Macquarie Australian Small Companies Fund

Monthly report – 31 December 2022

Investment objective

Aims to outperform the S&P/ASX Small Ordinaries Accumulation Index (**Index**) over the medium to long term (before fees). It aims to provide capital growth and some income.

Key information

Fund details	
APIR code	MAQ0454AU
Inception date	6 July 2006
Fund size	$297.4m
Distribution frequency	Quarterly
Management fee*	0.60% pa
Performance fee*	15% of outperformance of the Fund (after management fee and expenses) above return of the Index, subject to a 'high watermark'
Minimum investment (Direct)	$20,000
Unit prices and spreads	macquarie.com.au/unit_prices

*Read the Product Disclosure Statement for more details on fees and costs.

Fund performance to 31 December 2022

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)
1 month (%)	-2.98	-3.04	-3.73	0.69
3 months (%)	10.65	10.31	7.54	2.77
1 year (%)	-5.76	-6.73	-18.38	11.65
3 years (% pa)	9.85	8.83	1.38	7.45
5 years (% pa)	10.70	9.47	2.92	6.55
Since inception (% pa)	10.90	9.47	2.90	6.57

Past performance is not a reliable indicator of future performance.

Total returns are calculated based on changes in net asset values and assumes the reinvestment of distributions.

Total net Fund returns are quoted after the deduction of fees and expenses. Due to individual circumstances, your net returns may differ from the net returns quoted above.

The management fee was reduced to 0.60% pa from 18 January 2017.

Top 5 overweight positions (alphabetical)

Centuria Capital Limited
Champion Iron Ltd
News Corporation
Nufarm Limited
Spark New Zealand Ltd

Top 3 stock attribution (alphabetical)

Champion Iron Ltd
Core Lithium Ltd
New Hope Corporation Limited

*Italics denotes underweight

Bottom 3 stock attribution (alphabetical)

Chalice Gold Mines Limited
Johns Lyng Group Ltd
Liontown Resources Limited

*Italics denotes underweight

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Fund highlights

In December, the Fund finished down -3.04% (post-fees), outperforming the benchmark by 0.69%.

The key contributors to relative performance included overweight positions Champion Iron (CIA) and Spark New Zealand (SPK), and an underweight position in Core Lithium (CXO).

Iron-ore producer Champion Iron outperformed for the period as iron ore prices continued to rise.

New Zealand telecommunications company Spark New Zealand, which was recently added to the ASX200, outperformed due to its defensive characteristics in weak market conditions.

The key detractors from relative performance included overweight positions in Liontown Resources (LTR) and Johns Lyng Group (JLG), and an underweight position in Chalice Mining (CHN).

Lithium producer Liontown Resources underperformed, giving back some of their strong 2022 gains, amid increased uncertainty of lithium demand from China.

Building services company Johns Lyng Group underperformed for the period after the market reacted to the Chief Operating Officer selling 31% of his shares in the company.

Market overview

Australian equities fell in December, with the S&P/ASX Small Ordinaries Accumulation Index finishing the month down -3.7%, slightly underperforming the broader market with the S&P/ASX 300 Accumulation Index returning -3.3% for the period.

Australian shares outperformed global shares (MSCI global -4.3%) and the various US equities markets (S&P500 down -5.9%, NASDAQ down -8.7%). Central bank commitment to returning inflation to pre-pandemic levels continues to weigh on the big US technology companies which are large constituents of these indices.

Outside Australia, the Federal Reserve's battle against US inflation continues to set the stage for US growth and consequently global growth. Even though the Fed increased rates by a smaller 50bp compared to recent meetings, the continued strength of services inflation along with a tight labour market but lower participation (compared to Australia) means further rate rises are inevitable. Comments by the Fed following the December meeting confirmed the battle against these "stickier" elements of inflation will continue well into 2023. Subsequently the forecast peak official rate increased and the risk of the US economy falling into recession became a little higher – both triggering the sell-off in global equities in December.

In December, Australian shares did not fall as much as global shares as the risks of recession remains low. Most economists expect the RBA to pause rate rises early in 2023 after the central bank lifted rates by only 25bp at the December meeting. The latest monthly CPI series printed lower than expected however the labour market remains strong; unemployment is at a record low of 3.4% and the participation is at a record high. However, house prices continue to weaken from their pandemic high and this will function as a brake on further RBA rate hikes with lower house prices flowing on to lower consumer spending (via the wealth effect) and impacting the housing and construction industry. This is already evident with downgrades in Domain (where profits are a function of sale listings) and James Hardie during December.

For the Small Ordinaries, all sectors retreated last month (except for consumer staples which were flat). The worst performing sector was consumer discretionary (-5.4%), which was weak on market concerns that consumer spending will slow in 2023 as rising interest rates begin to take effect. Information technology (-4.9%) followed the US NASDAQ index and was weak again, cementing a poor year of performance. Finally, healthcare (-4.8%) also underperformed.

Commodity prices had mixed results during the month. Brent oil fell -1.2% while Iron ore rose by +19.0%. Gold prices continued to rise, seeing a gain of +3.8%.

Australian 10-year yields bounced back, increasing by 0.52% to 4.05%. This was also seen in the US, where 10-year yields rose by 0.18% to 3.88%. The AUD strengthened against the USD, gaining 1.3% for the month.

Outlook

Moving into 2023, market focus will increasingly turn to the trajectory of company earnings as it assesses the impact of interest rates increases on demand. Company valuations have improved considerably over 2022 and in most cases, factor in a moderate earnings slowdown. Whether this buffer is sufficient will depend on the depth and duration of an economic slowdown. The first test will be the upcoming February results period.

Other challenges facing the market include the potential for another round of supply chain disruption as China grapples with its current COVID outbreak as well as heightened geo-political risk.

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For more information speak to your financial adviser, call us on 1800 814 523, email mam.clientservice@macquarie.com or visit macquarieim.com

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