EthicalPartners
FUNDS MANAGEMENT

Ethical Partners Australian Share Fund

MAY 2021

Ethical Partners Funds Management is a boutique Australian fund manager which is fully owned by its staff. We have a dual focus on performance and investing ethically over the long term. Our approach directly manages risk for our clients, provides the ability to invest in line with your values and actively advocates for change. Investors in the Fund invest alongside the owners and managers of Ethical Partners.

	INVESTOR CLASS	CLASS A	CLASS B	CLASS C	CLASS E
Unit Price 31/5/21	$1.0071	$1.0047	$1.0094	$0.9992	$1.0107
APIR code	EPF9951AU	EPF9964AU	EPF3813AU	ETL8683AU	-

INCEPTION DATE
8 August 2018

BENCHMARK
S&P/ASX 300 Accum. Index

UNIT PRICING
Daily

DISTRIBUTIONS
Every six months

BUY/SELL SPREAD
0.20%

MANAGEMENT FEE (PDS)
0.95%

PERFORMANCE FEE (PDS)
15% of outperformance

MINIMUM INVESTMENT
$25,000

INVESTMENT DIRECTOR & CEO
Nathan Parkin & Matt Nacard

GOOD INVESTING PODCAST
Link to the latest episode

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Link to PDS

This newsletter is intended for wholesale and institutional investors only

MONTHLY COMMENTARY

During May 2021 the Fund returned 1.56% versus the S&P/ASX 300 Accumulation Index of 2.31%, underperforming the market by -0.75%. An underweight position in Information Technology and an overweight position in Westpac contributed to relative performance while an overweight position in Consumer Staples and an underweight position in Commonwealth Bank detracted from relative performance.

The Australian equity market continues to deliver strong monthly returns as we recover from COVID-19 and governments and central banks provide strong economic support. Consensus earnings revisions continue to be positive (source: UBS) and market expectations for double digit industrials earnings growth over the next two years is reasonable, in our view.

While in some markets (cypto, SPACS, US Tech, meme stocks) there are clearly excesses, driven by liquidity and loose monetary conditions, there is still moderation and appealing valuations in selected areas of equity markets. For instance in the US it has been a small number of large Tech stocks leading the market's gains while returns in general industrials have been more modest.

The NASDAQ has outperformed the Dow Jones Industrials by around 98% over the last five years, with much of the excess gain occurring over the last twelve months. Australian equities (which have also underperformed the NASDAQ by an even greater margin) valuations' appear reasonable in our view which places the Australian market in a relative better position should some of the global excesses unwind.

SIGNIFICANT HOLDINGS

Bega Cheese	Macquarie Group
Graincorp	Meridian Energy
IGO Limited	Mirvac
Insurance Australia Group	Qantas
OZ Minerals	Westpac

Performance as at 31 May, 2021

INVESTOR CLASS	1 MONTH %	3 MONTHS %	6 MONTHS %	12 MONTHS %	SINCE INCEPTION (ANNUALISED %)
Fund (after fees)	1.56	8.48	10.06	22.98	2.31
S&P/ASX 300 Accum	2.31	8.53	11.95	28.72	9.16
Excess	-0.75	-0.05	-1.89	-5.74	-6.85

At market inflection-points like today where normal revenue growth, cost assumptions and demand patterns are distorted, consensus earnings expectations are likely to have a higher rate of error and are subject to a wider array of outcomes than usual, in our view. Investors can thus can take longer to accept the new level of earnings that are achievable in the current environment and this can result in a delay in the stock price of the company fully reflecting the move until the outcome becomes obvious. Today we believe this means a higher frequency and more material opportunity set than normal.

Take **Bluescope Steel** (overweight) for example. Through the latter half of 2020 the company upgraded FY21 earnings guidance four times (from 23 October 2020 to 29 January 2021) by a magnitude of around 104%*. The stock price only increased by 15.5% from $14.36 to $16.59 over this period as the market reasoned that it was likely a one-time earnings boost and did not represent a higher earnings base into future periods. On 27 April 2021 the company upgraded earnings again (outlook for the second half of FY21) and consensus finally capitulated and upgraded earnings for FY21 and even into FY22.The stock also responded having rallied another 33.6% into the last upgrade taking the total move to almost 50%. Thus it took some months for the market to accept that earnings were going to be higher for a longer period of time. The Fund had an overweight position in the stock for the duration of the move and today our team sees similar opportunities across various sectors where the market has not yet fully appreciated the possible move in earnings per share that we believe is likely.

* Bluescope Steel increased expected EBIT to $530M for the Dec 2020 half from expectations of earnings of $260M in the June 2020 half.

Some other examples are below:

Qantas: Our analyst forecasts significant earnings growth from FY22 to FY23 based on conservative assumptions around increases in domestic Revenue per Average Seat Km (still less than pre COVID levels), aided by a moderate pick up in International travel (~20% capacity utilization FY22) as well as significant cost savings.

Graincorp: The company has been fortunate to de-merge with a record crop harvest in its first year as a stand-alone business. Graincorp continues to demonstrate however that the initiatives that were undertaken to take cost out of the business and grow operations have been delivered which has increased through the cycle earnings.

Macquarie Bank: Our analyst views Macquarie as being able to produce a higher than consensus profit result in FY22 given the available capital it has to deploy, a likely pick-up in asset realisations and an ongoing improving asset pricing cycle. Additionally we believe the market is undervaluing Macquarie's Green Investment Group (one of the largest diversified green energy groups in the world) given its results are grouped with Macquarie Capital's results and are not separately reported.

Insurance Australia Group: Our analyst is forecasting double digit earnings growth for FY22 whereas the market expects flat earnings year on year, hence consensus estimates for IAG are very conservative. We expect considerable momentum in top line growth with volumes being supported by mid-single digit premium increases in personal lines and higher in commercial lines.

Westpac: While the company is exposed to the same macroeconomic factors as peers, it also has internal drivers that we expect to drive improved earnings outcomes such as improved mortgage trends and a credible cost strategy to drive improved efficiencies across the business.

We continue to increase positions in high quality industrials, resources and financials that have strong balance sheets, sensible management teams, solid operating cash flow and where our analysis indicates the market is providing a significant and attractive investment opportunity.

ESG AND ENGAGEMENT COMMENTARY

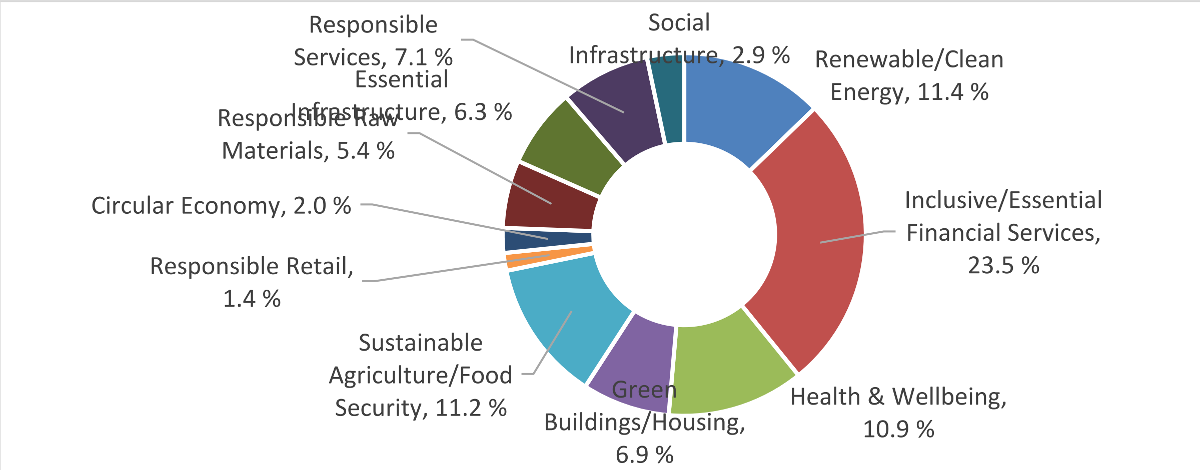
Ethical Partners part of 40 Collaborations

Ethical Partners is proud to be part of over 40 collaborations across the investment industry and with civil society. We believe it is crucial for investors to collaborate, as we see collaboration as both a powerful way to compel companies and policy makers to address issues and a way to advance conversations on these issues. We have recently signed on to several new collaborations and initiatives, including the Investor Alliance for Human Rights and the Investor Statement on Corporate Accountability for Digital Rights. We have also recently signed on as a TCFD Supporter, reflecting our commitment to the TCFD's recommendations, and our continuous engagement with companies on implementing TCFD reporting. Our most recent signatory collaboration is the Global Investor Statement to Governments on the Climate Crisis. We are proud to be one of 457 investors, managing more than US$41 trillion in assets, who have signed the statement. This statement urges a global race-to-the-top on climate policy and calls for all governments to undertake five priority actions before COP26 in November. Please see the full investor statement here.

Reconciliation Action Week

In the recent Reconciliation Action Week, Ethical Partners reiterated its commitment to integrating Indigenous rights within our own approach as well as through the investment process. As part of the proprietary EPORA investment process we consider Indigenous rights as well as a company's commitment to cultural heritage, reconciliation action plans and procurement and corporate actions. We believe that as the first stewards of Australia, Aboriginal and Torres Strait Islander people and culture should hold a special and celebrated place in the institutions and fabric of modern Australian society. In addition, and consistent with the UN Declaration on the Rights of Indigenous Peoples, Aboriginal and Torres Strait Islander people we believe should have a say on the laws, policies and services that impact their lives. We support the Uluru Statement from the Heart as this is a historic mandate for substantive constitutional change and structural reform and we believe an Indigenous Voice, enshrined in the constitution could provide the necessary mechanisms for this change, in a fair and practical way. It is for this reason Ethical Partners also recently made a submission to the Interim Report to the Australian Government: Indigenous Voice Co-design Process 2021. Alarmingly, our recent EPORA analysis this year has found that there are only 14% of ASX 200 companies that specifically address Indigenous rights in their reporting or public corporate policies. More details can be found here.

SECTOR EXPOSURE, MAY 2021



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