

Australian Equities Strategy – Investment Newsletter

Performance (As at 31 st March 2021)	Month (%)	Rolling 3 Months (%)	Rolling 1yr (%)	Rolling 3yrs (%)	Inception Gross (%)	Inception Annualised (%pa)
JMFG Australian Equities Strategy	+0.29	-1.99	+37.49	+25.73	+74.23	+8.57
All Ords Accumulation Index	+1.84	+3.61	+41.14	+33.43	+71.77	+8.35
Outperformance	-1.55	-5.60	-3.65	-7.70	+2.46	+0.22

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 – and is after management fees, taxes (excl imp. credit benefits) and any paid or accrued performance fees. Strategy Inception for Performance Data is July 1st, 2014.

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

The rotation to so-called ‘value’ stocks continued in March with low PER and typically higher-yielding sectors performing the best. Consumer Discretionary increased 7.03% through the month, with Utilities rising 6.8%, Property Trusts +6.56%, Telecommunications +6.24%, and Financials +4.31%. Weakest sectors included Materials -3.01%, I.T. -2.95%, Energy +0.02%, and Health Care +2.51%. The ASX Small Ordinaries, with its higher proportion of I.T. and Health Care exposure, was weaker than the broader market through the month, rising 0.79% compared to the ASX 200 which increased 2.44%.

The JMFG Australian Equities Strategy underperformed its benchmark by 1.55% during the month, rising +0.29%, being largely a function of perceived ‘value’ stocks performing better than ‘growth’ stocks. The strategy underperformed its benchmark by 5.6% for the rolling 3 months and underperformed for the rolling 12-month period by 3.65%. The annualised return since inception is 8.57%, compared to its benchmark return of 8.35%.

During the month, we exited our position in Xero and added Alcidion Group. Xero has performed well for the portfolio for quite some time, but we see the company facing headwinds to overseas growth. We have held Alcidion Group in the higher-risk Innovation Strategy for a while, and, recently, the company has gained momentum winning new contracts with hospital networks, particularly in the UK. We added Webjet to the strategy and added to positions in Nuix and CSL following price falls post reporting season. We also exited Sezzle and Livehire during the month, taking gains on these positions.

The strongest performers for the portfolio during the month included:

- Universal Biosensors +26%, Centuria Industrial REIT +14%, PolyNovo +12%, and Telstra +10%

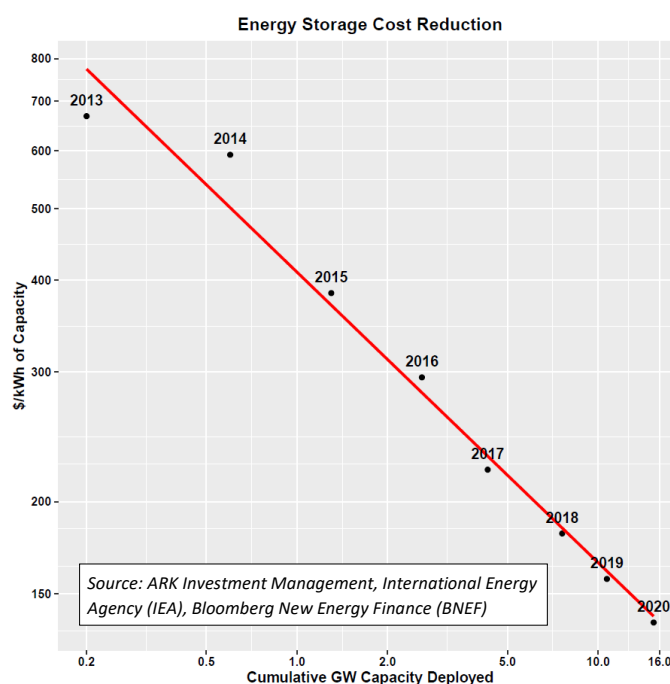
The weakest performers for the portfolio during the month included:

- Nuix -15%, Megaport -11%, Fortescue Metals Group -11%, and Rio Tinto -10%

Chart of the Month – Energy Storage Costs

Over the last 10 years, battery prices have fallen significantly as global investment in energy storage has increased. The chart to the right demonstrates how the total cumulative amount of power storage capacity deployed relates to the cost to produce the capacity. This substantial deployment of battery capacity has created a cycle in the energy storage market whereby the investment in battery technology leads to innovation and a lower cost to produce the batteries, thereby encouraging further investment. Investment in battery capacity only shows signs of further increasing in the future, based on the continuation of unit cost declines.

The bulk of battery investment is in Lithium-Ion Batteries (LIBs) as these tend to have a long comparable lifespan, charge faster, and tend to be more efficient than other battery types. Lithium-Ion Batteries are also the battery of choice for Electric Vehicles due to their high energy density. As such, electric vehicle manufacturers have benefited from the substantial cost reductions in battery production seen in recent years. Grid-level storage is also on the rise – for example, in January 2021, Origin Energy announced that it was progressing with plans to build Australia’s largest battery with a power capacity of 700MW.



Due Diligence – Lithium Companies

Galaxy Resources (GXY), Orocobre (ORE), Piedmont Lithium (PLL), and Pilbara Minerals (PLS)

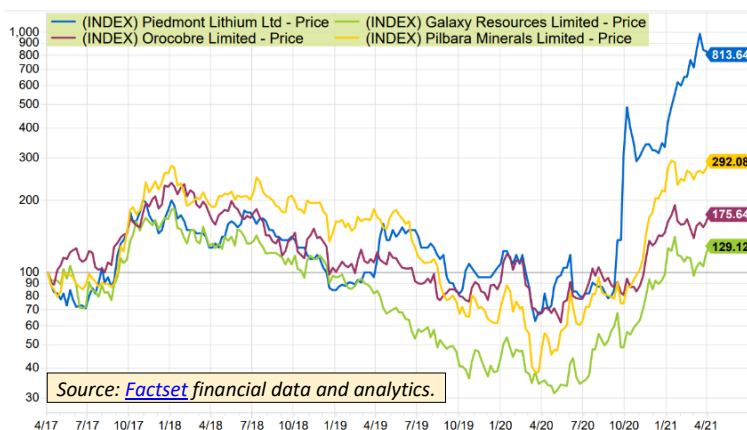
The substantial rise in lithium prices during the early months of 2020 has seen Australia's listed lithium companies reaching their highest valuations since the lithium price peaked in 2018. After bottoming in March 2020, the largest lithium companies have seen share prices soar over the rolling year: Piedmont Lithium +958%, Pilbara Minerals +560%, Galaxy Resources +219%, and Orocobre +128%.

Piedmont Lithium, the smallest of the stocks mentioned here and currently pre-production, returned 958% in the rolling year to 31 March 2021. In September 2020, the company announced that it had entered into a binding sales agreement to supply Tesla from its North Carolina operation, with spodumene concentrate of 160,000 tonnes per annum for five years commencing between July 2022 and July 2023.

Pilbara Minerals, the largest listed lithium producer in Australia, reported a 62% increase in sales of spodumene concentrate in the December quarter from the previous quarter. Galaxy Resources reported that its December quarter shipping of spodumene concentrate exceeded the previous quarter by 349% and stated 1Q21 shipments would most likely be contracted at materially higher prices.

Orocobre, which sells brine-evaporated lithium carbonate, has been steadily reducing its cost of sales and expects sales prices to be 50% higher for the 6 months through to June 2021 compared to the prior period.

This substantial demand increase for lithium demonstrates the increasing demand from battery manufacturers for raw materials; however, it remains to be seen whether lithium prices will retest their 2018 highs.



Electric Vehicles and the Changing Auto Industry

Electric Vehicles (EVs) get their energy from rechargeable batteries rather than by the combustion of fuel, as with internal combustion engine vehicles (ICEVs). While EVs currently represent only a small fraction of the total automobile market, EV sales have accelerated substantially over the last 10 years with improvements in battery technology and the introduction of punitive emissions regulations. Major automakers are investing heavily in R&D to shore up their EV offerings to take advantage of this growing market.



Tesla Model 3 is the best-selling EV to date

Tesla is currently the leader in the EV market, producing solely EVs unlike traditional ICEV automakers that are now attempting to transition into the EV market. In 2020, Tesla delivered 499,550 vehicles, up more than 35% on 2019 deliveries. In 1Q21, typically a weaker quarter following Christmas, Tesla had its strongest quarter on record delivering 184,800 vehicles, more than double the same quarter last year. This puts the automaker well on track to hit its target of 50% annual growth in deliveries and the company expects this delivery growth rate to continue for years to come.

Volkswagen has been one of the more aggressive traditional automakers with its transition into EVs. In November 2020, the German automaker announced that it would invest €73bn over the next 5 years in future technologies, of which ~€35bn would go toward electric vehicles and ~€11bn would go towards hybrids. The company also expects to be selling 3 times as many EVs by 2030, and 35% fewer ICEVs as they are slowly phased out.

Daimler AG, the parent company of Mercedes-Benz, is following a similar strategy to Volkswagen by scaling up production of both plug-in hybrids and pure EVs. The company announced in 2020 that it was planning to have 10 EV models launched by 2025 and 25 hybrid models. Daimler is also targeting 50% of vehicles sold to be hybrids or EVs by 2030.

Ford Motor Company has committed that its Europe sales will be all electric by 2030. Ford has invested US\$7bn since 2016 and is planning to invest a further US\$15bn in expanding its global EV manufacturing by 2025. While Ford is not yet a major player in the EV market, it sold 6,614 of its all-electric Ford Mustang Mach-E in 1Q21.



GMC Hummer EV announced by General Motors

General Motors has announced it will invest US\$27bn by 2025 to develop 30 new electric vehicles. The company is also planning to phase out of ICEVs by 2035.

Toyota Motor Corporation has been less willing to enter the EV space despite being one of the world's largest automakers and the earliest proponent of hybrids. While Toyota sold 9,528,438 vehicles in total in 2020, the company only reported EV sales of 3,346. As the company has a wide range of hybrids, it is one of the lower emission automakers. New emission regulations thereby have less of an impact on Toyota and, as such, the company is able to take more time in entering the EV space.