BLACKMORE CAPITAL
EQUITY INVESTORS

Blended Australian Equities Portfolio

Q3 FY21 Quarterly Investor Letter | March 2021

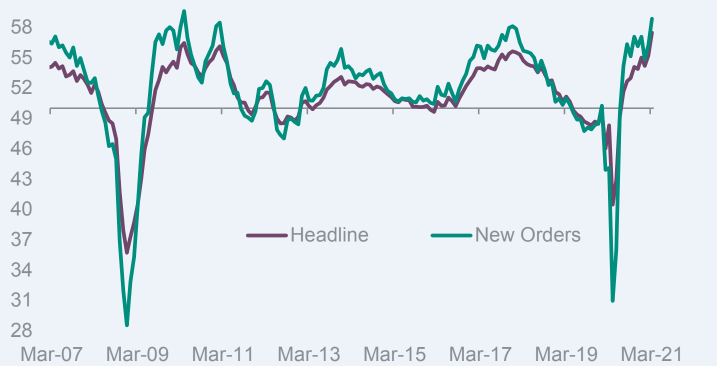
> "The recovery has progressed more quickly than generally expected and looks to be strengthening. But the recovery is far from complete, so, at the Fed, we will continue to provide the economy the support that it needs for as long as it takes."
>
> **Federal Reserve Chairman Jerome Powell**

Equity markets made it to the end of the first quarter of 2021 demonstrating bulletproof resilience. The opening months of the year have not provided anything like the scale of the "once in a century" pandemic shock that global economies faced in the same period in 2020.

We have just passed the 1-year anniversary for the trough in global equity markets. The event-based pandemic led to one of the sharpest contractions and rebound in equity markets.

What is clear that the magnitude and breadth of the response by government and central banks combined "firepower" of fiscal and monetary policy measures successfully inoculated economies from the worst effects of the lockdowns. Combined with the successful discovery of a COVID-19 vaccine the result has been that consensus estimates for the global economy and earnings have consistently under-estimated the speed and magnitude of recovery.

Global manufacturing PMI is rising to yet another new high



Source: Markit, Haver Analytics, IMF, national sources, Morgan Stanley Research. Note: Prior to Apr-11, Canada, Indonesia, & Colombia are excluded from Global aggregate due to lack of data. India, Norway, Mexico and Colombia are excluded from all charts in this publication due to unavailability of the March 2021 data.

In FY21 earnings and dividends collapsed by >20%, however, evidence of earnings and dividend recovery was remarkedly quick with the 1H21 results season being the strongest in terms of earnings revisions.

Bond yields have pushed higher as global economies continue to recover, while stock indices are sailing higher shifting their enthusiasm from growth stocks toward value and cyclical recovery plays. Climbing bond yields have posed a challenge to the ascendancy of growth/tech focused companies but have underpinned an impressive rise in resource and banking shares over the March quarter. The bank and commodity sectors have been notably supported by the 1H21 earnings reporting season which delivered the strongest upgrades to earnings expectations in more than 20 years.

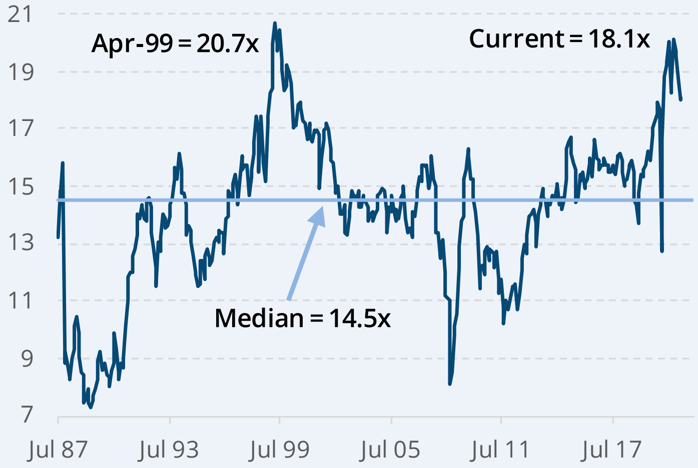
Whilst the foundations of a broad economic recovery continue to provide ballast to an earnings and dividend uplift such as the banks and resource sectors, our attention has shifted to allocating new capital to quality companies that have lagged the recent sharp rally in equity prices. Notably, we see investment opportunities in stocks that have markedly underperformed in the latest part of the rally, namely:

- Offshore earners: Amcor, Brambles & CSL
- Reopening recovery plays: Ampol & Ramsay Health Care.
- Attractive dividend payers: Waypoint REIT.

Nonetheless, with equity prices elevated at levels well above long term averages we need to be conscious there are several factors that could pose a challenge to risk assets. Specifically, there are growing signs that the vaccine rollout in Australia and across many countries are facing unforeseen complications around efficacy and delays to distribution potentially delaying a full recovery in economic activity. Caution is also warranted over the historic level of liquidity and stimulus being used to support growth with the risk that economies become overheated fueling the need for higher interest rates to curb excess activity.

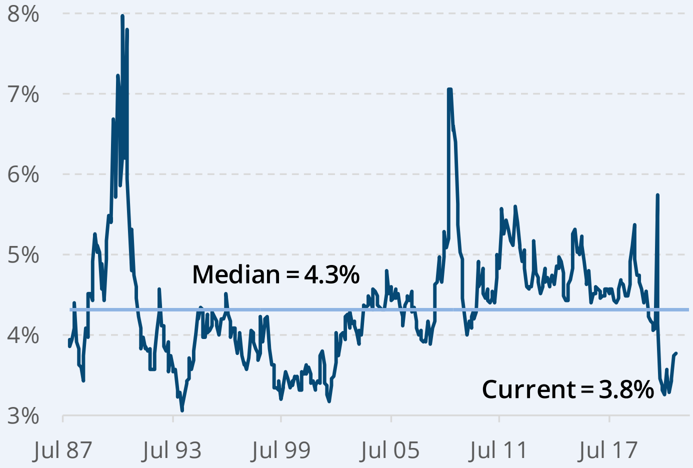
Yet for now, the only thing that matters to asset prices is fiscal & monetary policy largesse. From an equity market perspective current valuation (12-month forward PE for the ASX 200 ~18.1 times) the economic recovery is now largely priced into the ASX 200 following a ~50% rise in equity prices from trough in March 2020. Indeed, the market is now adequately reflecting the earnings recovery and upside will be more limited from here.

ASX 200 12-month forward PE – A bullish de-rating



Source: MST Marquee

ASX 200 12-month forward Dividend Yield is rising



Source: MST Marquee

What is more interesting is the rotation we are already seeing within sector performance. The first recovery plays (commodities, banks) have started to plateau after significant outperformance this year. Overall, we are seeing earnings revisions moderating and outperformance maturing.

Our preference remains with Quality and Value, where our attention is now focused a stocks' that have lagged in the recovery rally.

The Blended Australian Equity Portfolio finished the March quarter up 4.04% (+4.46% inclusive of franking credits) compared to the ASX Accumulation Index up 4.26%. Positive attribution for the Blended Australian Equity Portfolio was driven by Westpac (WBC), News Corporation (NWS) and BHP Group (BHP). Whereas Northern Star (NST), Ampol (ALD) and Cleanaway Waste Management (CWY) weighed negatively on attribution.

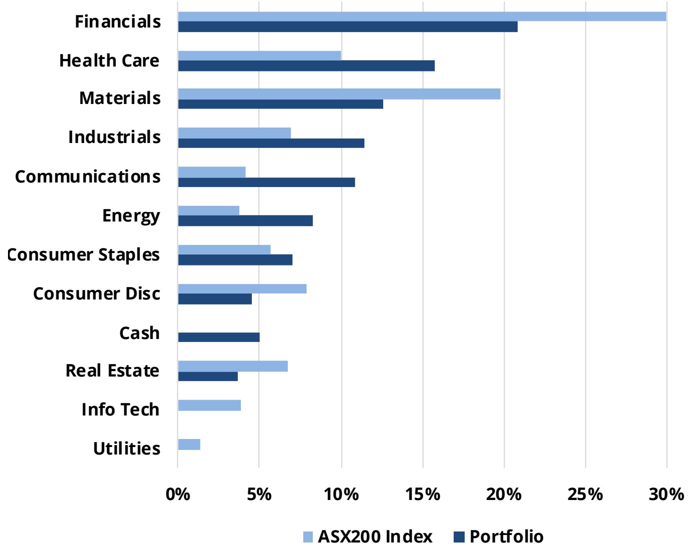
Investment Performance since Inception (%)

Portfolio returns

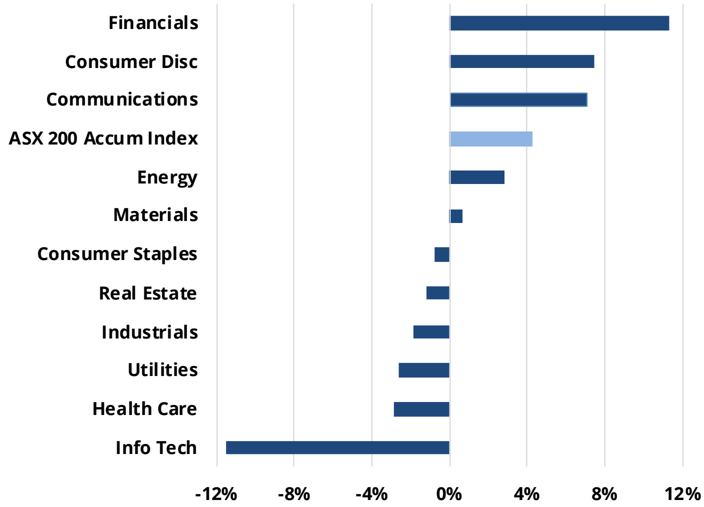
	1 mth	3 mths	6 mths	FYTD	1 Yr	3 Yr	5 Yr	Inception p.a	Since inception	FY15	FY16	FY17	FY18	FY19	FY20
Portfolio performance	2.2	4.5	15.3	15.5	33.0	11.6	11.5	11.0	110.3	15.4	6.1	11.2	16.6	13.5	-1.4
ASX 200 Accum Index	2.4	4.3	18.5	18.0	37.5	9.7	10.2	7.7	69.1	5.7	0.6	14.1	13.0	11.5	-7.7
Relative performance	-0.2	0.2	-3.3	-2.5	-4.5	2.0	1.2	3.3	41.1	9.7	5.6	-2.9	3.6	2.0	6.3

Figures shown are before fees and inclusive of franking credits

Relative sector weights - March 2021



Sector returns - Q3 FY2021



Past performance is not an indication of future performance

Appendix

Portfolio Objective

The portfolio seeks to generate long-term capital appreciation by investing in Australian listed equities. The portfolio aims to do so with lower volatility and greater downside protection relative to the ASX 200 Accumulation Index benchmark.

Investment Principles

Our investment approach aims to generate long-term risk adjusted returns, by investing in companies that focus on producing high-quality earnings and operate in industries that exhibit favourable long-term growth prospects. More broadly, we consider a range of attributes which we view as important qualities in the companies we invest in. We construct and manage the Blended Australian Equities Portfolio with eight consistent guiding principles:

- Grow capital and income over the long term;
- Focus on the quality of company earnings;
- Identify quality assets at an attractive valuation;
- Generate a suitable return on capital employed;
- Invest in companies operating in robust industry structures;
- Select for balance sheet latency and sustainability of dividend income;
- A corporate governance structure that actively promotes alignment with key stakeholders; and
- A vigilant process of portfolio risk analysis.

Benefits of Active Management

Performance and Risk (%) Comparison since Inception

A key benefit of active portfolio management is the recognition that return, and risk are inseparable. A core portfolio objective of the Blended Australian Equity Portfolio is to generate returns that exhibit lower volatility and greater downside protection relative to the ASX 200 benchmark index. The accompanying chart illustrates the value of understanding the interlocking nature of return and risk.

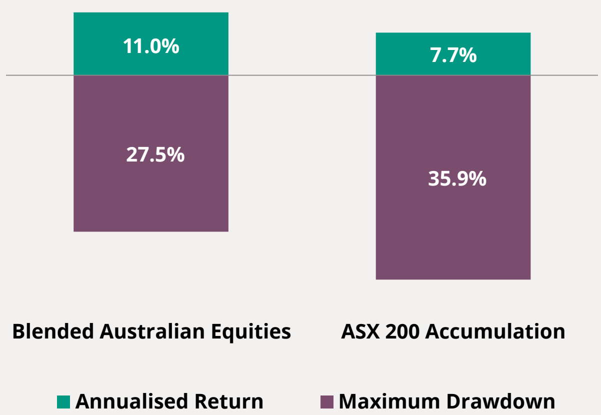
The chart below shows both the annualised return (green bar) generated by the Blended Australian Equities Portfolio compared with ASX 200 Accumulation Index, and the maximum loss/drawdown (purple bar) in the value of the portfolio compared to the ASX 200 Accumulation Index since the inception of the portfolio in February 2014. Maximum drawdown measures the magnitude of the worst loss an investor would have incurred by investing in the portfolio or benchmark. Drawdown is a useful measure of risk management, as it indicates the portfolio's response to periods of market stress as well as the relative sensitivities to market risk.

Our investment stance is predicated by two central tenets:

- At a portfolio level we want to broadly participate when equity markets rise, but importantly we want the portfolio to be able to decline less when the market declines; and

- With a portfolio buttressed by a solid cash position, we can be more assertive in participating when the market is low, thus providing a better chance in participating meaningfully in a subsequent market recovery.

Return and Drawdown since Inception



Platform availability

Research Ratings

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