JM Financial Group

Issue 82: February 2022

Australian Equities Strategy – Investment Newsletter

Performance *(As at 28th February 2022)*	Month (%)	Rolling 3 Months (%)	Rolling 1yr (%)	Rolling 3yrs (%)	Inception Gross (%)	Inception Annualised (%pa)
JMFG Australian Equities Strategy	**+0.2**	**-6.6**	**+2.6**	**+25.8**	**+77.5**	**+7.8**
All Ords Accumulation Index	+1.7	-2.4	+10.0	+30.5	+85.0	+8.4
Outperformance	**-1.5**	**-4.2**	**-7.4**	**-4.7**	**-7.5**	**-0.6**

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 reasons, 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 February*

For the month of February, the JMFG Australian Equities strategy rose 0.2%, with some relative stability returning to markets. The strategy underperformed the All Ordinaries Accumulation Index by 1.5% for the month, after outperforming last quarter. Weakness persisted in some software related holdings. We have exited or reduced some of these positions but retained others where we remain confident in the underlying growth, which should see those stocks return to favour with investors in the coming months. We continue to make refinements to the portfolio to better align the strategy with the current market environment.

The best-performing sectors for the broader Australian market in February were Energy, which continued its rise by a substantial 5.8%, and Consumer Staples, which recovered some of its January decline, up 5.6%. Other rising sectors included Utilities 3.0%, Materials 2.6%, Financials 2.4%, Property 0.9%, and Industrials 0.1%. Sectors which fell through February were Information Technology -6.9%, Consumer Discretionary -5.8%, Communications -2.2% and HealthCare -0.2%.

During February, the portfolio was actively traded, trimming some positions, and adding to others, as a significant amount of new information came to market with the first half reporting season. New positions were entered to increase exposure to Energy, Property, and Agriculture. The free cash level remained relatively stable throughout the month around 6%.

The strongest performers for the portfolio during the month included:

- Northern Star +24%, Credit Clear +22%, Woodside Petroleum +20%, and Lotus Resources +18%

The weakest performers for the portfolio during the month included:

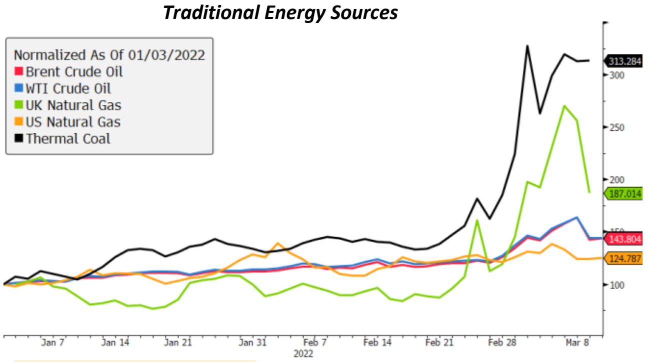
- PolyNovo -24%, Uniti Group -21%, Mineral Resources -18%, and Dubber Corporation -17%

Chart of the Month – *Energy Market*

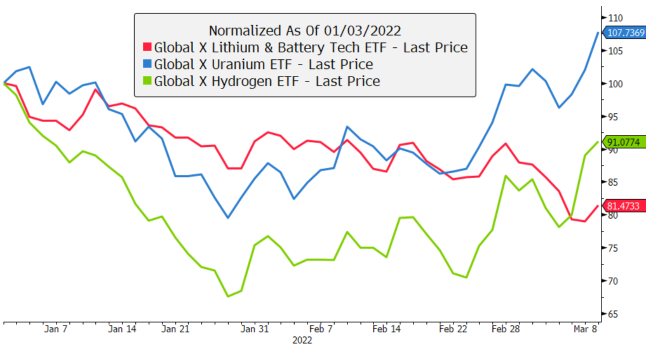
The start of 2022 has seen an interesting reversal in some of the broad energy trends that have led the market in recent years. The charts below show the comparative performance of traditional energy sources and future-facing energy sources over the year to date, demonstrating this clear reversal. Traditional energy commodities, such as crude oil, natural gas, and coal, have all strongly rallied in recent months following the Russian invasion of Ukraine underscoring a multiyear underinvestment in these traditional energy sources as countries have instead been investing in renewables.

Countries globally have announced a move away from cheap Russian energy which will mean more expensive resources will need to be relied upon while the transition to future-facing energy takes place. This comes at a time when global demand is rebounding as international travel returns and economic activity recovers. This strong performance of traditional energy has not been paralleled in the performance of future-facing energy and the equities in these industries have had a bumpy start to 2022. However, while Uranium equities have had a volatile start to the year, their performance is still positive year-to-date. The strong tailwinds of recent years are expected to persist, however, and the need for catch-up investment in traditional energy projects is also likely to be required to fill the gap as the transition takes place over the next decade.

Traditional Energy Sources



Future-Facing Energy Sources



Source: Bloomberg Finance

JMFG Australian Equities Strategy - February		ASX All Ordinaries Index - February	
Best	**Worst**	**Best**	**Worst**
Northern Star (NST)	PolyNovo (PNV)	Helios Energy (HE8)	Laybuy Group Holdings (LBY)
Credit Clear (CCR)	Uniti Group (UWL)	NRW Holdings (NWH)	Praemium (PPS)
Woodside Petroleum (WPL)	Mineral Resources (MIN)	Cimic Group (CIM)	Doctor Care Anywhere (DOC)

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

Northern Star (NST) – up 24% for the month. Rising with the gold price as investors seek defensive assets with international markets becoming volatile, Northern Star reported first half revenue up 63% to $1.8Bn and net profit up 43% to $261M, although underlying NPAT was $108M vs A$193M a year ago on an increase in D&A post-merger. The company also shuttered plans for its Windfall Project JV with Osisko, freeing up capital for other opportunities.

Helios Energy (HE8) – up 49% for the month (Not held). Texas-based oil and gas exploration company reported some encouraging progress with well developments and seismic works. The company also started a new helium business unit based in China under wholly owned subsidiary Helios Energy China, having commenced a boil-off gas helium extraction JV with Chinese domestic LNG company Ordos Xingxing.

PolyNovo (PNV) – down 24% for the month. Strong first half sales results weren't enough to encourage investors who remain wary of a capital raising as management continue to invest in sales staff in USA and Australia to take advantage of the growth opportunity. Management continues to expect a strong second half driving a cash-positive result for the full year, thus not requiring additional capital.

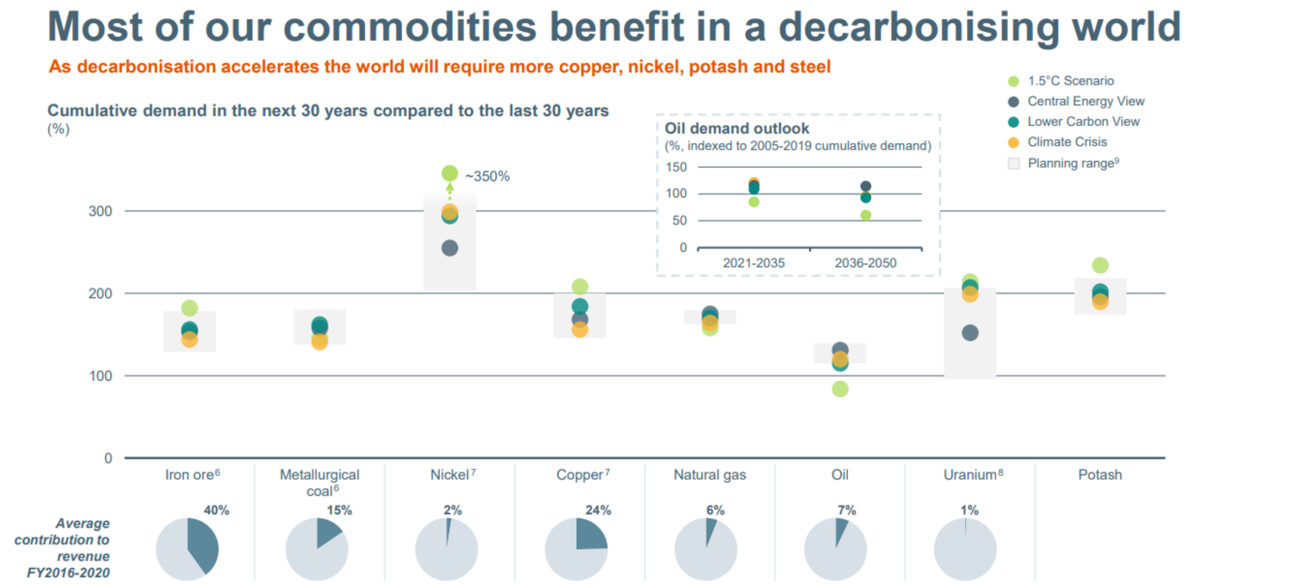
Laybuy Group Holdings (LBY) – down 53% for the month (Not held). NZ-based Laybuy Group reported solid growth and customer momentum but continues its decline along with its BNPL peers as the sector remains out of favour. Recent UK regulator focus on BNPL offerings may directly impact Laybuy Group's bottom line with its significant exposure to merchants in the region.

Due Diligence – *A closer look at a Company of Interest* – BHP Group Limited (ASX: BHP)

BHP Group Ltd (BHP), a global resources company with a market capitalisation of $255bn, is the largest Australian listed company and accounts for 10.2% of the ASX All Ordinaries index following consolidation of its dual-listed structure. Over the past decade, BHP has pursued a strategy of "shrinking to greatness", including divesting South32, selling US onshore gas assets, and, more recently, selling its remaining coal assets to Stanmore Coal and merging BHP Petroleum with Woodside Petroleum (subject to shareholder approval). Mike Henry, BHP's current CEO, commenced in the role at the start of 2020 and has continued to refine and realign BHP's portfolio strategy to future-facing commodities. This realignment is now complete with the exit of out-of-favour fossil fuel assets.

BHP's largest commodity exposure is iron ore followed by copper, with increasing exposure to nickel and potash. It remains unclear yet whether BHP will only focus on growing within these existing commodities or expand into additional future-facing commodities like lithium or hydrogen. M&A in Electric Vehicle related commodities has commenced and BHP is expected to participate more actively going forward. Although commodity prices can be volatile, the current supply/demand dynamics are as favourable as ever, particularly in the future-facing commodities to which BHP has pivoted. As a result, BHP has become a significant cash generator, returning ~A$40bn to investors over the last two years and retaining plenty of dry powder for new investments. After years of shrinking, BHP is now in a position of strength from which it is well placed to enter a period of growth.

Future-facing commodities are expected to perform well going forward, with demand expected to outpace the growth in supply due to decarbonisation which is driving a transition to electric vehicles and the increased electrification of the broader expanding global economy. Transitions often take years, sometimes decades, to play out. As discussed in the last newsletter, there are still gains to be had in the medium term in "old" energy, to which JMFG strategies are also well positioned.



Source: BHP climate change briefing - 10 Sept 2020