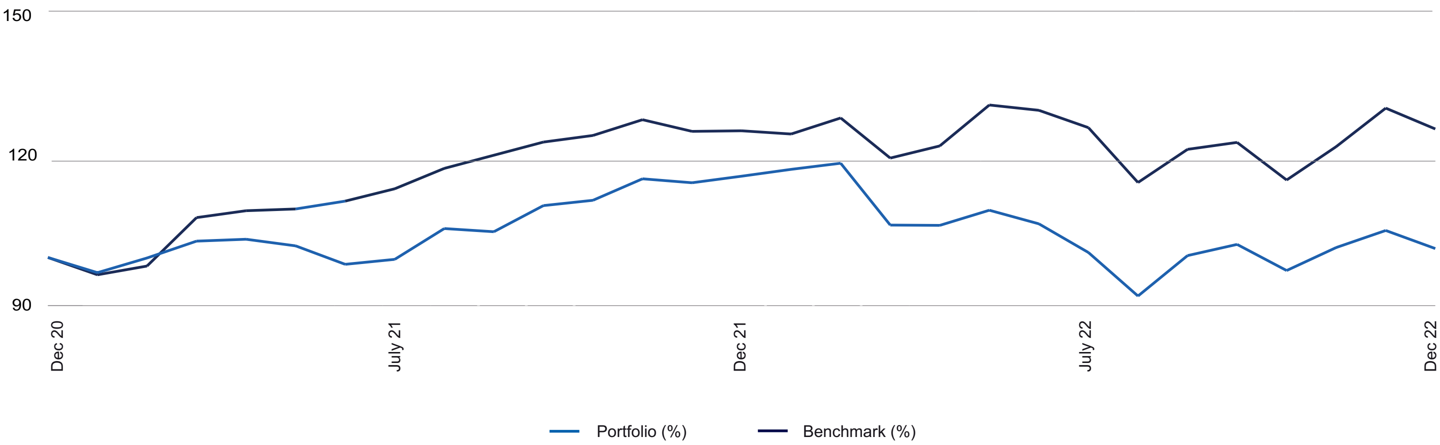
Sterling abrdn Ex20 Australian Equities Portfolio

Monthly Factsheet - December 2022

Investment Objective

To outperform the benchmark, the S&P/ASX 300 Accumulation Index excluding S&P/ASX 20 Leaders Index, after fees, over rolling five year periods.

Performance – 31 December 2022



Cumulative and annualised performance

	1 month	3 months	6 months	YTD	1 year	3 years (p.a.)
Portfolio (%)	-3.55	4.69	10.70	-14.81	-14.81	-
Benchmark (%)	-3.29	9.13	9.62	-1.77	-1.77	-
Portfolio vs Benchmark (%)	-0.26	-4.06	0.99	-13.28	-13.28	-

For the purposes of reporting, the Benchmark is the SS&P/ASX300 Accumulation Index . Per the advisory agreement, the model portfolio aims to outperform the S&P/ ASX 300 Accumulation Index, excluding S&P/ASX 20 Leaders Index, after fees, over rolling 5-year periods. Portfolio performance is provided Net of fees on underlying investments but gross of Advisory/Platform fees.

Inception Date : 01 September 2020

Past performance is not a reliable indicator of future results.

Performance review

For the quarter to end-December, the portfolio rose 4.69% but underperformed the benchmark's 9.13% return. Overall, our stock selection in the financials and materials sectors was the main cause of the underperformance. On the other hand, our stock selection within the real estate sector was additive to returns.
Key detractors from performance were:

- Our lack of exposure to benchmark heavyweight BHP (part of the ASX20, hence we are not able to hold this name). Its outperformance was driven by the China reopening theme, with Chinese policymakers seeking to relax Covid-19 restrictions and support the property sector, which flowed through to higher iron ore prices.
- Our overweight to **Medibank**, with the company battling a very public and ongoing data breach that resulted in the theft of customer information by cybercriminals. While investigations will take time to finalise, it remains difficult to ascertain the longer-term impact on the brand and customer churn; there will also be remediation, legal and other costs. Investors tend to assume the worse, and the share price has been accordingly affected.
- **Pilbara Minerals**, which underperformed after recent market commentary and spot pricing suggesting that the lithium price may have passed its peak, which negatively affected the company's share price.

Conversely, contributing positively to returns were:

- **Northern Star**, which was a beneficiary of the rising gold price over the quarter. In addition, the stock has traded at a discount to its net asset value for much of 2022, though we have seen this begin to close as investors increasingly recognise the strong organic growth optionality on offer.
- Our overweight to **Gold Road**, as the company has continued to execute well and also benefited from a strong increase in the gold price during the month as the US dollar fell after a year of strong gains.
- **HUB24** – the company posted strong growth in new fund inflows for the September quarter, which provided comfort that the weaker momentum observed over the prior quarter was a one-off and largely related to market volatility. Investors also welcomed the news of a better-than-expected outcome for HUB24's renegotiation of its pool cash deposit interest rates.

Portfolio Activity

During the quarter, we exited Evolution Mining, given its near term operating performance has been disappointing and any subsequent turnaround is likely to be protracted. We reallocated the capital into another gold miner, **Gold Road Resources**. In our view, the company has demonstrated much better operating performance which should result in an improvement in ore grade in the near term. As both a miner and explorer, we see upside in its exploration part of the business which is not being priced into the equity value of the business.

Market review

Australian equities rose across the fourth quarter. The Australian dollar reversed its decline against the US dollar, strengthening well after falling to two-year lows early in the period. Meanwhile, commodity prices rose slightly over the quarter, appearing to find a more stable price range after retreating from their peak earlier in the year.
Australian equities continued their strong momentum in the last quarter of the calendar year, outperforming most global equities with positive returns over the calendar year. Investor confidence was generally solid over the quarter. However, it was dented slightly by recessionary fears towards the end of the quarter after the US Federal Reserve (Fed) indicated further interest rate hikes would be likely in 2023, surprising investors after a lower-than-expected US inflation figure for November. The purchasing managers' index reading for Australia continued to fall more than expected, with the latest measure from November firmly in contractionary territory. Performance was mainly driven by the utilities, materials, real estate and financials sectors, although all sectors rose over the quarter.

In economic news, the Reserve Bank of Australia (RBA) raised interest rates again, to 3.10% by the end of the quarter, with further rate rises expected in 2023. Employment data supports this view, with a higher-than-expected 64,000 jobs created in December, along with an improved participation rate of 66.8%. However, GDP data was weaker than expected for the quarter to end-September 2022, with annual growth of 5.9% versus expectations of 6.2%. Elsewhere, Westpac's Consumer Sentiment Index remains close to levels normally associated with a recession, while NAB's Quarterly Business Survey showed that conditions remain resilient, but sentiment has begun to fall.

Top ten holdings (%)

OZ Minerals Ltd	5.3
Insurance Australia Group Ltd	4.5
Northern Star Resource Ltd	4.1
Cochlear Ltd	4.0
Auckland International Airport Ltd	3.8
Medibank Pvt Ltd	3.6
Spark New Zealand Ltd	3.4
AUB Group Ltd	3.4
Bapcor Ltd	3.2
ASX Ltd	3.1

Sector (%)

Financials	18.7
Materials	17.8
Industrials	10.8
Health Care	10.2
Real Estate	8.9
Consumer Discretionary	7.2
Consumer Staples	6.6
Energy	5.1
Other	12.9
Cash	1.9

Source : abrdn 31/12/2022.
Figures may not always sum to 100 due to rounding.

Outlook

As we head into the new year, noting that economic conditions are typically slow changing, our macroeconomic position, in summary, remains one of caution.

Over in the US, while the rate hiking period is close to its peak, we remain wary of the Fed's conviction in bringing inflation well under control, meaning elevated rates and restrictive monetary conditions could well persist for an extended period of time. This is unlikely to bode well for equity markets, particularly when we compare this to the bond markets, where investors continue to anticipate rate cuts towards the second half of this year. From an economic perspective, we still believe a material economic slowdown will occur, as the typical US consumer has been significantly weakened over the course of 2022 thanks to inflation. This will likely flow quickly through to corporate earnings and a further pullback in capital investments.

As for Australia, while the RBA is also looking to re-establish its credibility, we take comfort that our local policy transfer mechanism is faster and that our policymakers appear to be more cognisant of an overreliance on what are effectively lagged economic indicators. With China also looking to exit its 'zero-Covid' policy, we are generally more optimistic on the domestic market and those companies whose operations are confined locally, with the view that Australia has a higher probability of achieving a soft landing.

With the last reporting season continuing to demonstrate strength in corporate earnings, with balance sheets solid, we think the upcoming reporting season will be very telling.

Corporate earnings have the potential to unravel much quicker than investors expect, while balance-sheet strength will be more heavily tested given rapidly rising debt costs. While we have seen downward revisions in investor expectations for the forward period, we continue to believe that only earnings multiples have normalised (mainly driven by the rising cost of capital). In contrast, earnings estimates have yet to fully capture the impact of subdued economic growth.

Given this volatile backdrop, our portfolio positioning remains biased to businesses that offer strong pricing power and those that exhibit defensive business moats. We continue to be cautious on rate-sensitive sectors and businesses that are just beginning their journey toward profitability.

We remain committed to our 'bottom-up' investment style, with a focus on quality companies. We favour businesses with clear growth prospects that are leveraged to long-term structural shifts. Our holdings' defensiveness (i.e., their robust balance sheets and prospects for generating healthy through-the-cycle earnings and dividend growth) is an added advantage. Many of our companies are also leaders in governance and sustainability, positioning them well to adapt to future challenges and opportunities. This will ensure that the portfolio remains resilient despite the current uncertain environment.

Fund performance is available on the relevant factsheet.
The opinions expressed are those of abrdn as of the date of publication and are subject to change at any time due to changes in market or economic conditions.