Maple-Brown Abbott Australian Geared Equity Fund Retail

Monthly Commentary - December 2020

FUND PERFORMANCE (%) [1]

	1 month	3 months	1 year	3 years p.a.	4 years p.a.	5 years p.a.	Inception p.a. 30 Sep 2002
Fund [2]	2.2	34.2	-22.9	-5.5	-1.7	3.5	2.6
Benchmark [3]	1.2	13.7	1.4	6.7	8.0	8.7	9.0

MARKET COMMENTARY

The Australian equity market had a good finish to a volatile year, with the S&P/ASX 200 Index (Total Returns) rising 1.2% in December. Global markets were generally solid, with Australia outperforming in constant currency terms. Local economic data was improved, including some positive signs from the labour market and strength in retail sales and housing. The Australian Government 10-year bond yield rose 0.07% to close at 0.97% and the AUD rose materially against the USD. Commodity prices were also generally higher, most notably for iron ore which has now pushed above US$150/t. Looking at performance by sector, Information Technology (+9%) was strongest, followed by Materials (+9%) and Consumer Staples (+2%). Utilities (-5%) was weakest, followed by Health Care (-5%) and Industrials (-3%). Financials (-1%) also underperformed.

PORTFOLIO COMMENTARY

The portfolio returned 2.2% in December, outperforming the benchmark by 1.0%.

The gearing level of the Fund as at end of the month was 43.32%.

Our resource holdings were significant positive contributors to performance, including positions in BHP Billiton (+12%) and Sims Group (+19%). BHP was supported by strength in prices for its key commodities including iron ore and oil. Similarly, Sims Group benefited from improved steel scrap demand and prices. Our overweight holding in Metcash (+17%) also performed very well. Metcash's three divisions of grocery, liquor and hardware wholesale have all seen an uplift in demand due to COVID-19 and this drove a very strong half-year result released during the month. Our decision not to hold health care growth stocks CSL (-5%) and Cochlear (-14%) also contributed positively, lagging due to currency headwinds and a rotation out of defensives.

Our decision not to hold Fortescue Metals Group (+29%) was a significant negative contributor to performance. Fortescue is particularly sensitive to the iron ore price and has been the biggest beneficiary of the strength noted earlier. Our decision not to hold hyper-PE growth stocks Afterpay Touch Group (+24%) and Xero Limited (+11%) also detracted. We view the valuations on these stocks as incomprehensible, with Afterpay now capitalised at more than Coles Group yet never having made a profit. Of stocks that we hold, QBE Insurance (-15%) contributed negatively. The company provided a disappointing trading update, with earnings impacted by rising re-insurance costs and claims inflation.

Please see next page for Outlook

Notes:

1 Past performance is not a reliable indicator of future performance. Source: Maple-Brown Abbott Ltd, S&P as at 31 December 2020.
2 The Fund's performance relates to retail investors only. If you are a wholesale investor, you can obtain up to date returns at maple-brownabbott.com.au. Total return is based on the movement in withdrawal price per unit plus distributions and is before tax and after all fees and charges. Imputation credits, foreign income tax offsets and entry fees, are not included in the performance figures.
3 Benchmark: S&P/ASX 200 Index (Total Returns).

WANT TO FIND OUT MORE?

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OUTLOOK

2020 was a year of extreme volatility. The emergence of the COVID-19 pandemic saw the ASX300 Index (Total Returns) fall 36% from peak to trough during February and March, then rebound quickly in subsequent months supported by low interest rates and government stimulus. November marked the next stage of the recovery, with optimism around an effective COVID-19 vaccine and a re-opening of economies driving a surge in global equity markets. The S&P 500 finished the year at all-time highs and the Australian market only 5% off its February peak.

We have previously discussed the significant divergence in valuations that exists across the market, with some segments looking attractive and others extremely expensive. This divergence has been building steadily over the last decade, with the most premium valued stocks (notably health care and Tech stocks) becoming more so and the cheapest stocks seeing little uplift. As value investors, our focus is on stocks evidencing strong valuation support; often out-of-favour stocks that have faced shorter-term challenges but where we believe better long-term prospects are being ignored by the market. Hence, this market dynamic has created significant headwinds for our performance and of the value style more generally. Typically, bear markets result in a change of market leadership – whereby expensive in-favour stocks that drove the market higher underperform and valuation dispersions narrow. This was not seen in the bear market of 2020 nor in the initial rebound.

November saw a significant shift in sentiment, with increased optimism around the economic outlook starting a rotation into cyclical stocks and particularly those that had been most impacted by the COVID-19 pandemic. Our portfolios are overweight these segments and hence we achieved very strong outperformance for the final quarter of the year.

We are encouraged by the recent rebound in performance but expect ongoing volatility ahead. That said, we continue to see material opportunity for the value style to outperform as economic conditions normalise. Many of our out-of-favour holdings remain well below their past highs and we would expect a recovery in earnings to support their performance. In contrast, many of the highly rated growth and yield stocks that we don't own remain near their highs and are yet to de-rate from excessive valuations. The valuation dispersion between these groups remains at extreme levels that cannot be sustained indefinitely and we expect further rotation to support a further recovery in our performance.

For latest Fund factsheet click here.

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