MARKET MATTERS
INVEST

MONTHLY REPORT | SEPTEMBER 2022 | ACTIVE HIGH CONVICTION

PORTFOLIO DETAILS

Portfolio Name	Active High Conviction
Structure	Separately Managed Account
Benchmark	S&P/ASX 200 Accumulation
Management Fee	0.85% incl GST
Platform	Open Wealth | Praemium
Included Assets	Equities, ETFs
Portfolio Manager	James Gerrish
Annual Performance	5.45%*

**Inception Date 10.05.2016*

OBJECTIVE

The objective of the Market Matters Active High Conviction Portfolio is to provide an active exposure to Australian large-cap shares, with reduced volatility. Returns will be achieved through a combination of capital appreciation and income with an overall objective of outperformance of the S&P/ASX 200 Accumulation Index over the medium term, (3 years).

MARKETS & PERFORMANCE

The Market Matters Active High Conviction Portfolio declined 5.71% in September, outperforming the S&P/ASX 200 Accumulation Index which fell 6.17%. The portfolio has returned -6.02% for the rolling 12 months, 12.88% per annum over 2 years, 1.91% per annum over 3 years & 5.45% per annum since inception.

PERIOD	1 MONTH	3 MONTH	6 MONTH	1 YEAR	2 YEAR PA	3 YEAR PA
PORTFOLIO %	-5.71	5.25	-9.88	-6.02	11.93	1.91
BENCHMARK %	-6.17	0.39	-11.56	-7.69	9.80	2.67
RELATIVE %	0.46	4.86	1.68	1.67	2.13	-0.76

Benchmark: S&P/ASX 200 Accumulation

Equities struggled in September on the back of global recession fears and an increasingly hawkish US central bank. The MSCI Developed Markets Index fell 8.3% while the US S&P 500 was worse, dropping 9.2% in local currency terms.
Australian stocks were down but outperformed global peers. The S&P/ASX 200 fell 6.2% over the course of the month, as investors priced in the most aggressive RBA rate hiking cycle since the 1990s. There was carnage in bond markets as they reflected an increasingly hawkish outlook, the Australian 10-year yield hitting a yield of 4.10%.

Over the pond, US yields rose 67bps to 3.80%, driven by better-than-expected economic data firming expectations around future interest rate hikes.

Commodity prices fell in September, Brent Oil prices declined US$9 to US$88/bbl amid concerns of slower global growth. Iron Ore prices held up relatively well, off just US$1 to US$98/Mt while gold prices were hit by continued strength in the US dollar, bullion down US$44 to US$1,672.

Locally, the material sector was the top relative performer down by ‘only’ 2.3% for the month, while Energy -3.8%, Healthcare -4.4%, Consumer Staples -5.4% & Communication Services -6.1% did better than the broader market. The underperforming sectors included Financials -6.5%, Consumer Discretionary -9.1%, Industrials -9.8%, IT -10.6%, Property -13.6% and Utilities -13.8%.

PORTFOLIO STOCKS

The portfolio held 20 positions at the end of September and was back to being fully invested by the end of the month, having run cash up to around 14% in August. It was a tough month from a performance perspective, the portfolio down nearly 6% clearly shows as much, the only slight solace being outperformance versus a weak benchmark which fell more.

Despite the sharp decline during the month, we are actually very positive about the positions within the portfolio if our views around the macroeconomic backdrop come to pass. Put simply, we believe that the strange sequence of events in the UK has created a 'blow-off' style top in bond yields, and when interest rates do top out, equities will enjoy a rally into the latter part of the year. Most in the market will shun macroeconomic forecasts, however, at Market Matters we believe it is incredibly important to have a handle on the external influences impacting company valuations, and we continue to put a lot of work into developing & refining our macro roadmap during a fascinating time for markets.

We were active in the portfolio during September, increasing exposure to rate-sensitive pockets of the market with a specific focus on beaten-up technology stocks.

We initiated new positions in **Seek (SEK), REA Group (REA) & Megaport (MP1)**, two of which are highly profitable growth stocks trading more than 50% below their prior peak while the 3rd (MP1) is more speculative in nature, and not yet profitable.

Online real estate platform **REA Group (REA)** was bought during the month on two separate occasions, our preferred strategy of accumulating on the back foot into weakness was clearly obvious here. While we are very comfortable with the quality of the business and the dominance of its market position, these attributes were also well known when the stock was trading at ~$180 midway through 2021.

PORTFOLIO STOCKS	
NO. OF HOLDINGS	20
ESTIMATED YIELD (%)	3.92
TOP 5 POSITIONS (% OF AUM)	35.01
TOP 10 POSITIONS (% OF AUM)	58.70

STOCK	CONTRIBUTION (%)
BHP GROUP (BHP)	0.32
RESMED (RMD)	0.20
IGO LIMITED (IGO)	0.16
OZ MINERALS (OZL)	0.41

STOCK	DETRACTION (%)
GOODMAN GROUP (GMG)	-1.04
RAMSAY HEALTHCARE (RHC)	-0.78
XERO (XRO)	-0.74
MACQUARIE GROUP (MQG)	-0.69
ILUKA (ILU)	-0.55

%	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	YTD
FY23	8.16	2.80	-5.71										**5.25**
FY22	0.25	2.53	0.78	1.75	-3.49	2.72	-4.00	2.06	5.51	-2.30	-4.69	-7.70	**-6.58**
FY21	0.27	4.94	-4.10	-1.07	14.87	1.34	-0.50	3.08	0.66	4.10	1.17	2.70	**27.46**
FY20	1.21	-2.16	3.75	-1.55	0.80	0.34	2.06	-10.25	-24.12	12.66	5.30	2.02	**-9.94**
FY19	1.11	1.64	-0.77	-2.16	-1.22	-1.94	3.39	4.98	-1.00	2.39	1.72	4.41	**12.55**
CUMULATIVE													**28.74**

Rising interest rates & prevailing views around the housing market are key determinants of what the market is prepared to pay, and these concerns pushed REA to a low of $93. While we did not buy the low, we believe the risk/reward was attractive ~$120, with the view that REA will be a major beneficiary when bond yields ultimately stabilise.

Seek (SEK) was also added to the portfolio in September below $20 having been as high as $36 in the last 12 months. We have followed the online recruitment company that has well-documented global ambitions for many years, holding the stock at various times. As global interest rates moved ever higher, Seek continued to trade lower, once again presenting a solid risk-adjusted entry point for our purchase.

We expect profit to be substantially higher in FY23 and while a PE of 42x will be off-putting to some, this must be considered in the context of their ability to drive sustainable earnings growth over time, while the macro-economic headwinds faced over the last 12 months will ultimately subside.

The third in our trio of new stocks is software-based elastic connectivity provider, **Megaport (MP1)**. Unlike REA & SEK, MPI has had several operational issues which put a huge question mark over its capacity to grow at the rates implied by the multiples it was trading on, and when we overlay operational concerns with a debilitating macro backdrop for companies focussed on monetising a big idea, the share price carnage was breath-taking.

Megaport shares were selling for $22 less than a year ago, hitting a low of under $5 in June. We paid ~$7.50 and we like management's current focus on profitability and commitment to achieving free cash flow breakeven by the end of FY23. While we can easily see MP1 trading back into the $11-12 area this year, we're not considering a retest of the $20 region any time soon.

Ramsay Healthcare (RHC) and a consortium of investors led by private equity powerhouse KKR have finally parted ways after a drawn-out process of 15 months that lined the pockets of many financial bankers but alas not shareholders like us. The RHC board refused to take an alternative to the original $88 all-cash bid by KKR, and both parties decided to bin talks, prompting a sell-off in RHC shares which quickly became one of the largest detractors on performance for the month.

Overall, our sympathies lie with the suitor KKR as they were unable to gain access to Ramsay Santé books and RHC itself delivered a lacklustre FY report including small downgrades into FY23 & FY24. If we believe the press, it was an acrimonious parting with both parties blaming each other and shareholders missing out again!

At this stage, there appears to be no alternative to the RHC board which is frustrating as a shareholder given there was undoubtedly an enthusiastic buyer at the table over a year ago at share price levels not seen ever before. We do see value in RHC, and our first inclination was to average our existing position, but with stocks that have delivered strong earnings in the recent reporting season pulling back in a weak market, we felt better value alternatives lay elsewhere. We continue to hold a position in RHC.