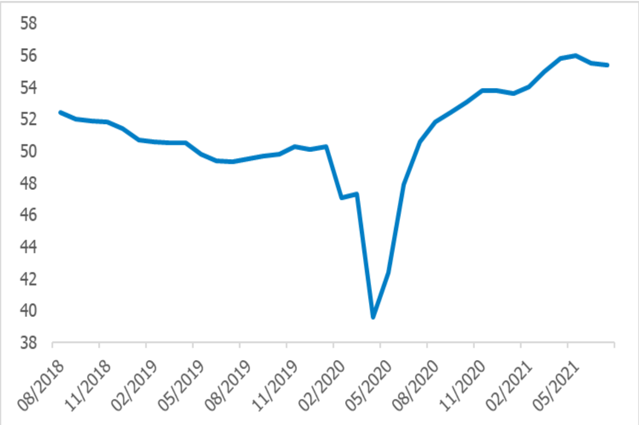
Monthly Fact Sheet July 2021

Market comment and outlook

Global equity markets continued to rally in July, spurred on by falling bond yields and strong second quarter earnings reports in both the U.S. and Europe. In AUD terms, the MSCI World Index gained +3.8%, with both the US (S&P 500: +4.4%) and Europe (STOXX Europe 600:+4.2%) outperforming amongst Developed Markets. In comparison, Emerging Markets were significantly weaker, triggered by concerns about the Covid Delta variant, as well as increased Chinese regulatory scrutiny of the Technology and Education sectors, which precipitated an 8.2% fall in Hong Kong stocks and 3.5% loss in China A-shares.

Global Manufacturing PMI softened in July

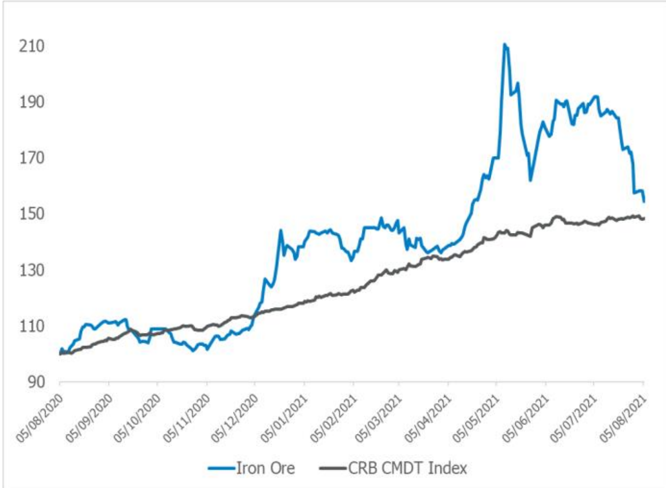


Source: *Bloomberg, JPM data, 31 July 2021*

Economic data released in July was more mixed. The Global Manufacturing Purchasing Managers Index (PMI) softened to 55.4, versus its peak of 56 at the end of March, with industries including Semiconductors, Autos and Homebuilders highlighting capacity constraints and supply chain shortages of inputs like microchips, raw materials and labour. The June US CPI print came in at +5.4% y/y, or +4.5% y/y excluding food and energy, both well above expectations. The Fed left policy rates and their bond buying program unchanged, with Chairman Powell wanting to see a stronger labour market before tapering. The CRB All Commodities Index rose 1.1%, although this masked a significant fall in iron ore (-15.4%) as China curbed steel output. The benchmark 10-year bond yield fell 25bps to close at 1.22%.

The falling yield environment contributed to Growth outperforming Value, reversing recent cyclical market leadership, with Healthcare (+3.7%) and Technology (+3.5%) among the strongest sectors, while Financials (-0.3%) and Energy (-6.4%) both lagged. In relative contrast, earnings leadership through another strong, and better than expected, reporting season largely retained its cyclical bias.

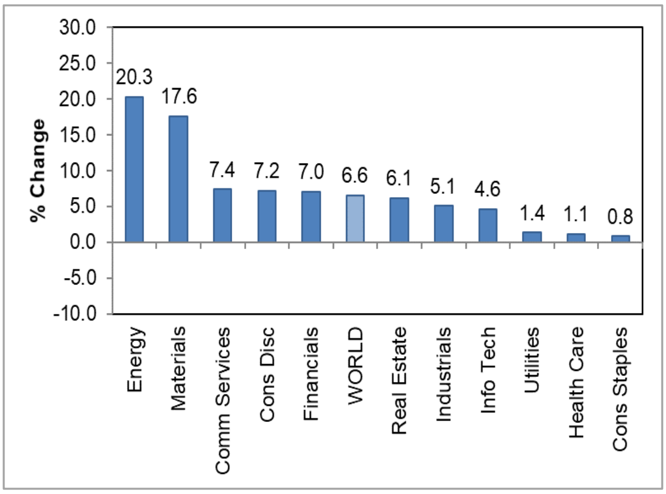
Commodity index rose despite Iron Ore seeing a significant fall



Source: Bloomberg, 8 August 2021

Despite growing concerns about the impact of higher input costs and supply constraints, earnings in the U.S. grew an impressive +101% y/y, which was 15.9% higher than consensus. A similar story played out in Europe, with 33% of companies beating on earnings, and 16 sectors out of 24 beating on margins. Overall, in July, global earnings expectations were revised upwards for both 2021 (+3.2%) and 2022 (+2%), with revisions strongest in Energy and Communications, and relatively weakest in defensive sectors including Consumer Staples and Real Estate (albeit still positive).

Cyclicals continue to see majority of earnings upgrades (3 Month EPS revisions)

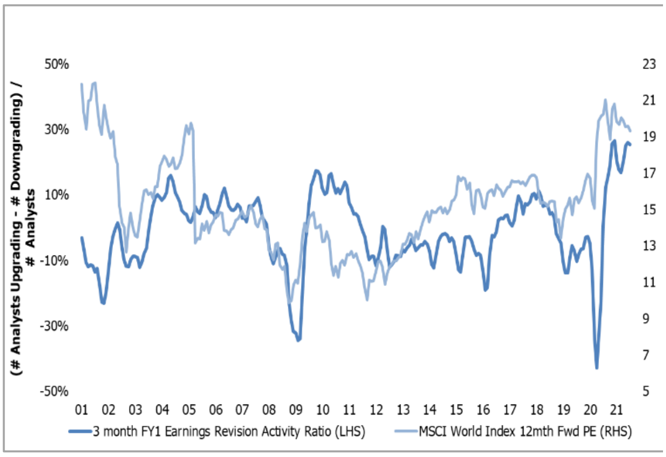


Source: Alphinity, Bloomberg, 2 August 2021

Portfolio comment and outlook

Re-opening of many major economies has driven a powerful recovery in growth, which is now broadening out despite fears around the Delta variant and some new mobility restrictions in some parts of the world. Meanwhile policy makers have remained generally supportive despite some initial talks about tapering, with little apparent appetite to significantly reign in fiscal or monetary stimulus in any of the larger global economies. It's clear that strong inflationary forces are currently in play, however at this stage they appear mostly transitory, in-line with the view of the Federal Reserve.

MSCI World PE vs EPS Revisions activity



Source: Alphinity, Bloomberg, 2 August 2021

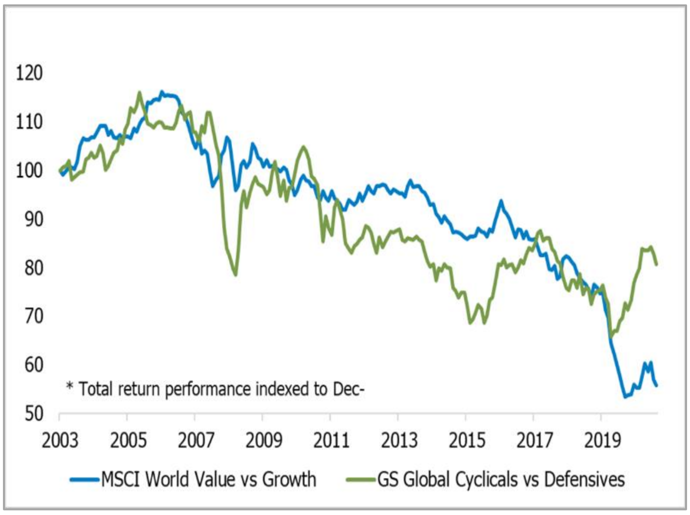
But, of course, this supportive backdrop is now relatively well understood by investors. Equity markets have already rallied strongly, and while corporate earnings have also surged back in-line with growth, this has been needed to justify elevated valuations. In this context, it's understandable that concerns have grown about a potential triple peak in growth, inflation and stimulus, which combined with the spread of the new Covid 'Delta' variant, has tamed the cyclical rally and sent bond yields sharply lower.

Nevertheless, while the most explosive part of the recovery is now behind us, we remain relatively optimistic about the economic outlook. European growth in particular looks set to accelerate over the next few months as vaccine rates continue to improve and economies re-open further. Overall, global growth still seems likely to remain above trend for the next few quarters at least, and policy removal will occur far slower than historically.

As a consequence, and also reflecting current earnings leadership, we have largely maintained our pro-cyclical bias, albeit continuing to shave some positions reflecting the maturing cycle and rising valuations. We are conscious of remaining disciplined on both valuations and quality as we move deeper into the cycle. During the month we reduced our position in Bank of America and sold out of Activision Blizzard, reflecting lower conviction on the outlook for earnings and growing ESG concerns. New positions were initiated in Estee Lauder and Zoetis, both high quality businesses with powerful long-term earnings drivers.

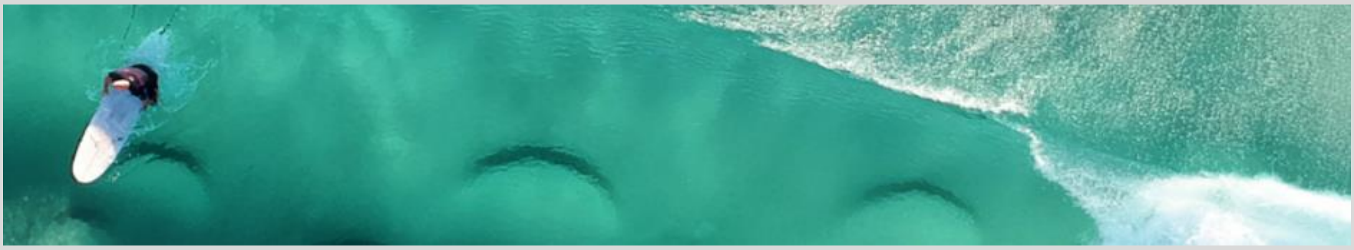
As a reminder, we have remained invested in our favourite growth stocks through the cyclical recovery, which continue to be some of our strongest earnings stories. In contrast, we remain relatively less invested in defensives, which are still facing various earnings headwinds. We are on alert for signs that analysts have over extrapolated current cyclical trends, with overly bullish expectations one of the classic end-of-cycle signals. As always, we will let the earnings leadership guide us through the cycle and avoid making sweeping, lower probability global macro calls in the portfolio.

Global Cyclicals/Defensives YoY Total Return vs Global Value/Growth



Source: Bloomberg, GS Data, 31 July 2021

What's on our mind - Stock in focus
Morgan Stanley – Catching the large waves

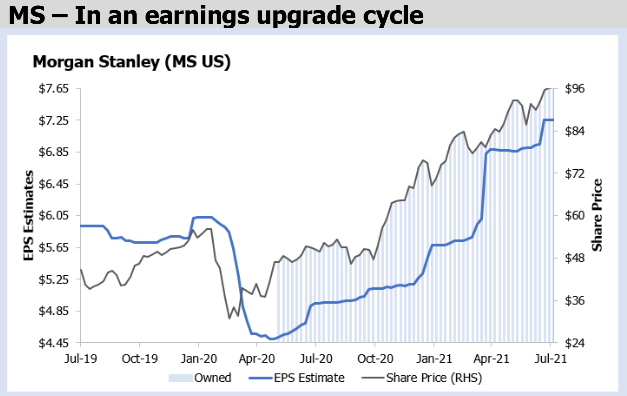


"I think every now and then in a business, you look, and you sort of see a wave coming and you catch the wave and it's a beautiful thing."

In typically bullish words on the recent earnings call, CEO and Chairman James Gorman, talked about Morgan Stanley's (MS) structural growth opportunities in surfing terms, as large waves which MS is positioned right on top of.

Following a decade of rebuilding and investing, MS has reached an important inflection point. The acquisitions of Solium, E*Trade and Eaton Vance have together created a powerful growth platform, which can support a sustained acceleration in earnings over the next several years as they benefit from a range of structural and cyclical growth trends, or 'waves', within the Wealth and Investment Management segments. These include capturing the opportunities within the emerging workplace and digital wealth channels, as well strong trends towards customisation and ESG investing. The acquisitions have also significantly improved the overall earnings mix by diluting the more cyclical and capital-intensive Institutional Securities Group to ~45% of Group earnings and creating a more stable and durable business overall.

MS – In an earnings upgrade cycle



Source: Alphinity, Bloomberg

These positive trends, as well as broader cyclical tailwinds, are already clearly evident in recent earnings reports, which have comfortably beaten consensus expectations and driven significant upgrades to future earnings expectations. This is a trend we expect to continue as these acquisitions are integrated and synergies realised.

All three businesses are also experiencing favourable cyclical tailwinds from strong financial markets and a recovering global economy. A rise in global interest rates could provide further upside to earnings.

In the second quarter, MS reported a return on average tangible common stockholder's equity (ROTCE) of 18.6%, with positive contributions from all three segments. The Wealth Management business was particularly strong, with margins of 27.8% (pre integration expenses), despite headwinds from low rates. Net new assets of $71bn in the quarter brings the year to date total to $176bn (+9% y/y). Overall inflows into Wealth and Investment Management in the first half totalled an impressive $240bn.

At the same time, MS is moving to return excess capital to shareholders. With strong profitability and a common equity tier 1 (CET1) ratio of 16.7%, 350 basis points above their aggregate CET1 requirement, MS recently doubled its' dividend to 70c/quarter (a dividend yield of ~2.8%) and announced a buyback of up to $12bn (~6.5% of the current market capitalisation).

With these cyclical and structural trends still driving upgrades, and trading on a forward price to earnings ratio (PE) of 13.8x with a total capital return yield of up to 9.3%, MS remains a compelling investment and a top five holding in the Alphinity Global Equity Fund.

Morgan Stanley – ESG Considerations

Morgan Stanley the leader among US banks in supporting climate disclosure.

The world's banks are facing immense pressure to move away from fossil fuels to sustainable alternatives. Indirect emissions are under increasing scrutiny, and the risks of loan losses and physical climate exposure are progressively becoming more material. In recognising this, Morgan Stanley no longer finances oil and gas exploration in the Arctic, new coal-fired power plants and thermal coal mines or coal project expansions without carbon reduction technologies.

The firm was the first US-based bank to commit to net-zero financed emissions by 2050. It is working closely with the Partnership for Carbon Accounting Financials to disclose their own financed emissions, but also is working with the Steering Committee to improve the methodology behind assessing environmental impacts of investment portfolios and loan offerings. While it is encouraging to see Morgan Stanley's leadership, the critical next step is to review their exposure and assess mitigation strategies, particularly in high emitting sectors such as energy and agriculture.

The prominent shift of Morgan Stanley's approach to the culture of inclusion.

Last year, diversity and inclusion was added as a fifth core business value, the Institute of Inclusion was created, and the global Head of Diversity and Inclusion was fast tracked to join the senior management committee well ahead of the 2021 proposal. Yet, Morgan Stanley lacks groupwide targets and only aims to achieve a minimum 30% female representation in senior management in the UK.

The firm has acknowledged that diversity is a long game – it does not change overnight – and assures that these changes serve to explicitly create an integrated and transparent diversity, equity and inclusion strategy and focus responsibility on policies and target setting.

Sustainability at Morgan Stanley

For more than a decade, Morgan Stanley has focused on integrating sustainability into core businesses and support functions. We execute innovative solutions that address complex environmental, social and governance (ESG) issues on behalf of our clients to help drive revenue opportunities, and take a forward-looking approach to sustainability in our operations and disclosure.

Traveller's Tales

Thank goodness for the Olympics. It was postponed last year due to the pandemic and even as recently as last month there was ongoing debate and dissent in Japan as to whether it should go ahead at all considering the state of emergency in force there. The rest of us are glad that it did as it provided a welcome distraction for those in lock down and trying to avoid catching/spreading the disease. It has been a bit confusing sometimes though, considering the games are still officially called Tokyo 2020 even though it is now only a few months until the 2022 Winter Olympics in Beijing, China. The cost of all the disruptions to the organisers must be immense, but our reward for Japan's pain has been a lot of entertainment and a slew of medals for Australia in many different sports. And when the Olympics is done we have the Paralympics to look forward to.

A fact little known to many of our investors is that Alphinity has its own Olympian. Portfolio Manager and health care/ transport/building materials guru Stuart Welch competed and won medals rowing in the Men's Eights at both the Sydney Olympics in 2000 and the Athens Olympics in 2004. A keen rower at school and throughout university, he is still involved in the sport at a high level as a director of Rowing NSW and Vice President of the UTS Rowing Club.

There aren't many people who join this industry and end up travelling less but Stuart is one. Over 14 years of competitive rowing he raced in countries across Europe, North America, South America, Asia, Australia, and NZ. While with the Australian Institute of Sport he would spend two months each year training on Lago Di Varese in northern Italy. Sounds glamorous, and it is, although he says the best rowing course in the world is actually at Lake Barrington in Tasmania.

He has lots of stories about the places he's been and races he's been in. Motivational talks from America's Cup skipper John Bertrand before the Olympic final in 2000 and mentoring from Wallabies captain John Eales in 2004. Being invited to race in Valdivia, Chile, where his team was provided with a rickety old boat that was held together with duct tape; the hosts were in an Italian carbon fibre job and, of course, won the race. A similar thing happened at an invitational in Jilin, China.

His most memorable trip though was coming home with all of the athletes from Athens in a dedicated Qantas 747 the morning after the closing ceremony. Gold medal winners were placed in first class, Stu was in Business with the other Silvers and Bronzes; all the non-medallists were way down the back. A lot of fun was had on the plane and on arrival they reunited with family and friends in a hangar at Mascot. Sadly this year's athletes are facing a more subdued return to Oz, straight into two weeks quarantine.

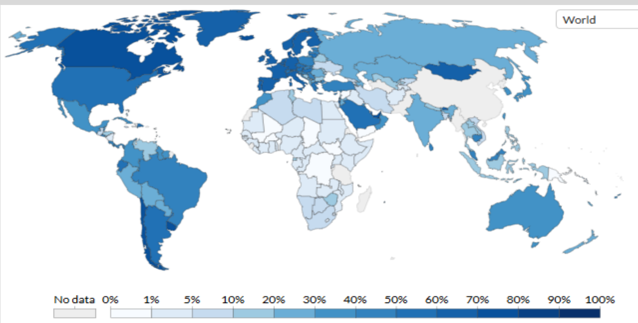
BTW

The head of the US Centre for Disease Control said this month that the Delta variant of Covid-19 is "one of the most infectious respiratory viruses we know of". It is now the dominant strain in the US, accounting for 90% of infections there, wreaking havoc in communities with low vaccination rates. There seems to be a political divide, with states that had most strongly supported ousted President Trump making up many of the vaccine-resistant regions. This seems a little odd considering one of the things of which Trump should be most proud is the way his administration drove the effort to develop the vaccines in 2020: one would think his supporters would also support the vaccines that were developed, but it seems not.

This time last year there were overflowing emergency wards in countries like the USA, UK and Italy, shortages of ventilation equipment and essential gasses, thousands of deaths daily – including of many health professionals caring for the infected – and so on, it is clear just how far the world has come. A year ago there was no vaccine and many experts were pointing out that no one had ever developed a successful vaccine for a coronavirus.

Equally, no one had ever thrown such immense resources at developing a vaccine for a coronavirus and, in an incredible triumph of medical science, by November last year several had been developed and proven. Approval was fast-tracked in some countries. The first was administered in the UK in December and by the end of July, only eight months later, 4.1 billion doses have been given worldwide; more than a billion people, almost 15% of the world's population, have been fully vaccinated and many more are only a jab away from being the same.

The vaccines however have not been evenly distributed. Those who developed the vaccines and had the biggest emergencies – especially US and Europe – have achieved very good coverage but less-developed countries are lagging. The chart below from ourworldindata.org shows first doses, which provide some coverage and indicate an intent of full vaccination, and the African continent has had very little. China apparently has a good level of coverage but is loath to disclose its numbers. It is also suffering Delta outbreaks in some cities. Countries that didn't suffer the worst impacts of the disease – ourselves and New Zealand, Taiwan, Vietnam and Thailand for instance – ended up scrambling for allocations.



There are glimmers of hope, however. The first piece of good news is that, despite a resurgence of infections in many other places, Covid hospitalisation and deaths in highly-vaccinated populations are substantially lower than was the case before the vaccines were available. This suggests that the vaccines currently being used in most places are working, even against Delta. The second piece is that vaccination supply is ramping up rapidly. Until quite recently some sections of our population has been reluctant to be vaccinated and, for those who were willing, not enough supply of the "right" sort of vaccine after a misguided but highly-effective campaign against the AstraZeneca vaccine in the media and even by some health professionals.

This is particularly unfortunate because of all the vaccines the Anglo-Swedish AstraZeneca seems to have the best ethical framework. It was developed by company with Oxford University but, unlike all the US vaccines, AZ took the moral stand at the start of the pandemic that it would not seek to profit from it. AZ is selling it to governments all around the world at cost and even donating some to poor countries. It is also allowing various parties around the world to make it, and since March it has been produced in vast quantities in Australia by portfolio holding CSL. It is therefore a "cheap" vaccine, selling for between $2 and $4 per dose in different parts of the world.

By contrast, Pfizer has charged what the market will bear, meaning $20-50 per dose according to some sources (actual prices are top secret). This is what you might expect a commercial operation to do, especially one which developed a whole new way of making vaccines, but it's not as noble as AZ has been. When you multiply those high prices by the ~15 billion doses that will be required to vaccinate the world, before you start factoring in the inevitable booster shots, the difference is stark. In the latest US earning season Pfizer reported record earnings and its share price jumped sharply. Same with Moderna.

Back home, as larger quantities become available in coming weeks we can look forward to the supply issue disappearing; and the reality of an easily-spread but preventable illness and the suffering and death it can cause, not to mention the great inconvenience, mental stress and financial loss resulting from lockdowns, seems to be solving the demand issue. All of a sudden people are clamouring for their jabs so the confluence of adequate supply and intense demand should result in a much higher vaccination rate within months. Our shading on the map should become a darker blue reasonably quickly.

Will it be enough to ease up on the draconian international travel restrictions we are living under? We can only hope. While not being able to go anywhere was quite pleasant for a while, we are all starting to develop itchy feet and keen to get back out there. If we can achieve strong take-up rates who knows, we might be back winging our ways around the world again in 2022.

Performance[1]	Quarter %	6 months %	1 year %	3 years % p.a	5 years % p.a	Inception % p.a[2]
Fund return (net)	15.4	28.2	38.7	18.8	18.5	15.5
MSCI World Net Total Return Index (AUD)[3]	10.1	21.3	31.8	15.0	15.1	13.5
Excess return[4]	5.3	6.9	6.9	3.9	3.4	2.0

Fund facts	
Portfolio managers	Jonas Palmqvist, Jeff Thomson, Nikki Thomas, Trent Masters, Mary Manning
APIR code	HOW0164AU
Inception date	21 December 2015
Investment objective	To outperform the MSCI World Net Index (AUD).
Management fee	1.00% p.a.
Performance fee	10% of the excess return of the Fund above the Performance Benchmark (MSCI World Net Return Index (AUD)) and only paid if performance is above the Performance Hurdle (Reserve Bank of Australia cash rate target). Any negative or unpaid performance is carried forward to the next period.[1]
Buy/sell spread	+0.25% / -0.25%
Fund size	$136M
Distributions	Annually at 30 June
Min. Investment	$10,000
Max. cash position	20%

Top 10 positions

Company	Sector	%
Alphabet Inc	Communication Services	6.4
Morgan Stanley	Financials Ex Prop	5.2
Microsoft Corp	Info. Technology	5.2
Target Corp	Cons. Discretionary	4.3
Danaher Corp	Healthcare	4.2
ASML	Info. Technology	4.0
Otis Worldwide	Industrials	3.9
Keysight Technologies Inc	Info. Technology	3.6
Blackstone	Financials	3.6
Prologis	Property Trusts	3.6
Total		**44.1**

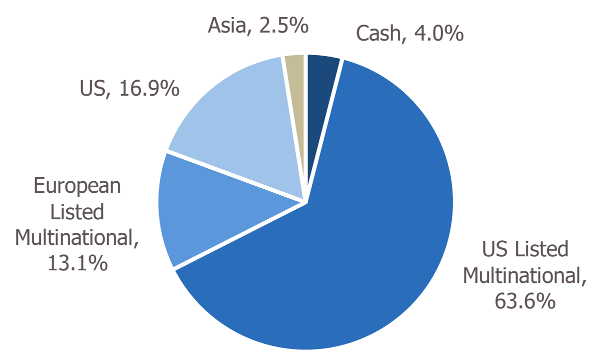
Data Source: Fidante Partners Limited, 30 June 2021.

[1] Returns are calculated after fees have been deducted and assume distributions have been reinvested. No allowance is made for tax when calculating these figures.

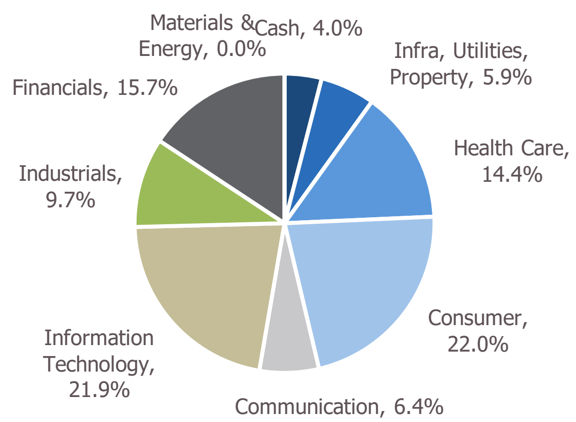
[2] The inception date for the Fund is 21 December 2015

Fund features
Concentrated: A long only, concentrated portfolio of 25-40 of our best ideas, highly diversified across sectors and regions. A truly global fund consistently exposed to powerful trends reshaping our world.
Discipline: A disciplined process finding quality businesses with strong earnings that are under appreciated by the market. This approach has proven successful across different market cycles.
Talent: A united and deeply experienced team of global portfolio managers each with over 20 years in the industry.
Aligned: Alphinity Investment Management is a boutique firm, strongly aligned with its clients' investment objectives and focused solely on growing clients' wealth.

Geographical exposure



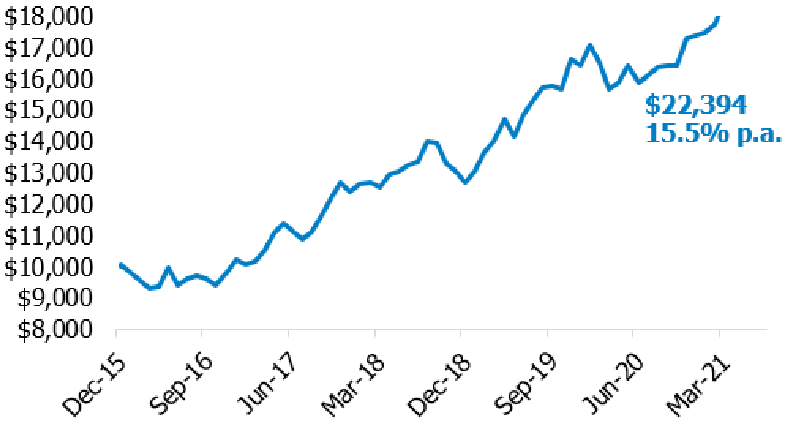
Sector exposure



[3] From 21 December 2015 to 31 March 2019, the Benchmark was the MSCI World Equity ex Australia (Net) Index. The current index is effective from 1 April 2019.

[4] Numbers may not add due to rounding

Growth of $10,000 (net of fees)



For further information, please contact:

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