The University of Queensland Business School

THE UNIVERSITY OF QUEENSLAND
AUSTRALIA
CREATE CHANGE

Student Managed Investment Fund Jan - Apr 2023 Update

Jan – April Fund Update

Dollar values are in AUD unless stated otherwise.

Fund Update

The three months to April 2023 have been a relatively less volatile period for Australian equities than the preceding period which was wrought with uncertainty surrounding central banks' pathway to zero inflation. Since this period, the RBA's hawkish stance has gained credibility, with the cash rate having been increased by 0.25 basis points five times in 2023 already despite fears of a slowing economy, taking the cash rate to 4.15% as of the 7th of June 2023.

Our expectations surrounding inflation have stayed constant over our tenure as portfolio managers, with our expectation that Australian CPI will begin to drop late 2022/early 2023 appearing to be on track with 2023 Q1 inflation having dropped to 7% from 7.8% in Q4 of 2022.

Our tenure marked the end of a near-zero cost of capital era that favoured high-growth companies, and the begging of a new era. Our vision of this new era was one of initial very high inflation, possible recession, and the begging of the return of value investing.

SMIF has delivered -0.66% of alpha over its benchmark with the fund delivering a total return of 9.49% compared to the All-Ordinaries total return of 10.15%.

Our performance was driven by a combination of our own microeconomic and macroeconomic beliefs, specifically that commodities prices would remain fundamentally strong over our tenure, with gold in particular being an important hedge in times of rising inflation and geopolitical turmoil. Our materials stocks Northern Star, DDH1, BHP, James Hardie, and Rio Tinto all benefited tremendously from this trend over the period, with Northern Star (ASX: NST) and DDH1 (ASX: DDH) being the top 2 contributors in the portfolio over the period. Additionally, our value stocks with strong economic moats that were able to combat inflation such as PWR Holdings (ASX: PWH) and Brambles (ASX: BXB) also drove alpha for the portfolio, with the stocks being the number 3 and number 4 contributors respectively over the period. Following rapidly increasing interest rates, Macquarie group (ASX: MQG) also delivered strong returns over the period being the number 4 contributor to the portfolio over the period.

Market Update

Monetary Policy Decision

In its latest meeting the RBA decided to increase the cash rate target by 25bpts. The decision comes in response to current CPI, which, although past its peak, remains high at 7 per cent. The RBA believes that these interest rate increases will help bring inflation back within the target range in a reasonable timeframe.

High inflation has been causing difficulties for individuals and the economy, eroding savings, straining family budgets, complicating business planning and investment, and exacerbating income inequality. The RBA has noted increased risks to the inflation outlook, with services price inflation remaining high and unit labour costs rising. The Australian economy's growth has slowed, and while the labour market conditions have eased, they remain tight with a slight increase in unemployment to 3.7 per cent in April.

Wage growth has responded to the tight labour market and high inflation, with an expected further increase in public sector wages. The RBA is closely monitoring the risk of ongoing high inflation leading to larger increases in prices and wages, especially given the limited spare capacity in the economy and the low unemployment rate.

The RBA's goal is to maintain economic stability as inflation returns to the 2-3 per cent target range but acknowledges the path to a soft landing is narrow. Uncertainties include the outlook for household consumption, with higher interest rates and cost-of-living pressures causing a significant slowdown in household spending. The global economy also presents uncertainties, with the RBA expecting below-average growth over the next few years.

International banking collapses

During the month of March, the US saw three banks collapse, marking some of the largest US banking collapses in history. In the lead-up to these events, many banks invested their reserves in low-yielding US Treasury securities. However, as the Federal Reserve raised interest rates between 2021 and 2023 in response to inflation, declining bond prices eroded the market value of bank capital reserves. Some banks experienced unrealised losses and had to sell bonds at significant losses to maintain liquidity. The bursting of the cryptocurrency bubble in late 2022 also negatively affected banks with exposure to cryptocurrencies and cryptocurrency-related firms.

The first bank to fail was Silvergate Bank, a cryptocurrency-focused institution, which announced its wind-down on 8th March 2023, due to losses in its loan portfolio. Silicon Valley Bank, heavily focused on the technology industry, experienced a bank run after announcing an attempt to raise capital, leading to its collapse and seizure by regulators two days later. Signature Bank, known for its involvement with cryptocurrency firms, was closed by regulators on 12th March, citing systemic risks.

Lastly, First Republic Bank become the second large regional bank with assets over US$200 billion to fail in just a few weeks. Similar to Silicon Valley Bank, which was seized by the government on 10th March, First Republic catered to a wealthy clientele, which helped it grow deposits rapidly but may have also contributed to its undoing. The bank's business model left it susceptible to a sudden rise in interest rates.

Once Silicon Valley Bank collapsed, clients began withdrawing their money from First Republic, fearing their deposits were at risk. The bank reported that depositors had withdrawn over US$100 billion, mostly during a few days in mid-March. Additionally, the value of the bank's large loans dropped as the Federal Reserve raised interest rates, making it challenging to sell them at a profit.

Government intervention was ultimately necessary to mitigate the fallout from these collapses, with the events highlighting the challenges faced by banks due to declining bond prices, exposure to cryptocurrency risks, and the withdrawal of deposits by concerned customers.

Summit Capital believe that the risk of contagion effects in Australia are low, with domestic banks remaining locally-focussed and having successfully passed recent stress tests by regulators. Moreover, we do not believe the recent banking collapses pose specific risks to the holdings in the SMIF portfolio. However, fluctuations in the Australian market, especially in sectors sensitive to the global economy and the US dollar may occur due to continued uncertainties abroad. It will be crucial for the RBA to monitor the situation, as a prolonged unease in the US banking sector and a downgrade in the domestic economic outlook may necessitate further rate hikes.

Position Updates

Codan (ASX: CDA 80.94%)

In January, the Codan share price surged by 19%, following the release of a trade update, which outlined management's expectations for revenue to hit the high end of its previous forecast at $215m. This cascades into an increased expectation of net profit in excess $31m, which overtook previous guidance of $25m. It is clear shareholders responded positively to this news.

By the end of April, Codan held the title of fourth best performing ASX-300 share in 2023, which contrasts heavily with the sell off in the second half of 2022, due to concerns of weakening detector demand. Increased defence expenditure and a resurgence in gold prices are two key drivers for the share price through the first half of 2023.

Investors are also expecting the strength of patented technology in the minelabs segment to further bolster these sales, alongside the stable communications revenue stream.

Codan subsidiary Zetron has agreed to acquire a 100% interest in GeoConex, which is a leading integrator of US Public Safety and Homeland Security systems. The acquisition is a significant opportunity for Codan to participate in the emergency response upgrade in the US, supported by US Government NG911 funding. Additionally, this acquisition will allow Codan to encapsulate a market-leading position in the US and accelerate growth for the combined business.

James Hardie Industries (ASX: JHX 26.86%)

After facing heavy selling pressure in December 2022, James Hardie shares have rebounded without significant news in January. The two driving reasons for this large sell off in December 2022 were largely attributed to interest rates and inflation. Elevated inflation and rising interest rates are both negative for the housing industry, which James Hardie operate in. In conjunction, global supply chain issues have largely effected construction activity, which compounded effects. The Australian Bureau of Statistics have released figures suggesting, there has been a 15% decline in new home builds and a 34% decline in apartment builds.

Considering inflation figures are now falling ahead of previous market expectations, the reduced guidance from James Hardie leading to a sell off, now appears to be overstated. With stabilisation in housing prices, James Hardie gained attention as a opportunity for investors to capitalize on a beaten down stock. Many analysts have a positive outlook for James Hardie throughout 2023, with many of the previously feared headwinds easing.

Sonic Healthcare (ASX: SHL 20.25%)

Sonic Healthcare shares soared to a three-month high after the company reported a profit increase of 50% from pre-pandemic levels. Falling PCR testing since the peak of Covid-19 a year earlier led to a fall in revenue of 14% and a fall in net profit of 54%.

Despite these reductions having a material impact on YoY growth, Sonic CEO, Colin Goldschmidt, claimed the reductions in Covid-19 related revenues had overshadowed the core business operation successes. The base business revenue had grown 6% since last year, providing shareholders with a 42 cent fully franked interim dividend.

Guidance suggested January 2023 was over 10% greater than pre pandemic levels, which is driven by its stable pathology business, while PCR testing volumes fluctuate across the world as outbreaks occur in different regions. While the core business is proving successful and Covid related operations are detracting, the company has decided to keep its Covid related business to take advantage of new strains developing.

Northern Star Resources (ASX: NST -24.81%)

Northern Star Resources has faced various challenges through the beginning of 2023. A key headwind was the shutdown of operations at the Pogo gold mine in Alaska. The damage of a ball mill motor required repairs, which prevented production for six weeks. While Northern Star implemented cost management initiatives, the prioritisation of staff reduced production in the short term. Despite these effects being labelled as short term by management, fears emerged of reduced production effecting the company’s ability to meet end of year guidance targets.

This interruption was exacerbated by more extend mill downtime in Northern Star’s Kalgoorlie production centre. Unplanned mill downtime has shown to be a challenge for Norther Star, despite the optimism reflected by management.

Elders Ltd (ASX: ELD -20.02%)

While the market perception of Australian agriculture industry is quite strong the drawdown of Elders is surprising and points toward firm specific factors. Firstly, there are margin pressures in generic crop protection commodities and these pressures are expected to be in effect over the short term. This is expected to tie into earnings and livestock prices, which are expected to fall by 10 to 15%.

The ASX queried Elders for the drop in share price whether any new information needed to be disclosed to the market. In response, Elders lodged an eight-page presentation with the ASX. The briefings outlined livestock prices, the effects of wet conditions outside of seasonality and slowing real estate activity. Alongside these points, Elders also disclosed winter crop outlook and the succession planning at Elders.

Ingenia Group (ASX: INA -14.50%)

Ingenia Group shares have fallen significantly throughout the start of 2023, as management have reduced guidance for the full year. The half year results for FY23 revealed that forecasts for EBIT growth had decreased from 30% to a range of 0% to 10%. Following this announcement, shares had fallen 21.85%. While sparking fears from many investors, shares went into a trading halt as per the company’s request. This trading halt allowed the company to review its home settlement forecasts that had recently been updated to confirm the impact on EBIT growth.

While Ingenia had an expanded asset base and growth in rents across residential portfolios, the production and settlement delays resulted in the guidance downgrade.

Ingenia look to weather the effects of labour shortages, elevated inflation and interest rates, but acknowledge the effect these factors have on delays.

IPH (ASX: IPH -4.91%)

IPH alerted customers of a cyber incident in mid-March, which potentially effected hundreds of thousands of customers. Alongside IPH, two member firms and personal loans provider Latitude Group were also affected by the cyber incident.

The cyber incident involved the document management system (DMS) of its head office. The DMS includes administration documents, client documents and correspondence. One day after the hack occurred, IPH entered a trading halt to address the issue.

This cyber attack is under investigation and is expected to take some time to complete. Evidently, shareholders did not respond positively to this incident.

Cleanaway Waste Ltd (ASX: CWY -7.05%)

Cleanaway workers took industrial action across five depots in NSW and ACT, while negotiations were in place between Shepparton City Council and Cleanaway for a multi-million-dollar contract. Cleanaway has faced challenges including a lack of drivers and was recently under a spotlight over a $600,000 fine for environmental offences in NSW.

The ongoing industrial disputes with workers and Cleanaway management has also been reflected in the market as the labour headwinds are unlikely to ease over the short term. Alongside these issues, Cleanaway has also faced inflationary pressure imposing higher costs on the firm. Evidently, the share price has been beaten down however, margins are expected to improve over as labour efficiencies increase.

PWR Holdings Ltd (ASX: PWH -6.30%)

Despite falling slowly since January, PWR has shown no significant events underpinning market sell pressure. PWR is most commonly recognized for its production and supply of Formula One cooling systems, however, this is likely to change. PWR cooling systems are sought after in Electric Vehicles, where PWR have identified a UK acquisition being advantageous for expansion into the global market.

After disclosing involvement with seven different EV supply arrangements, perhaps investors do not share the same vision as management. PWR has not been shy to make acquisitions, where it has made two in the last seven months, so it is likely the EV strategy is distracting PWR from its historic Formula One cooling system focus.

Performance:

	Jan-Apr 2023	Jan-Apr 2022	LTM (as of 30th April)	Inception p.a.*
SMIF	4.81%	-3.70%	-0.89%	9.49%
All Ordinaries Accumulation Index	7.10%	-0.79%	1.83%	10.15%
Alpha	-2.29%	-2.91%	-2.72%	-0.66%

Alpha may not equal SMIF return minus All Ordinaries return due to rounding.

* Return since fund inception on 19 November 2018.

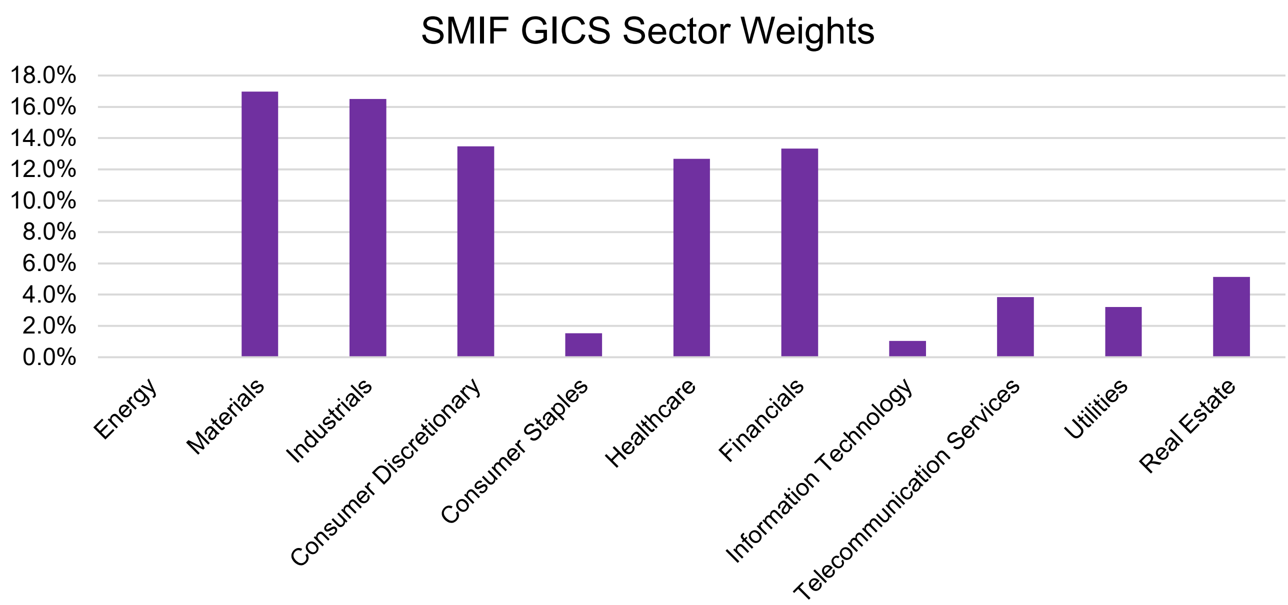
Sector Breakdown:

	% Weight	Change in rank
Energy	0.00%	
Materials	16.96%	
Industrials	16.50%	
Consumer Discretionary	13.47%	
Consumer Staples	1.53%	
Healthcare	12.67%	
Financials	13.33%	
Information Technology	1.05%	
Telecommunication Services	3.85%	
Utilities	3.21%	
Real Estate	5.14%	

Contributors to Returns (%)

Top 5 Contributors (%)	
CDA	80.94%
JHX	26.86%
NST	24.81%
SHL	20.25%
BXB	19.74%

Top 5 Detractors (%)	
ELD	-20.02%
BOQ	-15.94%
CWY	-7.05%
PWH	-6.30%
IPH	-4.91%



Cannot retrieve All Ordinaries weightings for periods prior Jan-Apr 2023.

SMIF Portfolio Holdings:

Ticker	Company Name	Portfolio Weight	Position 30th April	Capital Gains	Dividends	Return*
MQG	Macquarie Group Ltd	7.79%	$22,642	9.9%	4.4%	13.4%
PWH	PWR Holdings Ltd	5.69%	$16,546	39.2%	3.5%	41.1%
JLG	Johns Lyng Group	4.41%	$12,810	42.8%	3.4%	44.6%
DDH	DDH1 Drilling Ltd	4.37%	$12,702	7.6%	10.8%	18.4%
RMD	Resmed Inc	4.20%	$12,203	15.8%	1.1%	16.5%
BXB	Brambles Ltd	4.19%	$12,170	15.6%	3.4%	18.5%
CNU	Chorus Ltd	3.85%	$11,182	11.6%	5.2%	15.6%
SHL	Sonic Healthcare	3.50%	$10,171	11.4%	4.8%	14.8%
NST	Northern Star Resources	3.48%	$10,122	31.2%	4.9%	33.6%
BHP	BHP Group Ltd	3.44%	$9,990	8.4%	12.8%	18.9%
CSL	CSL Ltd	3.41%	$9,919	7.9%	1.4%	9.0%
CWY	Cleanaway Waste Ltd	3.27%	$9,503	3.1%	2.5%	5.4%
WES	Wesfarmers Limited	3.25%	$9,459	10.8%	5.7%	16.5%
APA	APA Group	3.20%	$9,314	-2.7%	4.7%	2.2%
JHX	James Hardie Industries	2.90%	$8,439	6.8%	2.1%	8.6%
CLW	Charter Hall REIT	2.90%	$8,439	-4.6%	6.1%	1.8%
CAR	Carsales.Com Ltd	2.85%	$8,292	2.3%	3.1%	5.3%
SUN	Suncorp Group Ltd	2.83%	$8,237	9.9%	8.2%	17.4%
RIO	Rio Tinto Ltd	2.74%	$7,970	6.5%	12.4%	17.4%
BOQ	Bank Of Queensland	2.68%	$7,807	-23.0%	4.6%	-18.4%
QUB	Qube Holdings Ltd	2.66%	$7,721	4.0%	3.4%	7.0%
INA	Ingenia Group	2.23%	$6,478	4.6%	2.7%	7.2%
IPH	Iph Ltd	1.95%	$5,668	2.8%	4.8%	7.4%
DSK	Dusk Group	1.65%	$4,794	-35.8%	8.4%	-25.5%
IDX	Integral Diagnostics	1.54%	$4,468	-2.3%	3.6%	1.4%
ELD	Elders Ltd	1.53%	$4,444	-19.0%	4.4%	-13.6%
CDA	Codan Ltd	1.04%	$3,033	-18.8%	2.9%	-14.9%
WDS	Woodside Energy	0.46%	$1,347	13.2%	18.0%	31.2%
CASH	Cash and Dividends Receivable	12.01%	$34,918			
		Total	**290,788**			

*Total return on each position since purchase
**Uniti privatisation is accounted for in the Cash and Dividends Receivable

Portfolio Management Team

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Information on the Fund and Disclaimer

This update has been prepared by the student portfolio managers of the University of Queensland Business School Student Managed Investment Fund. The Fund was seeded by the University with $200,000 in 2018 and the first investments were made in November 2018. The University of Queensland is the sole owner of the assets in the Fund and no fees are payable by the University for the management of the Fund. The Fund recognises the support of Morgans Brisbane as stockbroker to the Fund.

The information in this update is prepared primarily for educational purposes and to keep internal and external Fund stakeholders informed. Any views expressed in this update are the views of the student portfolio managers. The accuracy, reliability or completeness of data or information presented in this update is not guaranteed. The information is not intended as a securities recommendation or statement of opinion intended to influence a person or persons in making a decision in relation to an investment.