JM Financial Group

Issue 77: September 2021

Australian Equities Strategy – Investment Newsletter

Performance *(As at 30th September 2021)*	Month (%)	Rolling 3 Months (%)	Rolling 1yr (%)	Rolling 3yrs (%)	Inception Gross (%)	Inception Annualised (%pa)
JMFG Australian Equities Strategy	**-0.43**	**-0.52**	**+15.88**	**+26.60**	**+86.17**	**+8.95**
All Ords Accumulation Index	-1.58	+2.05	+31.46	+34.44	+90.46	+9.29
Outperformance	**+1.15**	**-2.57**	**-15.58**	**-7.84**	**-4.29**	**-0.34**

Although the JMFG Australian Equities Strategy is generally representative of client portfolios, Individual performance may differ from the results above. These differences can arise due to various issues, some of which may relate to initial timing of investments, and cash inflows and outflows. Performance is calculated on a TWRR basis after management fees (post 1 Jan 2017), performance fees (paid or accrued), GST, and excludes the effect of franking credits. Strategy Inception for Performance Data is July 1st, 2014.

Month in Review – A review of the share market and overview of the portfolio for September

For the month of September, the JMFG Australian Equities strategy outperformed its benchmark by 1.15%, finishing the month slightly down by 0.43%. This improvement in relative performance is a pleasing development and brought the 12-month return to 15.88%, after fees and taxes. Whilst the strategy has underperformed the benchmark in recent times, we see encouraging signs of improved performance from many of our individual holdings, as alluded to in the August newsletter, and are anticipating some more positive months leading up to Christmas.

The best-performing sector for September was Energy which rose by 16.7%. Other strong-performing sectors in September were Utilities +2.5%, Financials +1.6%, and Telecommunications +1.3%. Materials was again the worst performing sector falling 9.3% on the back of a continued weakening of the iron ore price. Other weak sectors included HealthCare -4.9%, Information Technology -3.9%, and Property Trusts -2.2%. Industrials and Consumer Discretionary sectors both fell only marginally.

Trading was minimal during September as the market moved from reporting season to looking outward at macro-economic drivers as the world looks to post-pandemic vaccine-managed operations. Overall, we increased portfolio exposure to income yielding financial services and mining and materials stocks, and reduced exposure in underperforming software technology and healthcare device technology stocks. The cash position was slightly increased as a result of trading activities during the month.

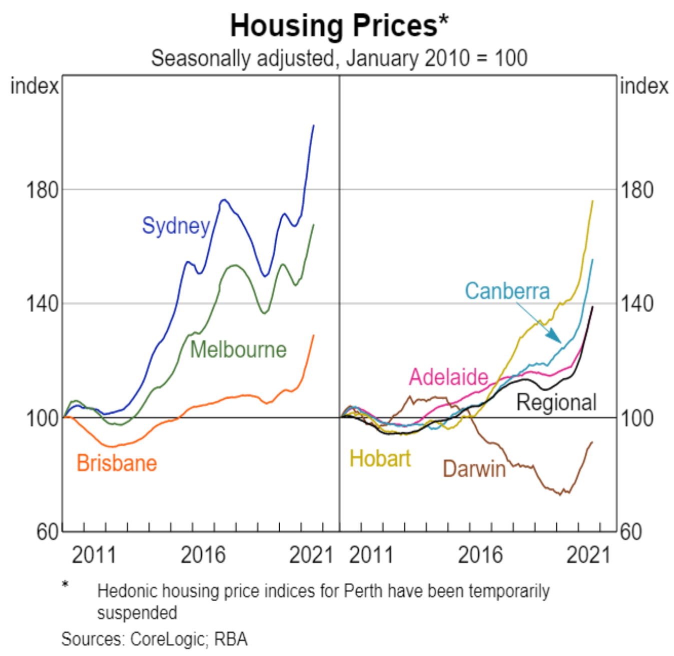
The strongest performers for the portfolio during the month included:

- Liontown Resources +48%, Medical Developments +42%, Elementos +39%, and AusNet Services +30%

The weakest performers for the portfolio during the month included:

- Mineral Resources -18%, Appen -17%, BHP Group -15%, and Universal Biosensors -11%

Chart of the Month – Australian House Prices



Housing is becoming increasingly scrutinised by governments and regulators in Australia and around the world, with prices soaring higher. The chart to the left from the RBA shows how house prices across Australia have jumped substantially over the last 12 months across all states. In April 2021, the RBA noted in its Financial Stability Review that low interest rates and rising asset prices could become a risk to financial stability if lending standards weaken. New Zealand has also faced a similarly strong housing market over the last 12 months and the RBNZ has taken more drastic actions. The RBNZ noted its objective of supporting more sustainable house prices as supporting its decision to raise the cash rate to 0.5%. This comes after the RBNZ was directed by the NZ government to focus on more sustainable house prices and affordability. Conversely, in March 2021, RBA Governor Philip Lowe said it would not make sense for the central bank to target house prices using higher interest rates. Instead, Lowe suggests that lending standards should be the mechanism to address the housing market so that monetary policy can maintain a focus on currency stability, employment, and economic growth. This is something that we have since seen more of with APRA announcing in early October an increase in the loan serviceability requirements for borrowers.

JMFG Australian Equities Strategy		ASX All Ordinaries Index	
Best	**Worst**	**Best**	**Worst**
Liontown Resources (LTR)	Mineral Resources (MIN)	Kingsgate Consolidated (KCN)	Marley Spoon (MMM)
Medical Developments (MVP)	Appen (APX)	Tuas (TUA)	Poseidon Nickel (POS)
Elementos (ELT)	BHP Group (BHP)	Anteotech (ADO)	PPK Group (PPK)

Hits & Misses *– A summation of the top hits and misses for the month of September*

Liontown Resources (LTR) – up 48% for the month. Shares in Liontown continued to rise as lithium pricing continues to gain strength, and the company was added to the S&P ASX 300 Index. The company continued the demerger of its non-lithium assets into ASX-listed Minerals 260, to be completed early October – a move which will focus Liontown and help fund it as a pure-play lithium enterprise.

Kingsgate Consolidated (KCN) – up 104% for the month (Not held). Share price jumped on news announced that long-term mining negotiations with the Royal Thai Government are nearing a favourable close. While noting settlement is not guaranteed, phrasing suggests excellent prospects for Kingsgate to restart its gold operations upon all parties meeting a set of reasonable conditions.

Mineral Resources (MIN) – down 18% for the month. Company sold its stake in successful lithium producer Pilbara Minerals at the start of September, to focus on its iron operations. Iron ore pricing continued to slide and adversely affect MIN's valuation - the cash windfall from the sale occurring around Pilbara's September peak may have served fortuitously to soften the fall.

Marley Spoon (MMM) – down 30% for the month (Not held). Despite anticipated growth announced alongside solid half year results, shares fell in September with Woolworths announcing it had sold down a ~10% holding and Marley Spoon's share price continued to slide to the end of the month. Woollies says it remains committed to the 5-year strategic alliance, however.

Due Diligence – *A closer look at a stock of interest*

AusNet Services (ASX:AST)

AusNet Services is an owner of key electricity and gas infrastructure in Victoria. It exclusively owns and operates the Victorian electricity transmission network, one of five electricity distribution networks, and one of three gas distribution networks. These three networks provide essential energy to 1.5 million Victorians, and operate in a regulated environment, overseen by the Australian Energy Regulator, which sets the price movements for electricity and gas networks every five years. AusNet's infrastructure assets are worth over $11 billion dollars, and it aims to grow this by $2.5 billion over the next five years. The company also owns a commercial business, Mondo, which provides services and technology for essential infrastructure in the energy, water, and transport sectors.

AusNet reported revenues of $1.9 billion in FY21 and spent $765m on growing and maintaining its infrastructure. This infrastructure will play a crucial role in the energy transition to renewables, as AusNet transforms Victoria's electricity system from coal-burning operations to sustainable energy sources. AusNet is currently progressing plans to develop the Western Victoria Transmission Network Project, which will allow an additional 900MW of new wind and solar project to join the Victorian electricity grid.

AusNet has been in the news recently as the latest acquisition target on the ASX. The company was initially bid for by Brookfield Asset Management, at an offer price of $9.6 billion. Brookfield is a Canadian investment company that specialises in real estate and infrastructure assets and has over US$626 billion under management. The $2.50 per share cash offer on the 20th of September represented a 26 per cent premium and included Brookfield gaining an eight-week exclusive due diligence period with AusNet's books – although the arrangement can be terminated with seven days' notice.

The next day, APA Group, the only other major energy infrastructure company listed on the ASX, submitted a rival bid for $2.60 a share ($1.82 cash and the rest in stock), and raised AusNet's valuation to $9.96 billion. However, the larger bid was unable to derail the eight-week due diligence period locked in with Brookfield, as AusNet preferred the certainty of the entirely cash offer. Having been locked out of AusNet's books is a surprise to APA, having been discussing a potential takeover behind the scenes three weeks prior to the Brookfield Offer.

Another factor that might impact which offer is accepted is AusNet's ownership structure. Currently, the top shareholders are Singapore Power with a 32.3% stake, which is indirectly owned by the Singapore Government, and the State Grid Corporation of China with a 19.9% stake. This means that the Foreign Investment Review Board may complicate the APA transaction as it would have to approve foreign governments gaining a substantial shareholding in APA Group.