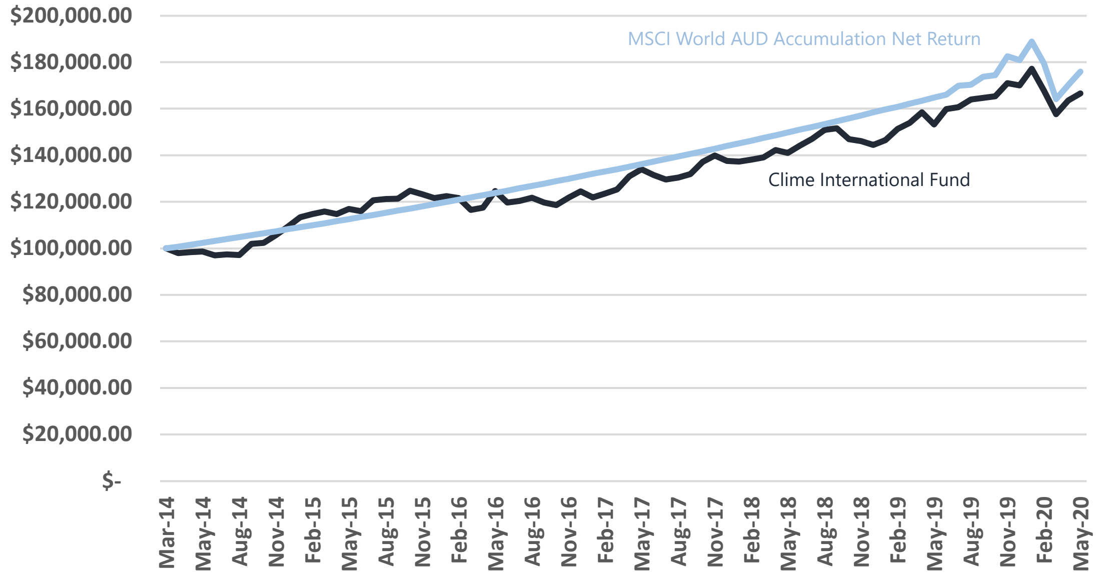
Clime International Fund

Monthly Report May 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
1.8%	9.0%	8.5%	$101.0m



	1 month	3 months	6 months	1 year	3 years*	5 years*	Inception*
Fund Net Return (Wholesale)*	1.8%	-0.8%	-2.6%	9.0%	7.6%	7.4%	8.5%
Benchmark^	3.4%	-2.0%	-3.7%	6.8%	8.9%	9.3%	9.5%
Excess Return	-1.6%	1.2%	1.1%	2.2%	-1.3%	-1.9%	-1.0%

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.

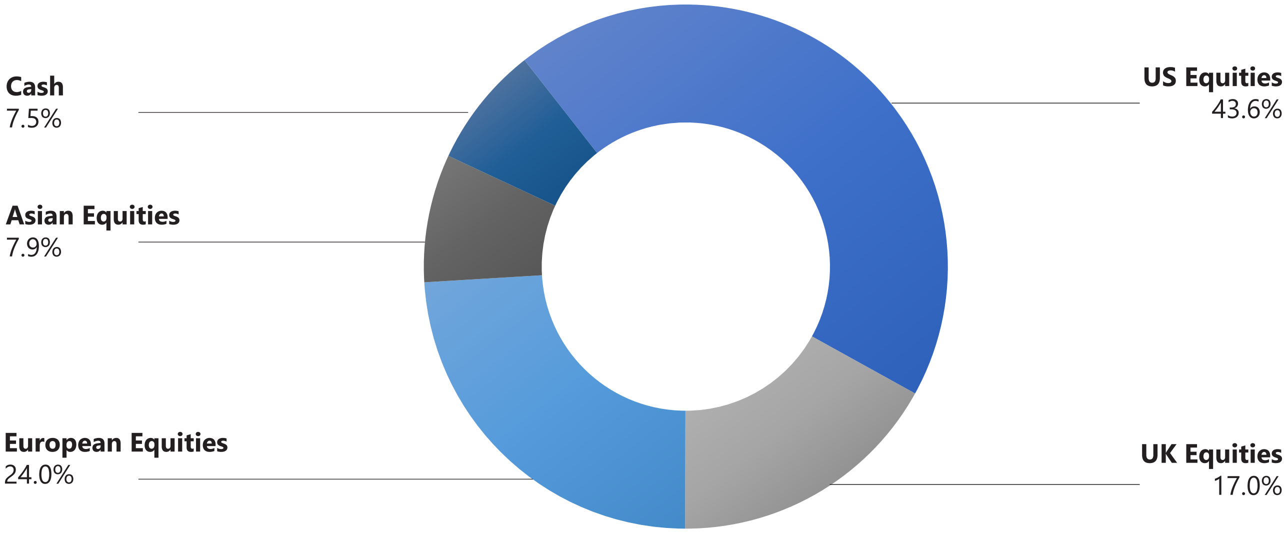
Fund Facts

Portfolio Managers	Pieter Fourie
Fund Inception	March 2014
Fund Size	$101.0m
Cash Distributions	Annually
Eligibility	Wholesale & Retail

Top 5 Holdings

Company	Sector	Weight %
Alphabet	Communications	4.9%
Booking Holdings	Tourism	4.6%
Facebook	Technology	4.4%
Tencent	Consumer Goods	4.2%
Medtronic	Healthcare	4.1%

Asset Allocation



Portfolio Commentary

If there is one thing equity markets are good at, it's being able to see beyond the here and now. Which explains why markets crashed well before cases of Covid-19 had peaked in Europe and the US. Investors extrapolated what could happen, but were unable to assess the impact, hence the panic and subsequent sell-off. Now markets are calmer as they look beyond the immediate impact of Covid-19 and can model the likely range of outcomes.

Although the extreme panic of March has moderated, markets are still volatile due to uncertainty around when economies can return to normal. We're now getting a good level of understanding of how different businesses will be affected by recent events, which makes it easier to identify the potential winners and losers.

Equity valuations have increased, which means buying opportunities are not as prolific as they were.

Clearly, the global economy is not out of the woods yet, and while we don't expect markets to revisit the lows of March, there is a lot for investors to come to terms with. There may well be aftershocks yet to come, but we see these as buying opportunities, and our focus going forward will be on careful stock picking. We favour growth stocks, such as technology companies and other businesses that can take advantage of the new landscape. We also favour defensive stocks, which are stable businesses with strong balance sheets and critical products that the market needs. Finally, we look for opportunities in slightly riskier stocks that remain 'cheap' (such as certain travel companies) but are likely to be the ultimate winners in their sector.

During April we sold our position in Accenture. Our holding period was shorter than normal as the stock bounced close to 25% from where we bought the company as a new position in March. In the process the free cash flow yield for Accenture collapsed from 6% to 4% and we followed our valuation discipline.

We have reduced our positions in Google, Facebook and Microsoft. These three businesses have been excellent performers for the fund over time but as these companies approach levels closer to our assessment of fair value we believe it is prudent to reduce the positions sizes after significant bounces from the March lows.

We initiated a position in Novartis. One of the world's largest pharmaceuticals, Novartis develops, manufactures, and markets branded and generic prescription drugs, biosimilars, and ophthalmic products.

Pieter Fourie
Portfolio Manager

Market Commentary

Global markets continued with their extraordinary bounce from the low point on 23 March through the month of May. Although volatile, the Australian equity market benchmark S&P/ASX 200 Accumulation Index rallied to finish up 4.4% in May, adding to the 8% surge in April. This is still around 20% below the high reached in February, before the global pandemic and subsequent lockdowns took hold. The market is now focused on the recovery as more sectors open up and return to a semblance of normality. We expect that the domestic economy will probably recover at a somewhat tepid pace as business and consumer confidence take time to rebuild.

What explains this extraordinary bounce in markets since late March?

The global mood in investment markets is set on Wall Street. US stocks have been on a tear since the March low even as the COVID-19 pandemic cost 100,000 American lives, tens of millions of American jobs, shut down huge swaths of the global economy and depressed international trade.

There are various explanations for the rebound. Firstly, the pandemic – while ghastly and enormously destructive – seems to have been largely contained in the developed countries, and the duration of the lockdown appears to have been shorter than feared. Secondly, the huge amount of stimulus coming out of the US Federal Reserve and other central banks have worked in avoiding a financial collapse and supported markets with ultra-low rates that will stay “lower for longer”. Third, record low bond yields have meant that investors had few other attractive choices but to invest back into stocks. A final explanation: large IT companies, like Google, Microsoft, Facebook, Amazon and Netflix, which make up a quarter of the S&P 500 index, have benefited from a surge in demand during the pandemic and could emerge from this period even stronger. Investors are looking “across the valley” and seeing beyond the anticipated short and sharp recession.

These factors, perhaps in combination, help explain why the S&P 500 has gained over 35% since 23 March, and the ASX 200 a healthy 33%. But emerging risks will test the resolve of investors: valuations are now exceedingly rich. The S&P 500 companies are priced at around 21 times next year’s earnings, and the ASX 200 close to 19 times. Both ratios are well above long term averages and close to or at 20-year peaks.

Geopolitical tensions are on the rise, which is certainly not helping the global economy. Chinese government officials told major state-run agricultural companies to pause purchases of some American farm goods as Beijing evaluates the ongoing escalation of tensions with the US over a range of issues, including Hong Kong. Chinese buyers have cancelled pork orders in the US, and barley orders in Australia.

With the US and its allies distracted by the pandemic, China’s leadership has taken some bold steps on issues where they have often faced international pushback, including Taiwan, the South China Sea and a disputed border with India. With the US presidential election approaching in November, we can imagine these tensions getting worse in coming months.

There has been some rare good economic news over the last month. New data indicate that China’s factories are continuing a tentative recovery from the pandemic. Manufacturing activity in the country unexpectedly rose last month, with the manufacturing Purchasing Managers Index increasing to 50.7 in May, better than expected. Manufacturing production recovered faster than expected, but exports from China remain sluggish as the rest of the world continues to grapple with the virus. Expectations are that across the rest of Asia, output is likely to remain well below normal levels for many months as domestic and global demand remain depressed.

While the economic data is yet to be presented, it is certain now that the global economy (including Australia’s) is already in recession. As such, it is perhaps courageous to focus exclusively on the landscape beyond the valley. Nevertheless, this is where the markets are at. Our approach is that where we find compelling value in high quality companies, we intend to invest with confidence and conviction. We retain slightly larger cash levels than normal and are thus well positioned to deploy as and when further opportunities arise.

Adrian Ezquerro
Head of Investments