Drummond Dynamic Portfolio

Quarterly Investment Review – Q3 2022

We believe we are in an era of increased volatility and uncertainty regarding future asset class returns. The Drummond Dynamic Portfolio (DDP) has been created to provide exposure to a diversified set of global investments, with the aim of protecting capital in bad periods and growing wealth in good periods. This is our core, dynamically managed multi-asset investment portfolio.

Market Overview

Equity and bond markets fell further in the third quarter, as strong jobs data and persistently high inflation drove interest rate expectations higher

Global equity market weakness continued in the third quarter. Most major markets were in the red, with the MSCI ACWI index falling -4.7% in local terms. Emerging markets continued to lead decliners falling -11.4% as strict government lockdowns continue to weaken Chinese growth. The Australian ASX200 index eked out a small gain of 0.4% as commodity sectors rallied. Central banks continued lifting rates, with the RBA and Federal Reserve both raising interest rates by 1.5% during the quarter. Interest rate sensitive sectors suffered while value underperformed growth as a style given the increasing likelihood of a recession.

Selling in the bond market continued in earnest over the quarter. US government bond performance was worse than that of Australian government bonds, however nothing matched the bond market volatility in the UK in response to a fiscally loose budget. Corporate debt was mixed as investment grade spreads were broadly steady and high yield spreads rallied from the June wides.

Commodities were weak over the quarter with oil falling -25.8% and broader commodities (S&P GSCI Commodity Index) falling -10.3% as the demand outlook weakened and USD continued to rally. Gold prices fell -7.4% while the AUD fell -5.6%.

Portfolio Performance & Review

The portfolio performed ahead of the peers over the quarter as volatility across all asset classes continued

Over the quarter, the Dynamic Portfolio returned -0.3%*. This was ahead of the FE AMI Mixed-Asset peer index that returned -0.5% over the period. As is shown in the table below, the portfolio continues to perform strongly when compared to the institutional peer group.

DRUMMOND DYNAMIC PORTFOLIO PERFORMANCE HISTORY

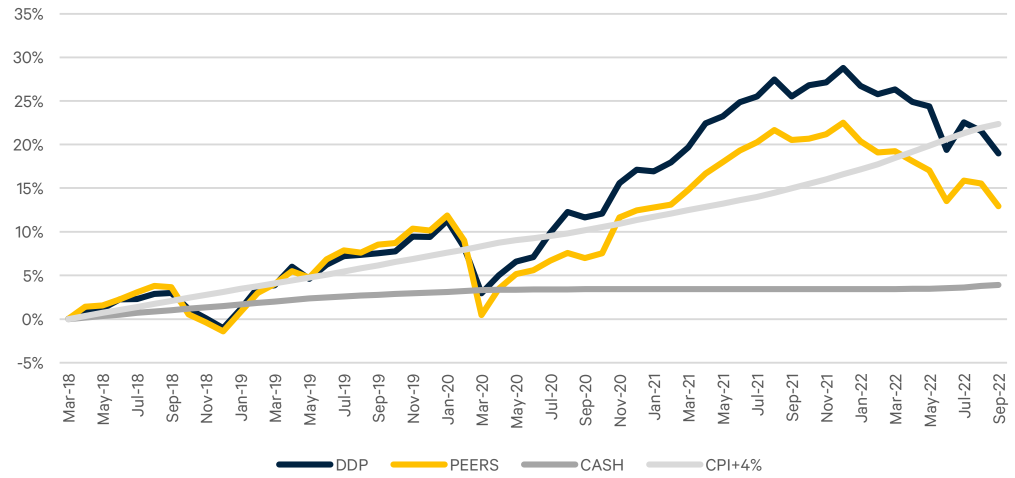
	3 month	6 month	1 year	3 year p.a.	Inception p.a.
Dynamic Portfolio*	-0.3%	-5.8%	-5.2%	3.4%	3.9%
Peers**	-0.5%	-5.3%	-6.3%	1.3%	2.7%
Outperformance	0.2%	-0.5%	1.1%	2.1%	1.2%

Source: Drummond Capital Partners, *BT Panorama, Refinitiv; **FE AMI Mixed Asset – Flexible Sector

The portfolio performed ahead of peers over the third quarter. The preference for larger exposure to global equities over Australian equities was a relative detractor over the quarter, as was the portfolio's government bond exposure. Positive contributors included strong returns from our global alpha managers along with the overall underweight exposure to equities, including no emerging markets, in a quarter where global equity performance was weak. The portfolio's neutral style exposure also helped in a quarter where value styles detracted relative to other styles. The portfolio continues to be well diversified by asset class and manager.

The changes made to the portfolio during the quarter took advantage of the rally in equities through July to reduce growth asset exposure and increase portfolio defensiveness by adding to infrastructure and global alpha. Exposure to bonds was reduced as inflation remains persistent while credit was also reduced in favour of liquid term deposits now providing a reasonable return. These changes improved the portfolios overall quality and defensiveness. Combined, these changes took overall growth asset exposure from 47.4% at the beginning of the quarter to 43.3% at quarter's end.

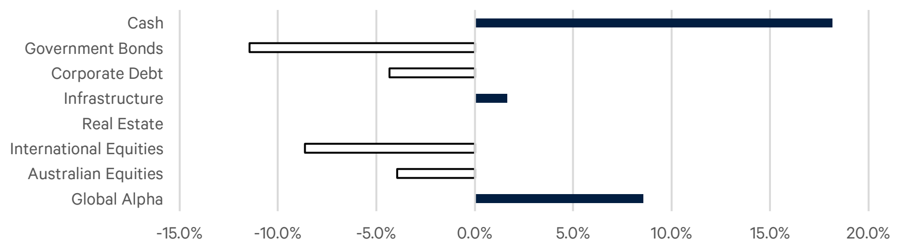
DRUMMOND DYNAMIC PORTFOLIO RETURN vs. PEERS**



Source: Drummond Capital Partners, Refinitiv, BT Panorama; ** FE AMI Mixed Asset – Flexible Sector

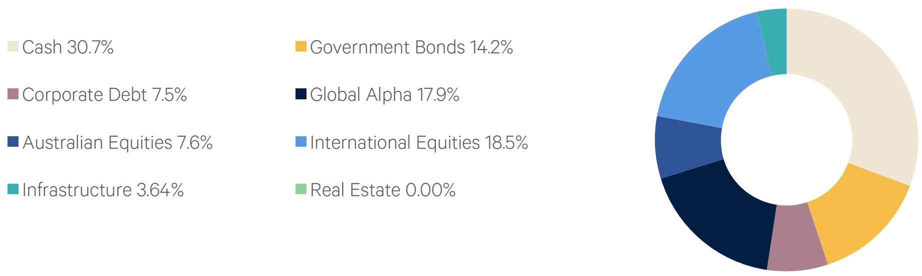
Allocations to growth assets, government bonds and corporate debt were reduced in the quarter in favour of cash and global alpha

PORTFOLIO ASSET ALLOCATION CHANGES – Q3 2022



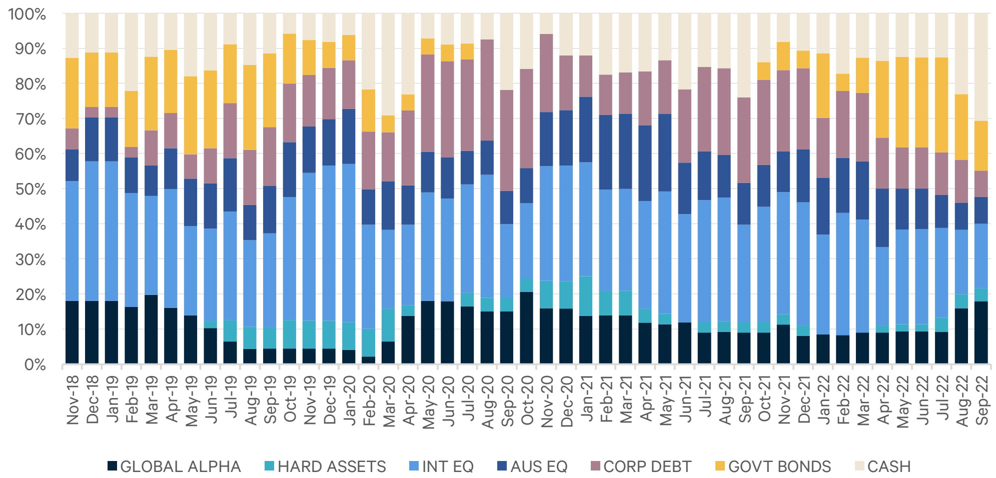
The portfolio is underweight growth assets, and overweight cash

PORTFOLIO ASSET ALLOCATION – Q3 2022



International equities and cash are the biggest asset class exposures

PORTFOLIO ASSET ALLOCATION HISTORY

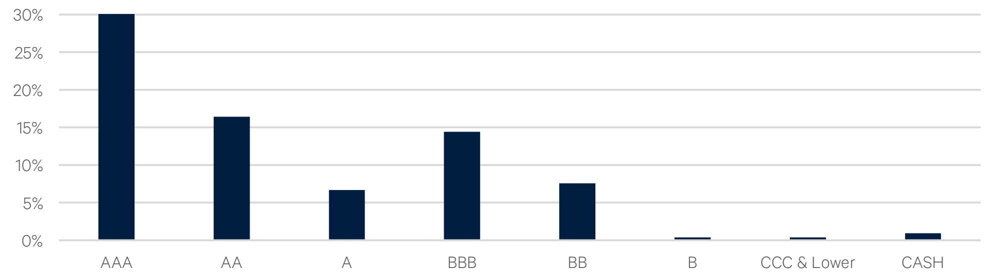


Corporate Debt

We continue to maintain a reduced overall credit exposure given the poor growth outlook

Credit markets were mixed over the third quarter, with high yield credit rallying from June wides before selling off again through September as markets continue to grapple with rising rates to combat inflation and the likelihood of an economic recession. US investment grade credit spreads were flat over the quarter finishing at 1.67% from 1.64%. US high yield spreads narrowed from 5.9% to 5.4%. We continue to maintain a reduced exposure to credit given the poor growth outlook.

PORTFOLIO LOOK THROUGH CREDIT GRADE EXPOSURE (CORPORATE DEBT & GOVERNMENT BONDS)



Source: Drummond Capital Partners, manager reports

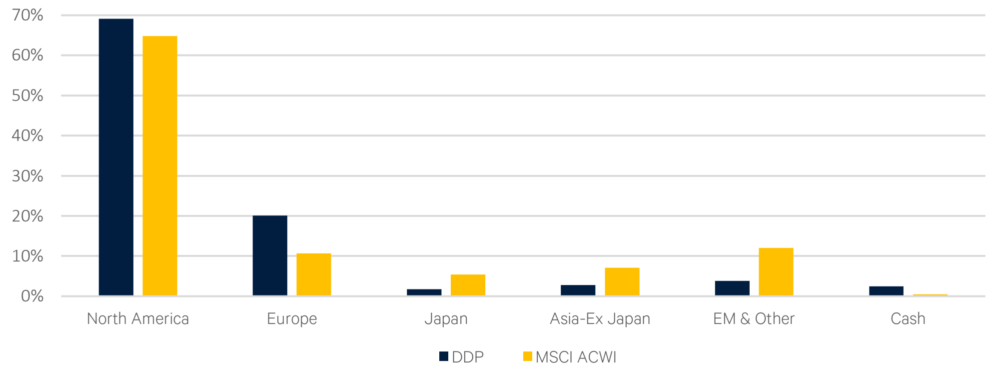
Government Bonds

Government bonds prices continued to fall over the third quarter as inflation persisted

Government bond prices fell further over the third quarter as core inflation remained elevated contrary to expectations of a fall. US 10 year yields climbed 80bps to 3.8%. Having sold off more aggressively already, the sell-off in Australian bonds was less aggressive with 10 year yields moving from 3.5% to 4.0%. We reduced exposure to Australian government bonds during quarter given the ongoing strength in stickier services inflation, though maintain exposure overall given we think there is value in government bonds with inflation likely to peak soon and economic growth slowing.

International Equities

PORTFOLIO LOOK THROUGH COUNTRY EXPOSURE vs. BENCHMARK



Source: Drummond Capital Partners, manager reports

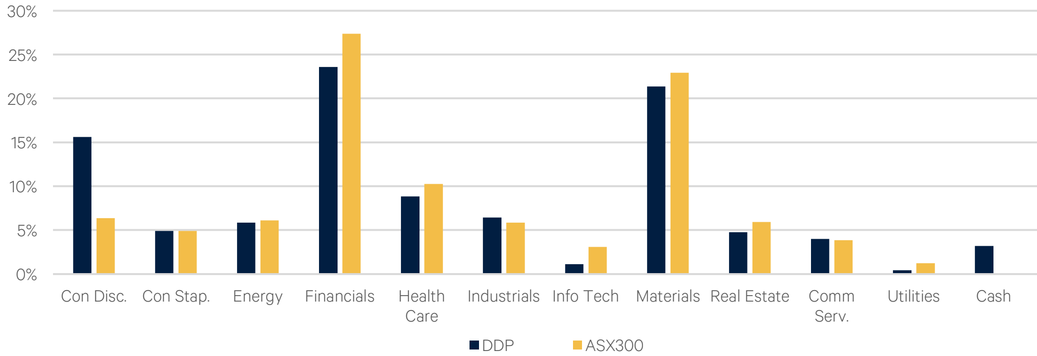
Global equity markets continued to fall in the quarter as the outlook for higher interest rates intensified

World equities (MSCI ACWI) fell -4.7% in local terms over the third quarter, taking 6 month losses to -18%. Markets rallied strongly through July as investors viewed central bank commentary around the path for interest rates as being less aggressive. Continued strong jobs data and core inflation numbers however saw this rally fizzle out and then some. Australian equites managed to outperform over the same period rising 0.4% while emerging markets weakness continued, falling -11.7% for the quarter. The typical link between value orientated sectors and the economy was evident in the third quarter as value styles broadly underperformed growth as prospects for recession intensified. The portfolio's exposure to global equities was reduced over the quarter in favour of global alpha strategies and cash. This reduction was undertaken via value managers.

Australian Equities

Australian shares had another strong relative quarter benefitting from resources and financials strength

AUSTRALIAN EQUITIES SECTOR EXPOSURE vs. BENCHMARK



Source: Drummond Capital Partners, ASX

Australian shares were flat over the quarter, continuing to outperform global equities given the relative defensiveness of the index. Despite weaker commodity prices, energy and resource sectors were the standouts helping to offset weakness in areas more effected by rising interest rates. Consumer related sectors, utilities and property all suffered while financials were mildly positive. Overall exposure to Australian shares was decreased over the quarter in favour of global alpha strategies and cash.

Hard Assets (Infrastructure / Real Estate / Commodities)

We lifted exposure to infrastructure marginally during the quarter

The interest rate sensitivity of real estate and infrastructure led to these sectors underperforming in the quarter. The latter had been able to solidly outperform until September which has been of benefit to the portfolio. Exposure to infrastructure was increased marginally over the quarter.

Global Alpha

One area that has proved beneficial to the portfolio has been the performance of our global alpha managers across growth and defensives sub-sectors as equity and bond market weakness persisted. We increased exposure to this asset class as equity exposure was reduced. We continue to believe that non-directional global alpha funds are well placed to outperform as rising interest rates create opportunities across both growth and defensive asset classes whilst also providing diversification benefits to the portfolio.

Outlook

High inflation continues to dash Investor hopes for a softer stance on interest rates by central banks, increasing the odds of a recession

It's not surprising that global equities were again weak in the third quarter. Equity investors were hoping that inflation had peaked and would be soon delivered the central bank pivot that has brought markets back to life in past downturns. Instead, inflation remained high, and the US Federal Reserve was resolute in their intention to keep raising interest rates.

The current investment environment is relatively unique by modern standards. The market is being led by inflation and central banks are being reactionary rather than pro-active. Since the 1980s policy tightening cycles were aimed at stopping inflation before it occurred. This time around, inflation is here, and central banks need to get it back under control.

While the equity market has continuously hunted for a central bank pivot to a less restrictive policy stance, services inflation continues to drive core CPI above expectations. The US unemployment rate is below 4%, significantly lower than the rate reached when previous pivots have occurred. It still seems that so far this is a Wall Street problem rather than a Main Street one, with the impact of higher interest rates yet to filter meaningfully through the economy. Historically, services inflation has not moderated without a fall in wages growth. Wages growth is unlikely to moderate while the unemployment rate remains low. Thus, we continue to think that central banks will need to cause some degree of economic damage (i.e., a higher unemployment rate) to generate enough deflationary pressure in the services side of the economy to normalise inflation.

It stands to reason that global equity markets have now breached prior lows set in June but in most developed markets there is nothing excessive about this year's drawdown to date. Equity valuations are really only getting back to some level of normalcy post the ultra-loose money expansion through last year. The relative valuation of global equities to bonds has not improved at all as the selloff in bonds has endured a similar timing and magnitude to equities.

Of course, equity market valuations are still based on forward year earnings that are estimated to grow ~6% in 2023. The rapid cooling in the ISM index as a real time barometer for US growth and earnings, higher USD detracting from the offshore earnings of the large multinationals, and higher labour and energy costs imply earnings should fall.

While markets often look through earnings cuts as a relatively lagging effect of economic conditions that have already deteriorated, with little chance of a near-term Fed pivot, and no margin of safety in valuations, we don't see reason to justify moving away from our underweight stance in equities. We remain in a strong position to take advantage of more attractive prices.

Regards,

The Drummond Capital Partners team

*Inception date is 31/3/2018. Source: BT Panorama. The returns shown are net of fund manager fees and do not incorporate any other fees including Advisory Fees, Admin Fees or Portfolio Manager Fees. They are calculated from the model portfolio within BT Panorama and as such may vary over time and vary by individual client.

Disclaimer: The information in this document has been provided by Drummond Capital Partners (ABN: 15 622 660 182) AFSL 534213. All the information in this document is general in nature and should not be considered personal advice. This document is not intended for public or third-party use.

To the maximum extent permitted by law, neither Drummond nor any of their associates, related parties, directors, officers, employees, advisers (including financial, accounting and legal advisers) or representatives make any recommendation in relation to the investments, or make any representation or warranty, express or implied, as to the accuracy, reliability or completeness of the information contained in this document. This document is intended to provide potential Investors with general information only and does not constitute a product disclosure statement or any other disclosure document under the Corporations Act 2001 (Cth) (Act). This document has not been lodged with the Australian Securities and Investments Commission (ASIC) or any other government body or regulator. This information is intended only for persons who qualify as wholesale clients (as defined in section 761G(7) of the Act) or sophisticated investors (as defined in section 761GA of the Act), (collectively, Qualifying Investors).

Past performance is not indicative of future performance. Please seek financial advice.

BT Panorama is an operating system developed by BT. All data where BT Panorama is referenced has been provided on an “as is” basis without any warranties. BT assumes no liability for or in connection with this data. BT makes no express or implied warranties or representations with respect to such data (or the results to be obtained by the use thereof), and expressly disclaims all warranties of originality, accuracy, completeness, merchantability or fitness for a particular purpose with respect to any of such data. Furthermore, in no event shall BT have any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.

DRUMMOND

CAPITAL PARTNERS