviewed by other commentators, including this lengthy but entertaining diatribe by an Irish hedge fund manager. One can't ignore Bitcoin, or indeed the ~$US2 trillion total "market capitalisation" of the 10,000-odd cryptocurrencies out there (and some are very odd!), but like so many things in life, buyers need to beware.

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Traveller's Tale

There's been a buzz about the office lately as at least a degree of normality starts to return after a very weird year of Covid-related disruption: travel is back! To be fair, so far it is only domestic and it is always on the proviso that a nervous state Premier doesn't all of a sudden close its border, but it is very energising to be able to get out there and see stuff again. And with the NZ bubble now happening the prospect of going even further afield – dusting off or even renewing that old passport – is in sight.

Stephane went to Perth during the month to see a number of domestic and international oil/gas companies operating in the Perth Basin, and also to meet with some engineering companies. Not only did he see the inside of a plane, he (and two others) also saw the inside of a helicopter. The aircraft shown opposite was flown by the great Nev Power and is one of the three choppers Nev owns. Nev is the former long-time CEO of iron ore behemoth Fortescue Metals Group. He retired from FMG in 2018 and has since been pursuing personal business and public policy interests. He is presently a director of gas explorer Strike Energy and was, until recently, heading up the Prime Minister's Covid-19 Commission.

The Perth basin has been surprisingly productive over the past few years and various parties have discovered large and deep onshore dry gas wells, much easier to access than the offshore gas that abounds around Western Australia. Strike Energy is aiming to commercialise the resource it has found but still make the company carbon neutral by 2030 by building a urea plant. Urea is a component in fertiliser, and most used here is presently imported from Qatar, Saudi Arabia or China. Strike believes it can halve the amount of carbon emissions involved in Australia's usage of urea, and at the same time supposedly add $8 billion to Australia's GDP. We look forward to seeing all the details.

For further information, please contact:
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