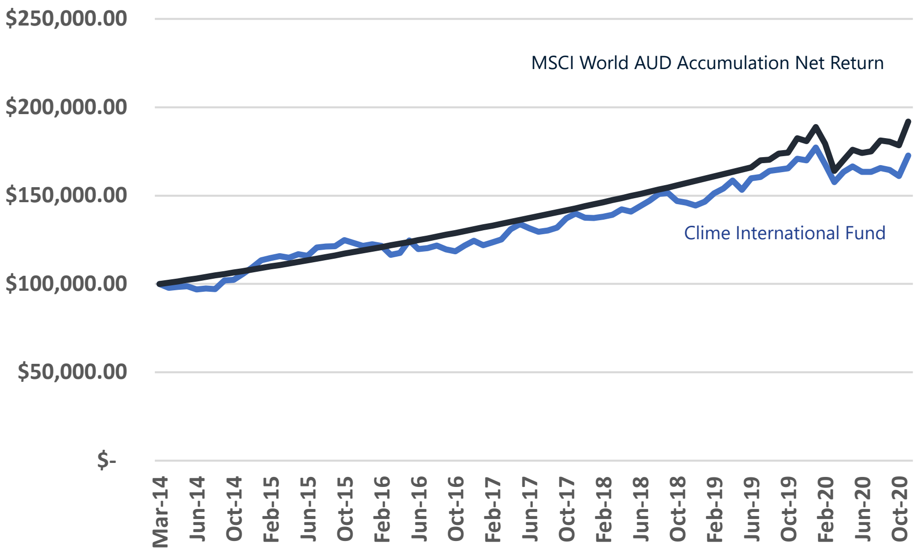
Clime International Fund

Monthly Report November 2020

The Clime International Fund (CIF) aims to provide consistent capital growth and income over the long term (5-7 years) by investing in international securities. The Fund is intended to be a medium to high-risk fund, however the ability of the Fund to hold a significant cash position allows for capital preservation and the delivery of a smoother return profile. The Fund seeks to deliver a return in excess of the MSCI World Index.

1 - Month Net Return (Wholesale)*	1 - Year Net Return (Wholesale)*	Inception p.a. Net Return (Wholesale)*	Total Fund Size
7.2%	1.0%	8.4%	$99.5m



	1 month	3 months	6 months	1 year	3 years*	5 years*	Inception*
Fund Net Return (Wholesale)*	7.2%	4.3%	3.7%	1.0%	7.3%	7.0%	8.4%
Benchmark^	7.5%	5.9%	9.1%	5.1%	10.3%	10.2%	10.1%

Inception: Wholesale Units: 4 March 2014. Retail Units: 11 March 2015.
*Performance figures for more than 1 year are annualised, calculated after all applicable fees and taxes. Performance figures compare unit price to unit price for the given period.
^10%p.a. from 4 March 2014 and then MSCI World Net Total Return Index in AUD from 1 July 2019.

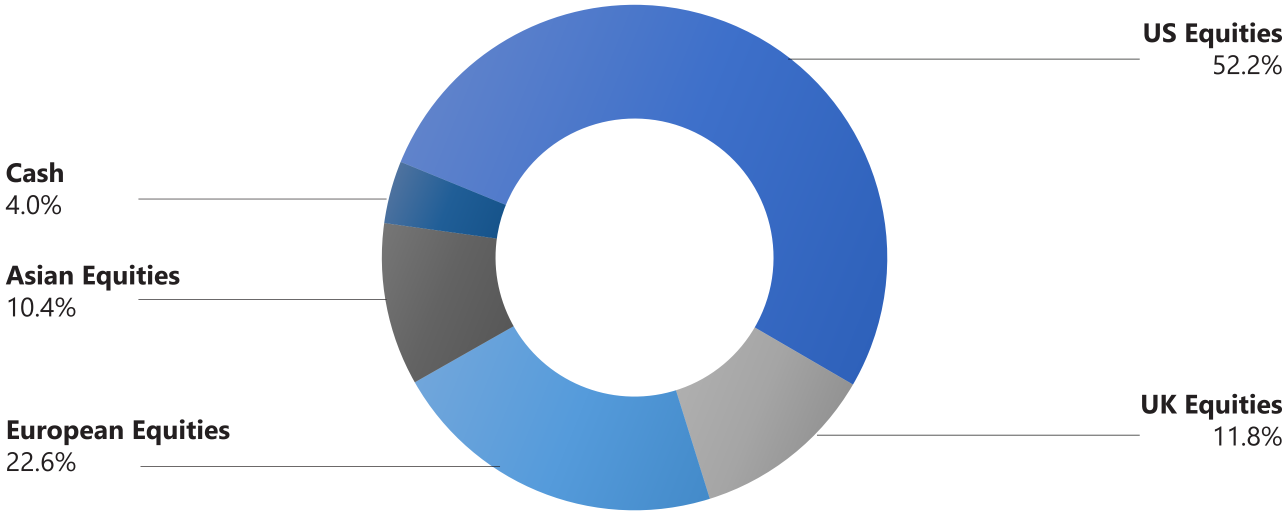
Fund Facts

Portfolio Managers	Pieter Fourie
Fund Inception	March 2014
Fund Size	$99.5m
Cash Distributions	Annually
Eligibility	Wholesale & Retail

Top 5 Holdings

Company	Weight %
Booking Holdings	4.3%
Alphabet	4.2%
Becton Dickinson	4.1%
Novartis	4.0%
Abbvie	4.0%

Asset Allocation



Portfolio Commentary

News of a working vaccine that came to light during November was a big positive for the equity markets. But as global lockdowns persist, it's clear we're not out of the woods yet, and markets pulled back again to reflect that. What we did see though, was a change in sentiment towards so-called value stocks, which has interesting implications for investors. Energy stocks, which do not feature in the portfolio, in particular were one part of the market that staged a spectacular rally, increasing 29% in USD during November, albeit this part of the market is still posting negative returns of more than 30% year to date.

Over recent months the gulf between the performance of growth stocks (companies with good cash flow and earnings that were largely insulated from the effects of Covid-19) and value stocks (companies with cyclical businesses, more dependent on a strong economy, which remain cheap relative to the rest of the market), has widened. Growth stocks have more than recovered their losses from the crash in March, while value stocks still languish below pre-Covid levels. But news of a vaccine seemed to stem this trend. In November we saw value stocks rise 4.2% percent more than growth stocks, and as the clouds start to dissipate over the future economic landscape this may continue. At the same time, growth stocks may fall out of favour as investors realise the profits they have made and reinvest elsewhere. What we could see is a convergence of the fortunes of these two investment approaches. There is still a huge amount of uncertainty, but carefully seeking the right opportunities in value stocks now whilst still adhering to our quality criteria principles could improve future returns.

A good example of this could be our investment in SAP, the leading provider of Enterprise Resource Planning (ERP), analytics, supply chain management and human capital management solutions. The company serves 440,000 customers in more than 180 countries. According to the company, 77% of the world's transaction revenue touches an SAP system. SAP customers include 92% of the Forbes Global 2K companies and 98% of the 100 most valued brands. The company employs 101,450 people worldwide with more the 73% of employees are shareholders in SAP. We believe the transition to cloud ERP is a once in a decade opportunity for SAP to drive customer retention, add new customers and capture share. The stock has had a volatile ride this year with a low of Euro87 and a high of Euro140. After another prolific drop of 36% from the July highs we felt that the stock now offers upside below Euro100 per share, and were able to reinitiate a position during the month.

A working vaccine should also lead to the resumption of normality in the travel sector and many other sectors in the not too distant future. We believe that our large exposure to the healthcare sector is based on good growth prospects and attractive valuations. The outcome of the US election appears sealed, with a Biden victory but Republicans likely maintaining control of the Senate and gaining ground in the House. With regards to the impact on the healthcare sector it looks like a scenario where large-scale dramatic regulatory changes are fairly unlikely, and this has helped enabled the strong market performance seen after the election results became clear. The result of a clear election outcome is that there is unlikely to be dramatic, landscape-altering change and that brighter days are ahead for the healthcare sector, which trades at a historically low relative valuation. The US healthcare sector posted the most broad-based outperformance of all sectors in the third quarter results announcements and has had the strongest earnings revisions of all sectors for both 2020 and 2021 since the start of the year. Further, the sector is actually expected to see the fastest EPS growth from 2019-2022 of close to 11% per annum yet trades at the second-lowest 2022 valuations multiple of all the sectors in the US.

During the month we used the strength in Heineken during the month to exit this position after a 33% rally in the shares from where we first invested in March this year.

We also sold our position in Diageo when the stock rallied by 20% in November.

We initiated a position in Electronic Arts (EA). EA develops, publishes and distributes electronic games on consoles, PC's and mobile devices. We also initiated a position in SAP after we sold out of the position in May. The stock has had a volatile ride this year with a low of Euro87 and a high of Euro140.

Pieter Fourie
Portfolio Manager

Market Commentary

As we head towards the end of 2020, some of the major issues which have bedevilled markets and investors this year seem to be on a path toward resolution. The good news is that promising vaccines and better treatments for coronavirus are appearing, economic recovery from recession is on the cards, and the US political process is grinding towards a new Administration in Washington DC. However, there remain areas of concern, with mountains of government debt, enduring fiscal deficits, rolling QE programs and zero bound interest rates being features of the economic landscape.

Positive news on coronavirus vaccines was followed by a rotation of stocks by market traders, who increased allocations to "value stocks" (those measured by actual profitability) that had been left behind during the pandemic. Market favourites in technology were switched into financials, real estate and energy.

Markets perceive that, whether it takes 6, 12 or 18 months, eventually the worst of the pandemic will be behind us. Therefore, the likelihood of economic recovery is not now in doubt and economists are upgrading their forecasts. US and other global markets were buoyed by vaccine developments and major US indices hit new highs. In Australia, the ASX 200 is lifting alongside and closing on the level it began 2020. However, our market (on a price basis, i.e., not including dividends) is still 5% below its pre-GFC peak (in 2007).

Markets are buoyed by two factors at present. First, is PER expansion caused by zero bound bond yields. Second are the earnings upgrades that flow from economic growth upgrades. EPS forecasts are rising across the world as analysts foresee certain recovery.

Away from asset markets, we are observing renewed growth in real economic activity. In the US, total retail sales during October bounced strongly, albeit with significant changes in composition. Compared with Oct 2019, total retail sales in the US were up 5.7%. In Australia, both business confidence and consumer confidence are recovering in a vigorous fashion.

Playing such an important role in consumer spending, housing remains of great interest. In the US, housing has been unexpectedly resilient through the Covid-19 downturn. Building stocks have benefited from PER expansion, building activity is recovering and US house prices have bounced. Indeed, house prices have outperformed the share prices of building stocks.

Australian residential property has also performed better than initially feared – except for small high-rise apartments. Following various stages of lockdown, most urban residents are prepared to pay a premium for larger space and better locations and have increased spending on home luxuries (electronic appliances, entertainment and more expensive kitchens and food ingredients). This divergence is showing up in capital cities across Australia and is particularly true in Sydney and Melbourne.

Some economists are predicting house price gains in Australia of 5-15% in the next couple of years, fuelled by low interest rates. Strength in housing is good news for the economy's recovery, and for the sharemarket. Australia's banks are among the world's most exposed to mortgages, with housing loans at the four major banks equating to about 75% of our A$2 trillion GDP.

It is not all good news, and the pandemic will leave lasting scars. Across the developed world (ex-Australia), high rates of unemployment are likely to endure. For instance, one in ten jobs worldwide is linked to travel and tourism and those industries are supported by a myriad of small businesses such as hotels, bus companies, tour guides, restaurants and souvenir shops. The knock-on effects are significant from the closure of international travel.

Many hundreds of thousands of small and medium-sized businesses have been decimated, and large corporates hurt, as demand for their output collapsed, their supply chains were disrupted, or they were locked down. The second waves and potential third waves now crashing on many economies in Europe and the US will make this worse. Financial fragility is increasing in already highly indebted sectors of high-income economies, as well as in emerging and developing countries.

However, it could have been much worse. The world economy has benefited from extraordinary support from central banks and governments. Sovereign debt has reached historic levels as countries across the globe do their best to support and sustain economic activity; estimates suggest fiscal and monetary responses exceed $12 trillion dollars in total – far more than what was expended in the GFC.

Massive spending is going to raise public deficits and debt substantially. The global government fiscal deficit is forecast to hit 12.7% of world GDP this year; in high-income economies, it will reach 14.4%. The global ratio of general government debt to GDP is forecast to jump from 83% to 100% of GDP between 2019 and 2022, with high-income countries going from 105% to 126%.

Fortunately, real interest rates on long-term borrowing are either close to zero, or even below zero. Central banks are also committed to maintaining very easy monetary policies. Spare capacity is forecast to persist for an extended period, ensuring that inflation remains relatively benign. Of course, this represents the "consensus expectation", and one thing we have learnt from the Covid pandemic is to acknowledge that the unexpected sometimes happens.

Australia is better positioned than most other countries – not only in controlling Covid, but in driving growth in recovery. We suggest that investors will benefit from staying invested in both Australian equities and quality property assets. Australian share prices have generally underperformed global share prices over the last 10 years (since October 2009, in local currency terms). There is now good reason to believe that this relative underperformance will reverse in the year ahead if the Australian economy recovers faster, cyclical sectors (like resources and financials) come back into favour over growth stocks (like IT and healthcare) and as commodity prices rise.

Adrian Ezquerro
Head of Investments