

Aberdeen Standard Focused Sustainable Australian Equity Fund



31 October 2021

Market Review

Australian equities fell slightly in October. Commodities such as gold and copper, rose and the Australian dollar strengthened over the month.

There was optimism across the country as lockdowns eased in many regions. New South Wales moved to a two-tier system, giving vaccinated citizens greater freedom. Melbourne was released from lockdown after nearly nine months of restrictions. Vaccination rates have continued to rise, with over 65% of adults in Australia fully vaccinated by the end of October. Authorities also lifted the travel ban restricting Australian citizens from leaving the country without permission at the end of the month. Meanwhile, the government indicated that it may soon relax rules for foreign citizens entering the country.

In part due to the greater freedoms, October's purchasing managers' index (PMI) data showed a notable uptick in business sentiment. Reopening pushed the services sector figure above 50, after three months of contraction, while the manufacturing sector expanded at the fastest pace in four months. Meanwhile, a preliminary reading showed that retail sales rebounded in September, rising by 1.3% month-on-month.

The Reserve Bank of Australia (RBA) maintained its cash interest rate at 0.1% after its October meeting. Policymakers repeated the central bank's commitment to holding rates until the country has reached inflation and employment targets, suggesting this might not happen until 2024. Late in the month, September's figures put core inflation at 0.8% in the third quarter, higher than the 0.5% forecasted the fastest pace of increase since 2015.

Portfolio Review

The Fund returned 1.65% (gross of fees) and 1.58% (net of fees) in October. This was ahead of its performance target, which returned -0.10%.

On a stock-specific basis, Netwealth contributed to performance. Its share price

gained after the firm achieved stronger-than-expected net inflows for the first quarter, leading to an upgrade to its growth outlook. Meanwhile, the company recently announced a proposed acquisition of wealth platform peer Praemium. While Praemium's board rejected the offer, we view these developments as strategically positive for Netwealth. Elsewhere, Xero outperformed amid a strong recovery within the broader technology sector. We continue to view the company as one of the highest-quality software businesses within the sector. IDP Education again performed well over the month. The pathway to the reopening of borders is now clearer, which is a positive step towards the return of international students to Australia.

On the other hand, Mirvac fell over the month, due to concerns about rising bond yields, which was viewed negatively across the yield-sensitive property sector. However, the company had a strong fiscal first quarter and reiterated its earnings guidance. Meanwhile, Medibank retreated on little stock-specific news. However, investors are focusing on the likelihood of rising claims costs as lockdown restrictions ease in the eastern states. Spark New Zealand also fell, with the current inflation outlook causing a steep rise in long-term bond yields being the most likely driver of share-price weakness.

There was no major trading activity over October.

In terms of engagement, we met with both the incoming and outgoing chairman of Insurance Australia Group (IAG) to discuss recent concerns about risk management and executive changes. While the meeting highlighted that the recent issues surrounding customer refunds and the wording of business interruption policy should have been addressed earlier, there was good indication that the board have undertaken a thorough review of risk systems and culture, held executives to account by way of clawing back past compensation and have aligned future key performance indicators accordingly. We are comfortable that the bulk of these legacy

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.

issues have now been addressed, and that IAG can return to focusing on growing its core business and driving margin improvement in the medium term.

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.

While we are monitoring inflation closely, we expect central banks to react cautiously with a view of ensuring stability of asset prices. 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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