EthicalPartners FUNDS MANAGEMENT

Ethical Partners Australian Share Fund

JULY 2021

Ethical Partners Funds Management is a boutique Australian fund manager which is fully owned by its staff. We have a dual focus on performance and investing ethically over the long term. Our approach directly manages risk for our clients, provides the ability to invest in line with your values and actively advocates for change. Investors in the Fund invest alongside the owners and managers of Ethical Partners. The Fund has adopted a Net Zero Emissions by 2050 target.

	INVESTOR CLASS	CLASS A	CLASS B	CLASS C	CLASS E
Unit Price 31/7/21	$1.0255	$1.0188	$1.0290	$1.0107	$1.0225
APIR code	EPF9951AU	EPF9964AU	EPF3813AU	ETL8683AU	-

INCEPTION DATE
8 August 2018

BENCHMARK
S&P/ASX 300 Accum. Index

UNIT PRICING
Daily

DISTRIBUTIONS
Every six months

BUY/SELL SPREAD
0.20%

MANAGEMENT FEE (PDS)
0.95%

PERFORMANCE FEE (PDS)
15% of outperformance

MINIMUM INVESTMENT
$25,000

INVESTMENT DIRECTOR & CEO
Nathan Parkin & Matt Nacard

GOOD INVESTING PODCAST
Link to the latest episode

NET ZERO 2050
Read about Net Zero 2050 here

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Link to PDS

MONTHLY COMMENTARY

During July the Fund returned 1.18% versus the S&P/ASX 300 Accumulation Index of 1.11%, outperforming the market by 0.08%. An overweight position in Consumer Staples detracted from relative performance while stocks in the Materials sector contributed to relative performance during the month.

Over the last 12 months the Fund has returned 30.46% versus the market at 29.14%, outperforming by 1.32%. We believe there is a change in equity market leadership that is driving the market higher. We have observed that the stocks of companies with cyclical earnings that have reported better than expected earnings are continuing to be supported by markets and generally trading higher post results. At the other end of the spectrum the companies with full valuations that are already trading on large premiums to the market (and with higher expectations) are trading flat to down post results.

Comparing the Australian market versus the US market, the S&P500 has outperformed the S&P/ASX 300 Accumulation Index by around 18% from pre COVID levels. The US market has rebounded more strongly from COVID related lows on the back of a higher proportion of the market in growth companies (Tech and Healthcare 43% of market cap vs Australia at 14.2% of market cap) as well as recording FY21 earnings growth of 43.8% versus Australian at 25.7%. Looking ahead, market expectations for the S&P500 are at +9.5% earnings growth in FY22 versus Australia at +20.5% earnings growth. Coupled with the Australian market PE at 16.1x (NTM) and the US PE at 21.7x (NTM) and the Australian market having a greater proportion of cyclicals, Australian equities look relatively good value, in our view.

(… over)

SIGNIFICANT HOLDINGS

Australian Clinical Labs (ACL)
Bega Cheese (BGA)
Graincorp (GNC)
IGO Limited (IGO)
Insurance Australia Group (IAG)
OZ Minerals (OZL)
Macquarie Group (MQG)
Meridian Energy (MEZ)
Mirvac (MGR)
Westpac (WBC)

Performance as at 31 July, 2021

INVESTOR CLASS	1 MONTH %	3 MONTHS %	6 MONTHS %	12 MONTHS %	SINCE INCEPTION (ANNUALISED %)
Fund (after fees)	1.18	4.02	11.02	30.46	3.00
S&P/ASX 300 Accum	1.11	5.77	13.86	29.14	9.85
Excess	0.08	-1.75	-2.84	1.32	-6.85

But despite this there are still signs of excess in equity markets here. Square's all-scrip acquisition of Afterpay (not held in the Fund), the largest Australian corporate deal ever done, announced on the 2nd of August has reminiscent signs of other mega cap deals done at extreme valuations. Square, which is issuing shares at 46x book value to acquire a company on 22x book value in all-scrip bid that valued Afterpay at $39bn, and a 30% premium to last, may be a marker for peak valuation of unprofitable companies.

Back on 10 January 2000, America Online announced plans to acquire Time Warner for $182bn (all USD) of stock and debt, creating the $350bn entity AOL Time Warner (with a book value $209 million and net income earnings of $1.1bn). The deal at the time valued Time Warner at $165bn roughly double its pre deal market cap and was the largest in US history. Stephen Case, a co-founder of AOL, said, "This is a historic moment in which new media has truly come of age." The company reported a goodwill write-off of nearly $99 billion in 2002.

Adding to the current mood are Ken Moelis' comments on the Moelis 2Q21 update: "And lastly, I'd say, there's a whole new asset class. I read somewhere I think yesterday that we're up to 900 unicorns… But when you have 900 unicorns that I think have a market capitalization of $3 trillion that's another asset class that will do something. Some may go public, but some move to M&A and I believe that's almost the market capitalization equivalent to private equity at this point".

By recounting these we are not saying there is no future value in global payments businesses or any of the unlisted tech but when there are 900 companies that are valued over $1bn and likely largely unprofitable, it seems like a lot. We are simply watching for signs that valuations for unprofitable companies may be at the peak cycle and large cap expensive-scrip-for-expensive-scrip deals can be one sign that we are there.

Of course if the valuation expansion cycle has run its course and the market has dreamed up too-robust valuations for companies with a big future but no earnings, it is time to own profitable companies that have low expectations around future earnings growth and where fundamentals and prospects are strong today. Especially in a world where economies are opening up (eventually) and demand is robust in key commodities and markets. We believe this is the equity market leadership change that is currently taking place.

ESG AND ENGAGEMENT COMMENTARY

Net-Zero 2050 Commitment for our Australian Equities Unit Trust

Ethical Partners has since inception carefully considered climate change risk within its investment process and integrated the opportunities and risks presented by climate change. We are excited to now extend this into a formal commitment to a Net-Zero 2050 target for the Ethical Partners Australian Share Fund. We continue to manage our mandate portfolios in line with clients' own individual climate change commitments. Ethical Partners will be now working towards setting clear and actionable interim targets to reach the 2050 goal and ideally bring that goal forward. We look forward to discussing this target with our clients, continuing our learning about how we can achieve these targets, continuing our advocacy on climate policy development and ongoing engagement with all our portfolio companies on how they can achieve these goals. Further details here.

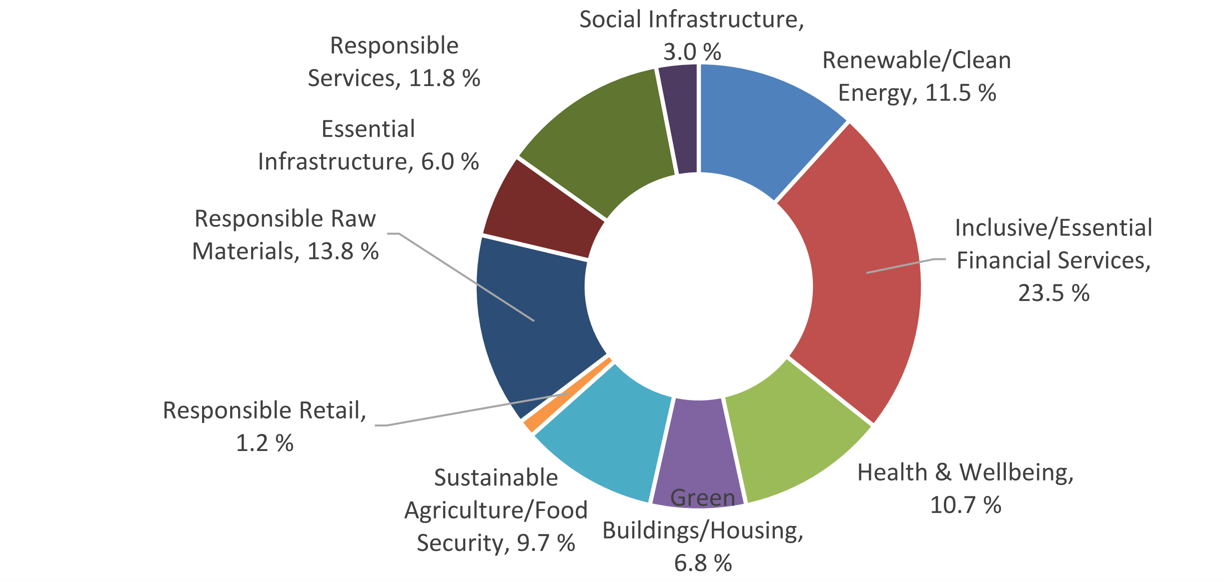
2021 Ethical Standards Report

This research is drawn from the results of our Ethical Partners Opportunity and Risk Assessment (EPORA) process and we believe it provides an important "snapshot" of the state of ESG reporting and disclosure across 216 ASX companies. It also discusses why these topics are so important to corporates and investors including the improvements, gaps and nuances we found and the next steps in corporate reporting standards that we believe ASX listed companies need to embrace. These are also areas that Ethical Partners will continue to engage on with companies and advocate for improvement across the ASX. Further details here.

Ethical Partners appeared before the Joint Standing Committee on Trade on Investment Growth

On Wednesday, 17 February 2021, the Joint Standing Committee on Trade and Investment Growth resolved to inquire into and report on the prudential regulation of investment in Australia's export industries. Ethical Partners made a joint submission to this inquiry with the Australian Centre for Corporate Responsibility (ACCR) and was subsequently asked to appear as a witness to the inquiry. Ethical Partners appeared before the inquiry panel on the 28th July 2021. Ethical Partners was grateful for the opportunity to explain to the panel from an investors point of view the economic case towards the consideration of ESG risks in investments. We also spoke about how we view the risks and opportunities in investing in industries exposed to energy transition risks, the difficulty in justifying favourable long-term valuations for fossil fuel companies, the opportunities for companies proactively mitigating these risk and our active engagements with companies and policymakers to encourage a timely, orderly and just transition. Ethical Partners' Opening Statement can be seen here.

SECTOR EXPOSURE, JULY 2021



The **Good Investing Podcast** connects you with successful investors and business leaders who invest in, or are experts in, a range of industries… but do it with a difference. These leaders of industry are the best at what they do in their chosen field but all have one thing in common - they are passionate about doing things the right way and giving back to the communities in which they operate. **Ep#3: Barry Irvin… Executive Chairman of Bega Cheese talks about milking cows while topping Bega High, starting Giant Steps and "owning" not "fearing" the Lion.** Link: https://www.ethicalpartners.com.au/podcasts or go to Apple Podcasts, Google Podcasts, Spotify.

NetZero 2050 AUSTRALIAN SHARE FUND

Investor Group on Climate Change

Zenith RECOMMENDED

PRI Principles for Responsible Investment