Aberdeen Standard Focused Sustainable Australian Equity Fund

Aberdeen Standard Investments

31 August 2021

Market Review

Australian equities gained over August, with healthcare, technology and financial stocks driving strong gains in the first half of the month. However, markets struggled thereafter, as New South Wales (NSW) and Victoria went into hard lockdowns as Covid-19 cases in those states surged. NSW, Australia's largest state, plans to stay shut during September and possibly October. And while vaccination rollouts lagged most developed economies, we have seen good momentum on this front recently.

Elsewhere, in monetary policy, the Reserve Bank of Australia (RBA) kept the cash rate at the record low of 0.1%, after confirming in July it would likely remain unchanged until at least 2024. The RBA cut its bond buying programme at the beginning of August to A$4 billion from A$5 billion. The central bank said it would continue monitoring the economic impact of the latest lockdowns and did not rule out taking further action if the situation deteriorated. Meanwhile, the RBA had initially forecast a contraction of 1% for the quarter, before the latest Covid-19 restrictions were imposed.

The economy continued to slow, with the Delta variant of Covid-19 having a negative impact on business confidence (through the purchasing managers' index) and consumer sentiment (with falling retail sales). The highlight was unemployment, which fell to 4.6%, its lowest level in 13 years.

Portfolio Review

The Fund rose by 5.76% (gross of fees) and by 5.69% (net of fees) in August. This was ahead of its performance target, which rose by 2.50%.

Pinnacle Investment Management (PNI) benefited from a strong rebound in funds under management inflows as prior investment in expanding the sales distribution team started paying off. Another positive was the strong performance of affiliate managers across a blend of investment strategies. Elsewhere, Afterpay (APT) benefited from an all-script takeover offer from US payment behemoth Square. The proposed transaction is subject to a shareholder vote and other customary approvals, and was struck at a 31% premium to the prevailing share price.

Conversely, Altium (ALU) detracted, with the deferral of its 2025 targets (i.e. A$500 million in revenues) and the company backtracking on longer-term margin aspirations driving the share price down. This follows the Board's recent rejection of a takeover offer at a higher share price. We continue to view Altium as a business with superior product intellectual property, although this needs to be matched by more consistent execution in order to fully realise long-term value. Cochlear (COH) also lagged over August. While the fiscal year 2021 result was largely in line with expectations, the shares underperformed as forward guidance disappointed, given the wide range for net profit after tax growth of 11-20%, and continued investment in growing market awareness. However, we continue to view COH as the market leader in hearing implants, offering significant growth potential, which continues to support our longer-term thesis.

In terms of activity, we increased our position in IDP Education (IEL), taking advantage of a partial sell down by a major shareholder. This also reflects our conviction that the business is poised to benefit materially over the next 12-18 months as international border restrictions start to ease, driving a strong recovery in international student enrolments.

Outlook

As we see the domestic economy begin to reopen, we expect a strong rebound in the fundamental drivers of business confidence, consumer sentiment and unemployment. While we believe the momentum in earnings growth has peaked, we still expect a positive growth skew over the coming months and the earnings up-cycle to continue.

In addition, the central bank's pledge to keep interest rates lower for longer should support asset prices. A strengthening property market will also boost consumer spending, construction and employment.

Investment strategy

The Fund utilises Aberdeen Standard Investments' Sustainable and Responsible Investment process to invest primarily in a concentrated portfolio of around 20-35 companies that are listed or proceeding to listing on the Australian Securities Exchange (ASX) and have the potential for capital growth and increased earning potential.

Investment objective

To outperform the benchmark, the S&P/ ASX 200 Accumulation Index, after fees, over rolling three year periods.

At the corporate level, as the recovery continues, companies are likely to move from capital preservation to capital allocation, with a notable pick-up in M&A activity and capital management.

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, in terms of their robust balance sheets and prospects for through-cycle earnings and dividend growth, is an added advantage. Many are also leaders on governance and sustainability, positioning them well to adapt to future challenges and opportunities. This will ensure that the portfolio remains resilient amid present uncertainties and well-placed to deliver steady returns in the long run.

Fund performance is available on the relevant factsheet.

The opinions expressed are those of Aberdeen Standard Investments as of the date of publication and are subject to change at any time due to changes in market or economic conditions.

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