MARTIN CURRIE

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REPORTING SEASON WRAP: LOOKING OVER THE EDGE

After mounting inflationary pressures, there are signs that the slowdown in consumer spending has begun. As we stand on the edge of a mortgage rate cliff and a potential Australian recession, how did these important market developments impact the shape of company results in Australia's February 2023 company reporting season? And what does it mean for Value, Sustainable and Income-style investors?

Reece Birtles, CFA, GAICD

Chief Investment Officer
Martin Currie Australia

Introduction

In the six months since we provided our wrap of Australia's reporting season "Paying the Piper", we have really seen the significant Reserve Bank of Australia (RBA) rate rises and inflation impacts that were just beginning to show.

We are now much further through the cycle and "looking over the edge" of a potential earnings recession, GDP recession, or both. At the time of writing, we are also absorbing news of the collapse of Silicon Valley Bank (SVB) in the US which has added further complexity into an already uncertain outlook.

Our analysis and one-on-one meetings with company management over February and March have highlighted that the consumer was still showing resilience in spending and company revenues remain strong. However, margin pressures are beginning to bite at earnings growth as sales begin to slow and costs continue to rise. And this is before the likely future interest rate rises and mortgage cliff.

As the world continues to normalise to higher rates and long-term inflation expectations, the market thematic continues to play towards an ongoing attractive environment for the Value style.

It is as important as ever for investors to be discerning in their stock picking, focussing on companies that can grow earnings and dividends in this environment and not be exposed to valuation risk.

Contents

Our bi-annual reporting season paper will cover the following in finer detail:

- Our top-down analytical and aggregated review of the reporting season's results for S&P/ASX 200 stocks. *Page 3*
- A deeper dive into the issues and themes that are driving earnings results – based on the 100+ meetings with company management teams undertaken by the MCA investment team over the period. *Page 6*
- The big picture outlook for Australian equities, and how our views are reflected in our portfolio positioning across Value, Sustainable and Income styles. *Page 11*
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Definitions

What we do each reporting season

On top of our fundamental analysis and company engagement on individual stocks, we have a framework to overlay an analytical market wide view of the reporting season's results for the stocks in the S&P/ASX 200 index.

This aggregated review allows us to more logically judge the overall pulse of the market. We can then assess the themes across the market that would be 'hard to see' when looking at each company result in isolation and apply our insight at the stock and portfolio level.

Key definitions used in our top-down analytical review

-12m: prior 12 month actual.

LTM: last 12 months actual.

NTM: next 12 months actual.

Surprise: the average difference where there is a >+/-2% difference between company reported results and broker consensus forecasts.

Follow-on Revisions: the average change in broker consensus NTM forecasts after companies have reported their results.

Price reaction: stock price movement of more than +/-3% within the two days after companies have reported their results.

Reporting Score: based on a simple average of Surprise, Revisions, Price Reaction.

Price to earnings (P/E) re-rate: change in price during the season versus the change in broker consensus earnings forecasts over the same period.

Data is calculated using the weighted average of broker consensus forecasts of each portfolio holding – because of this, the returns quoted are estimated figures and are therefore not guaranteed and may differ materially from the figures mentioned. The figures may also be affected by inaccurate assumptions or by known or unknown risks and uncertainties.

For broker consensus data, the number of brokers included for each individual stock will depending on active coverage of that stock by a broker at any point in time. A median of brokers is typically utilised. All estimates avoid stale forecasts which are removed after a certain number of days.

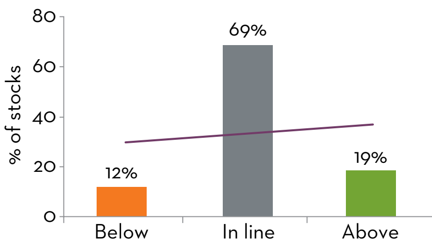
Top-down analytical review

Despite concerns leading in, results largely in line

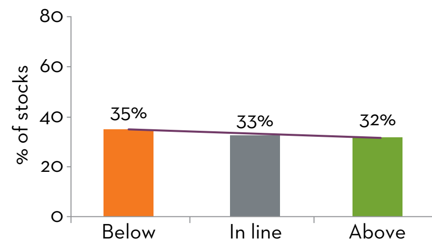
Let us begin our Reporting Season analysis by looking at the market "surprise", or how actual results came in versus broker consensus forecasts. Looking at the market in aggregate, and given the environment we find ourselves in, what has been somewhat startling is how much the results were in-line with these relatively normal lead-in expectations.

The charts below highlight the almost equal split of companies' meeting the lead-in earnings per share (EPS) and dividend per share (DPS) expectations versus those that missed, with just a slight beat on the revenue line. In aggregate we really saw nothing dramatically bad (or good) from headline profits.

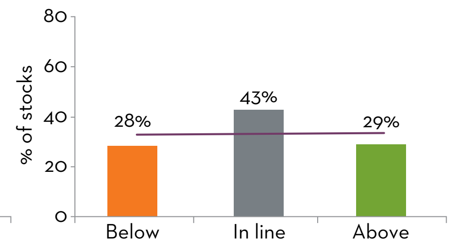
Sales surprise



EPS surprise



DPS surprise

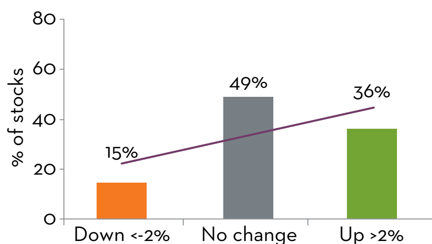


The concerns still impacted broker forecasts

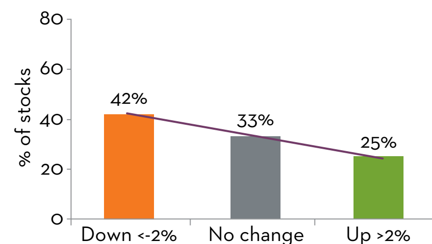
In fact, the key theme of results overall is the lack of volatility across the board, despite how it may feel. We had been looking for material evidence of the interest rate induced recession; however, the actual numbers simply didn't show that.

Having said that, it is not surprising that the broker consensus of forward EPS estimates were downgraded given the management commentary pointing to clouds on the horizon. We did see that more companies received upgrades than downgrades for their sales line given inflation is driving up underlying prices, and the size of sales forecast upgrades reached five-year highs.

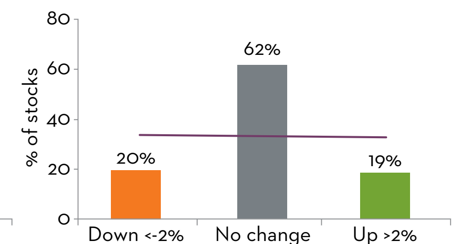
Sales revision



EPS revision



DPS revision



> "Looking at the market in aggregate, and given the environment we find ourselves in, what has been somewhat startling is how much the results were in-line with these relatively normal lead-in expectations."

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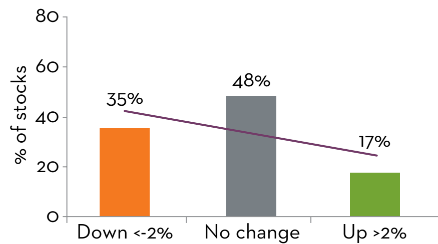
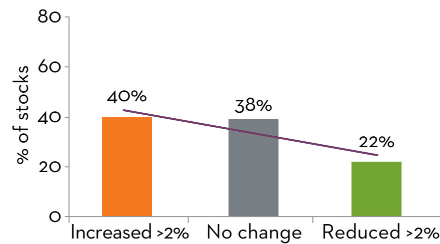
An Inflationary signature across financial statements

The impact of inflation has flowed through to expectations for each main element of company profit and loss (P&L) statements. Despite sales expectations being revised up as mentioned above, profit margins are down as the cost of doing business looks worse into the future. The expected cost of capex to businesses has also been increased due to inflation in energy and commodity prices, and building materials. Weaker cashflows have also translated into higher expected debt levels.

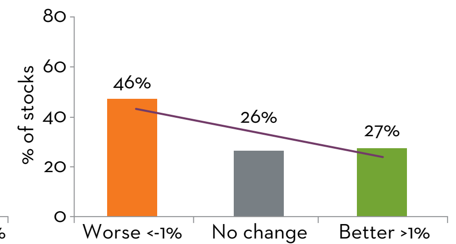
Profit margin revision



Capex revision



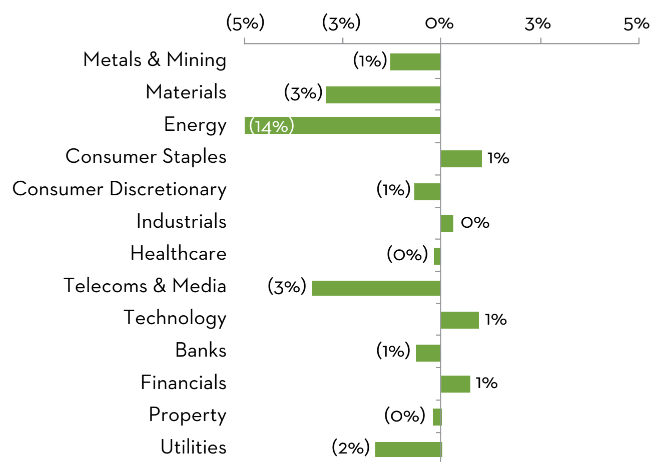
Debt revision



Cyclical sectors more exposed

Breaking this impact down across the sectors, the chart below highlights the cyclical skew to EPS downgrades this reporting season. Forecasts for metals & mining companies were impacted by cost increases and commodity prices coming off. This flowed through to energy stocks too. Materials, in particular building materials, were impacted by cost inflation and the impact of rate rises on housing construction demand. The rest of the market was more neutral, but telcos and media also suffered from the housing thematic, and lower advertising spend. In general, companies more exposed to the global economy also performed worse than those with a purely domestic focus.

Median change in NTM EPS forecasts

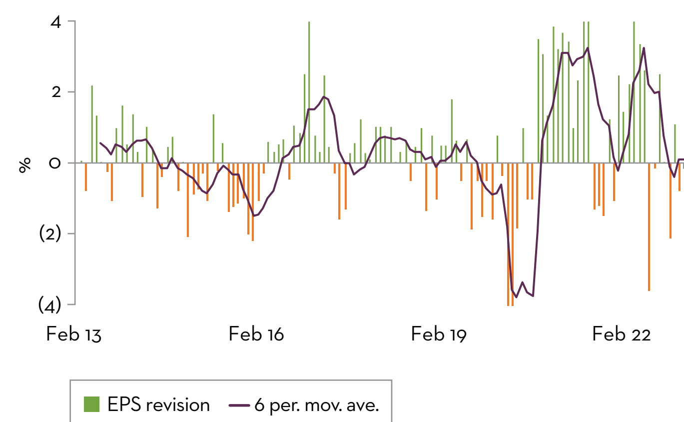


Post-Covid EPS recovery is now fading

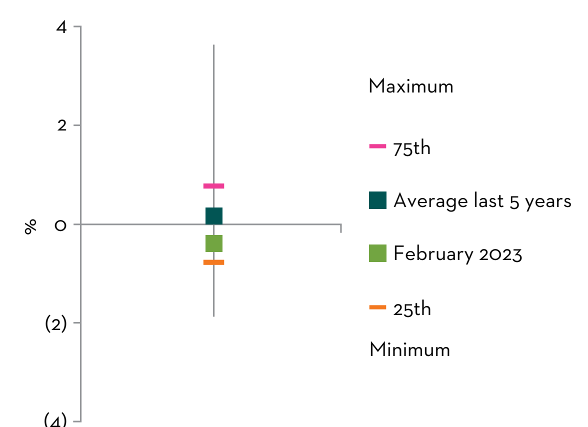
In the following chart we can see that the EPS revision cycle has again been very abrupt when compared to the past 10 years. Unlike the outsized downdraft in March 2020 from lockdowns, which rebounded quickly into upgrades on the back of stimulus and low rates, the recent forecasts for EPS since August 2022 have flip-flopped as markets have struggled to reconcile blow-out inflation readings and the impact of rate rises offset by a surprisingly resilient consumer.

Putting February 2023 into context of reporting seasons over the past five years, the size of the change in EPS forecasts during the month was only marginally more negative than average, much better than August 2022 but weaker than the other more upbeat seasons post-Covid.

Average monthly change in NTM EPS forecasts: last 10 years



Last 5 years

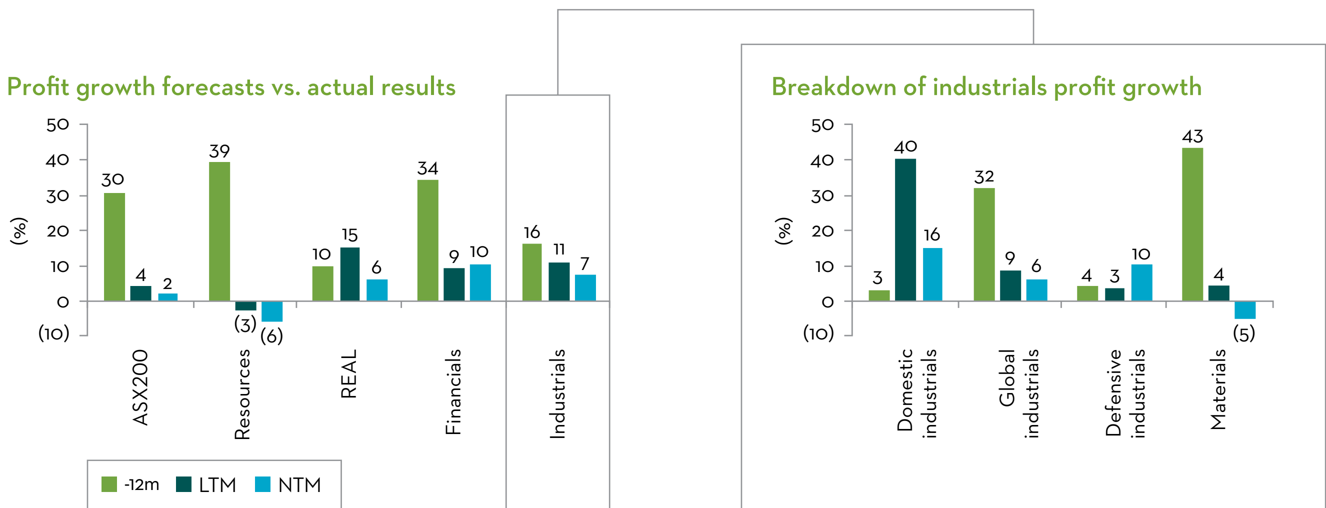


Growth is fading to zero, and we are looking over the edge

Finally, what does this mean for earnings growth? Looking at aggregate EPS forecasts versus the actual aggregate EPS delivered by companies in the recent results, we can see that broker consensus forecasts now have EPS growth at near zero for the next 12 months. To us, this really signals that the market thinks we are coming towards the peak of the earnings cycle.

We would note that there is still a strong contrast for growth outlooks across the sectors, with resources negative on lower expected commodity prices and capex spend, while the rest of the market is still benefiting somewhat from reopening (real assets), reflation (financials). Within the industrials, margin pressures are most prevalent for materials stocks as they too are exposed to commodity prices.

While headline inflation will eventually come down, inflationary impacts will be moving more towards the industrials and services sectors through wages pressure. Labour costs tend to have a lagged impact in inflation due to the time it takes to renegotiate enterprise bargaining agreements (EBAs). Of note is that the EBAs for **Woolworths Group** and **Coles Group**, two of the country's largest employers, are due in June.



Sources and disclaimers this section.

Past performance is not a guide to future returns.

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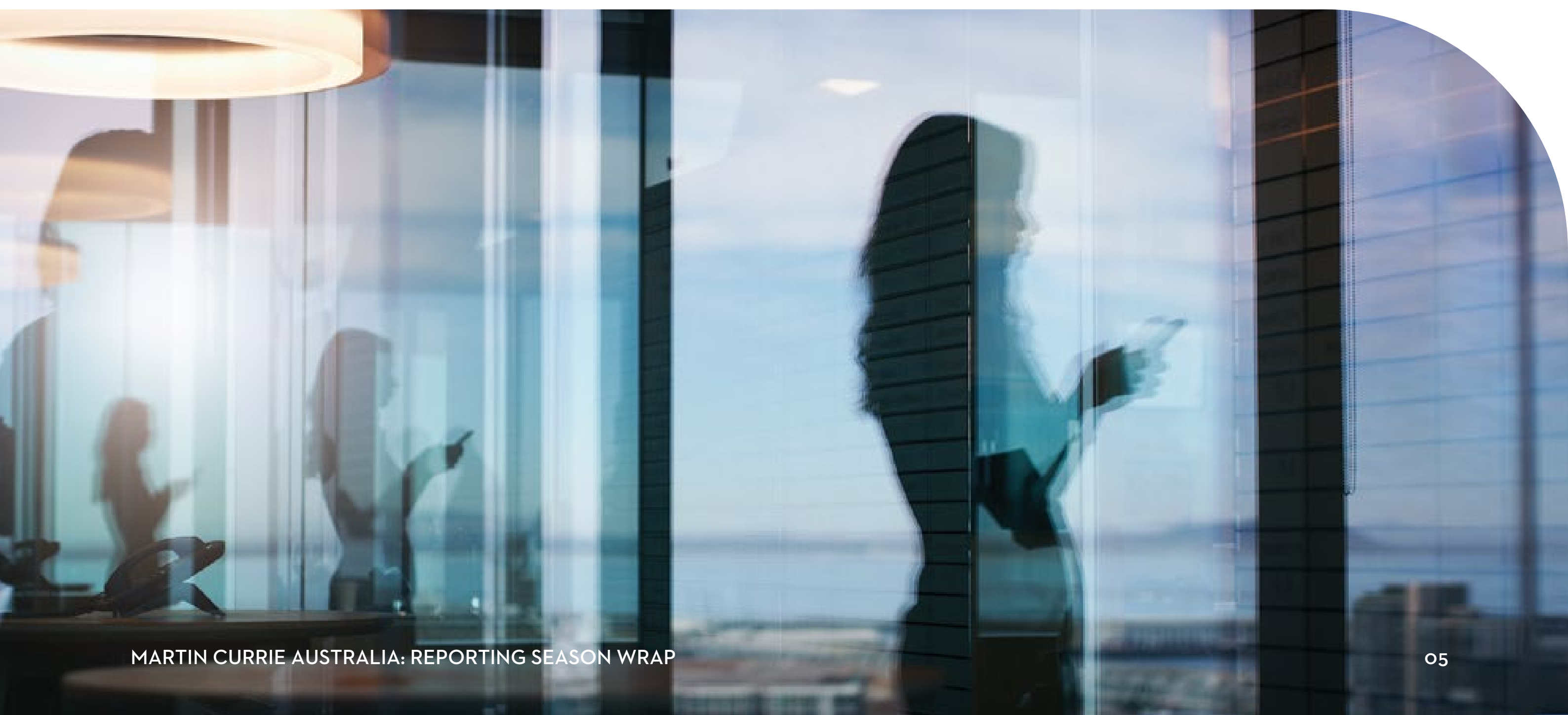
Source for all charts: Martin Currie Australia, FactSet; as of 28 February 2023. Chart data is for the S&P/ASX 200 Index unless noted otherwise. See further definitions on page 2.



Key fundamental themes from reporting season

Insight gained through company interactions

While the analytical and aggregated view of the reporting season's results provides a broader framework to judge what the street is thinking and doing, our fundamental analysis and company engagement of individual stocks allows us to do a deeper dive into the issues and strategies of each business.

Over the four-week reporting period, the MCA investment team conducted 100+ meetings with company management teams following the release of results, and this has helped us to refine our investment views and outlook.

Top positive and negative issues for companies

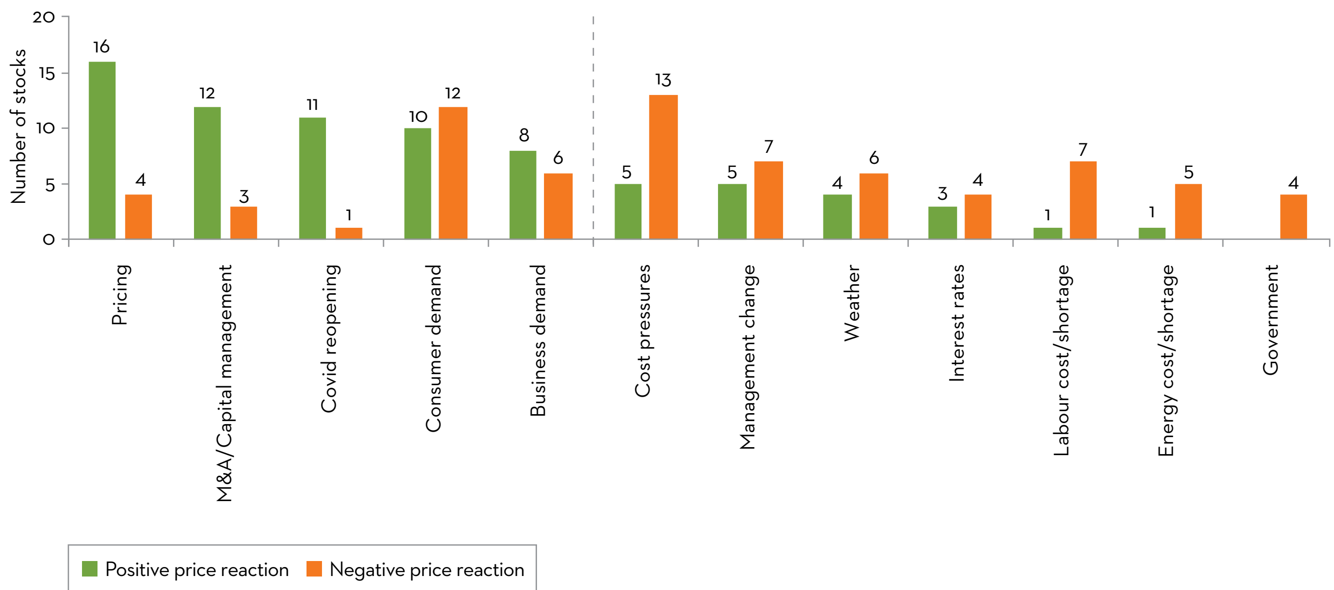
Based on our interactions with company management over the past month, we have categorised what we think are the key themes impacting each company, and tracked whether these themes have had a positive or negative impact on the share price.

While we can make some general assertions about positive and negative themes, we have found that what's helping (or hindering) one company isn't necessarily the same for another, and this often comes down to that company's business strength and quality.

For example, we were able to attribute pricing power, M&A/capital management, Covid reopening, consumer & business demand as a positive impact on the share price for many companies. However, for some companies these themes instead hurt.

On the other side, companies with a negative price reaction following their results could be categorised as facing cost pressures, disruptive management change, impact of adverse weather, higher interest rates, labour & energy shortages and increased government regulatory impacts.

Price reaction by key thematic



Past performance is not a guide to future returns.

Source: Martin Currie Australia, FactSet as of 28 February 2023. Chart data is for the S&P/ASX 200 Index. See further definitions on page 2.

"While we can make some general assertions about positive and negative themes, what we have found is that what's helping (or hindering) one company isn't necessarily the same for another, and this often comes down to that company's business strength and quality."

In the following section we discuss some of the more impactful themes in more detail, and also touch on the key sustainability insights from reporting season.

Inflation, pricing and the impact on profits and cashflows

We are seeing evidence of companies putting through price increases across the board. For example, **Domain Holdings Australia** and **REA Group** told us how they have lifted the price to create a real estate listing. **Telstra Group** and **TPG Telecom** have raised mobile phone prices. **QBE Insurance Group** has put through premium rate rises.

There is a question as to whether some of the price rises are truly inflation-related, or whether the companies are simply profiteering. We believe that, on balance, it is the former and that historical costs and accrual accounting are to blame.

One strong example of this is **Brambles**, a high-quality, market leading pooled pallet provider through its US CHEP business. They reported 13% revenue growth for H1 FY23, with 19% price growth, but negative volumes. At first blush, this looks like profiteering, but when you look deeper at their EBIT and Free Cash Flow margins, you can tell that the cost of making a pallet has actually increased by ~50% and that they have needed to put through price rises to earn a reasonable return from maintaining their existing pallet pool, and to finance continued growth in that pool for the future.

The inflation impact is that one can see accounting profits rise, but the economic cash flow returns are pressured by the higher cash costs on investment unless pricing is increased to compensate. This is the case for Brambles, and we are seeing this play out for many companies in the market.

On the other hand, we are also seeing companies negatively impacted after increasing their prices due to more elastic demand and lack of pricing power. For example, **Domino's Pizza Enterprises** volumes suffered after increasing prices. **Commonwealth Bank of Australia** has also pointed to pressure in new mortgage margins with the higher interest rates.

Chris Schade, CFA
Research Analyst

Brambles' management believes they are well positioned to retain the price increases they have successfully passed on to customers, as competitive conditions are more supportive than at the same point in earlier business cycles. The absence of new entrants or disruptive competitors in the market plus a current short supply of pallets in the market are supporting management's ambition to hold its stance as a disciplined market-leader.

Covid reopening still a tailwind

Travel companies have continued to rebound, and we have seen strong results and commentary from companies such as **Flight Centre Travel Group** and **Auckland International Airport**. This theme isn't just limited to tourism, with shopping centres and companies exposed to increased visitation such as **Vicinity Centres**, **Transurban Group**, **Endeavour Group** (hospitality) all continuing to do well. The supermarket majors **Coles Group** and **Woolworths Group** are also now benefiting from a lack of Covid compliance costs. Visa applications are also starting to tick back up, pointing to improved population growth.

Andrew Chambers, C.A.
Portfolio Manager

Transurban Group's 1H23 results were in-line with expectations with a modest upgrade to dividends per share driven in part by increased confidence in the sustainability of improved traffic volumes, particularly in Sydney and Brisbane. There is scope for further re-opening gains over coming months as lagging Melbourne and US markets regain previous volume results. Higher recent inflation readings will also flow through to boost inflation-linked tolls/rents in coming months.

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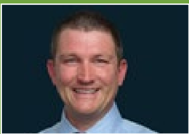
Julia Wang, CFA
Research Analyst

Australian Department of Home Affairs data for student visa applications showed total applications in 2H22 were up 9% over 2H19. Importantly this data is before the impact of China's recent policy change to discourage students from completing online degrees from foreign universities and underscores the potential of a strong tailwind in demand for **IDP Education's** student placement and English language proficiency verification. We met with management at IDP Education and they indicated that, although the number of Chinese students enrolled in Australian universities is still well below the 2019 peak, they are modelling a return to 2019 numbers during 2H24.

M&A and capital management continue growth

We have seen several positive M&A announcements from Australian companies, such as **Flight Centre Travel Group's** deal in the UK premium holidays space. **WiseTech Global** has also acquired a landside logistics company, expanding its total addressable market.

While we did see several companies announce special dividends, from **OZ Minerals**, **Ampol**, **Newcrest Mining**, **The Lotteries Corporation**, and on-market buy-backs from several others, we are seeing caution from other companies who seem to be hoarding cash for the bad times.



Jim Power
Research Analyst

Super Retail Group flagged a cautious stance on capital management following a very strong 1H23 sales growth outcome. Although management did not point to any current evidence of troubling signs for consumer demand, they do expect conditions will become tougher.

Business demand more mixed

We saw evidence of continuing business demand, specifically from the mining cycle and investment in renewables. **Worley** and **Seven Group Holdings** are benefiting from demand on the resources side. **Vicinity Centre** is seeing good re-leasing spreads from retail stores. The banks, in particular **ANZ Group Holdings** and **Virgin Money UK** continue to see positive lending volumes for their businesses side.

On the negative side, IT and communications sectors are seeing slower business demand, impacting the outlooks for companies like **Nine Entertainment Co Holdings**, **News Corporation** and **Megaport**.

Still little sign of full-blown consumer stress

The results from companies such as **JB Hi-Fi** and **Super Retail Group** suggested that the impact of rising interest rates on consumer spending did not have a material impact on holiday season and year-end sales. There are early indications however to suggest a more challenging environment into the new year compared against the very strong growth in the corresponding period last year. Any sales growth will likely come from price rather than volume.

However, housing related stocks such as **Fletcher Building**, and **GWA Group** are already seeing a negative impact and have flagged softer residential renovation activity for FY23. Interestingly, **REA Group** and **Domain Holdings Australia** say that consumers are coming back to auctions, but it's a lack of supply that's an issue for them. This could be an indication that investors are starting to project through to a rates peak or a slowing in the rate of rates changes.

Some companies also talked about a shift in the consumer mindset from "wants" to "needs". The supermarkets have seen evidence of trading down – from aspects such as home delivery to in-house premium products, or premium to the cheaper home brand. This means it hasn't impacted volumes much but has led to lower overall spending.

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At the end of the December quarter, less than 200 basis points of the rate rises had flowed through to variable rates, and 40% of borrowers were still on fixed rate loans in that period. It will be the next results where we see any real impact from the mortgage cliff.

Matthew Davison
Portfolio Manager

Weather as an excuse – 3 bad years in a row

Weather has been a common excuse for poor results so we wanted to delve deeper to understand the relative impact compared to history.

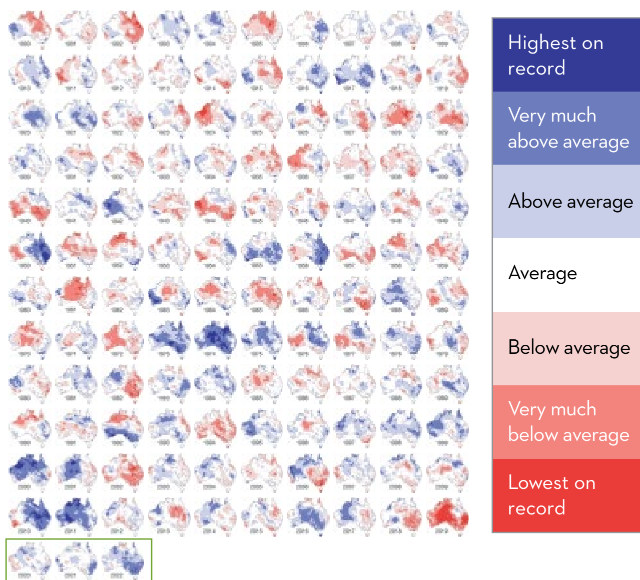
When you compare Australian rainfall data over the last 123 years, it is true that a three-year long La Nina event is unusual. Furthermore, the extremes in the last few years have been felt hardest on the eastern seaboard where the population is concentrated. Contrast this with 2011 or 2016 where the rain fell mostly in central Australia.

These extremes have had an impact on companies such as **Downer EDI**, **Aurizon Holdings**, and the builders. For example, a large part of Downer's business is in road maintenance, which simply can't happen when it is raining. Aurizon won a new contract to move titanium dioxide feedstock mined in NSW to a WA refinery by rail (rather than it being trucked /shipped) but, because of the floods, they haven't been able to start earning revenue, despite costs racking up.

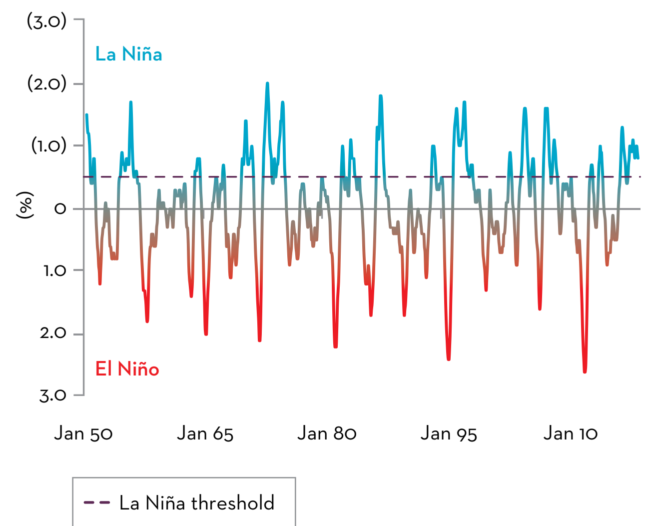
On the flip side, the wet weather has been a positive for agricultural companies like **Nufarm** and **GrainCorp**, and New Zealand utilities **Genesis Energy** and **Mercury NZ** which have benefited from better hydro volumes.

It would be surprising to see another La Nina year, so we do expect weather to have a lesser impact this year and next.

Australian rainfall deciles over past 123 years



Historical El Niño/La Niña episodes (1950-present)



Source: Martin Currie Australia, Commonwealth of Australia, Bureau of Meteorology, NOAA/National Weather Service National Centers for Environmental Prediction; as of 28 February 2023.

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Sustainability themes coming through in results and outlooks

One of the most significant Sustainability themes cited during the results period was the introduction of the US Inflation Reduction Act (IRA) and its heavy emphasis on promoting clean energy investment.

Several Australian companies, such as **Worley**, **South32** and **Incitec Pivot** have talked up the benefits of IRA's US$370bn investment in clean energy and manufacturing. This also shines a light on the lack of equivalent backing from the Australian government which may divert Australian company efforts to the US.

A few of the downstream impacts of the IRA include:

- Separate tax credits can be received for all different stages in producing batteries. Australia will be a significant source of free trade battery materials.
- Green Hydrogen costs will become more competitive and could potentially go negative after tax credits are applied.
- New tax credits will be available for nuclear energy and fossil fuel carbon capture utilisation and storage.
- Domestic content provisions for manufacturing, including mining costs, will be incentivised.

Will Baylis, GAICD
Portfolio Manager

For **Worley**, the IRA opens up new carbon capture projects in addition to one they have underway. **Incitec Pivot** could see funding for carbon capture and blue hydrogen, while **Woodside Energy Group** could for the H2 Oklahoma hydrogen project. **South32** could benefit from funding and accelerated mine approvals for its Hermosa mine.

Several company discussions around clean energy have flagged growing risks from the Government's policy approach. In our view, while gas price caps have generated short-term political capital for the Government, they undermine industry confidence in investment to bolster future gas production. On the back of the likely early retirement of Eraring Power Station, even the Australian Energy Market Operator (AEMO) has forecast a potential shortfall in electricity supply to the demand centres of Sydney and Newcastle from 2025 onwards. We see the risk of such blackouts driving government focus on the need for gas in the future and its role in filling the natural gaps in electricity generation of renewables when wind and sun is not available.

Ashton Reid, CFA, GAICD,
Portfolio Manager, Real Assets

Our recent meeting with gas pipeline owner **APA Group** focused on the critical role of gas in navigating the challenges of the transition to more renewable energy, especially given gas-based generation's ability to respond quickly to peak demand needs when wind and solar are intermittent.

APA Group is prudently investing in select projects to alleviate gas bottlenecks that are at the lower end of its targeted returns in order to avoid reputationally damaging gas shortages and ensure they meet their social license to operate obligations.

A related topic on government policy impacts was the Australian Government's 'Safeguard Mechanism' reform and its efforts in limiting the amount of greenhouse gases than can be emitted from Australia's largest industrial facilities. This looks like it will likely impact the Australian production capabilities of companies such as **BlueScope Steel** and **Boral**.

Finally, a sustainability topic that seems to have been unfortunately exacerbated by the current environment is safety issues. Several companies we have spoken to cited that the loss of experienced managers during Covid has impacted production capabilities in mining and heavy industries, and this has also contributed to poor safety outcomes including site fatalities.

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Big picture outlook for equities and portfolios

So what does all of this mean for investors in Australia equities, partiuclarly across the Value, Income and Sustainabilty style spectrum that we work in.

Value style stocks still cheap

The dispersion between the Price to Earnings (P/E) ratio of the Australian and global Growth and Value style indices continues to remain in the bubble territory created by the low-rate environment since the GFC that rewarded unprofitable companies generating no free cash flows.

The dispersion has contracted significantly since March 2020 with the effects of post-Covid stimulus beginning to wane and the impact of rising inflation and interest rates suppressing Growth P/Es. Yet the spreads between Growth and Value indices, both Australian and global, remain elevated by historical standards.

As the world continues to normalise on rates and long-term inflation expectations, we believe that it is very important to avoid the expensive stocks that have further to fall. These conditions continue to provide a clearer tailwind for the Value style. Value stocks are still far cheaper today relative to history. As these extremes will inevitably unwind, the Valuation starting point for excess returns to Value investing is strong for the next decade.

We would note that recent strong returns for Value will also continue to pressure those investors who had moved to underweight Value strategies to reassess their asset allocations, potentially redirecting flows back toward Value managers.

MSCI World: Next twelve month P/E ratio

MSCI Australia: Next twelve month P/E ratio

Past performance is not a guide to future returns.

Source: Martin Currie Australia, FactSet; as of 15 December 2022.

Positioning for Value opportunities, and the cycle

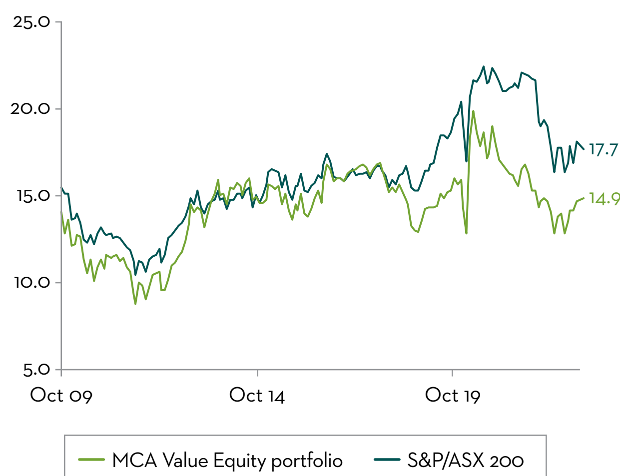
Looking more closely at how we are positioning our Value-style portfolios, we would note that what Value looked like in the low-rate environment between the GFC and Covid is different to the immediate post-Covid period and today.

In the post-GFC years, as a Value manager we were happy to be more cyclically exposed and higher beta as that was where the value was. And back in April 2020 we were looking for opportunities that were dislocated by the Covid lockdowns.

In today's environment of slowing earnings, we are now much more defensive in our positioning, avoiding those consumer discretionary sectors that will be impacted by contraction in household budgets and targeting companies with strong balance sheets and robust cash flows that can withstand any capital funding headwinds which may emerge following the SVB demise.

Portfolio Beta

Next twelve month P/E ratio



Past performance is not a guide to future returns.

Source: Martin Currie; as of 31 December 2022. Data presented for the Martin Currie Australia Value Equity representative account.

We are finding much better valuation opportunities in companies like **Worley**, **Aurizon Holdings**, **QBE Insurance Group**, **Medibank Private**, **ANZ Holdings Group** and **Brambles**.

Michael Slack
Head of Research

Sustainability through a style lens

We have found that Sustainability funds available in the Australian market are often more exposed to Growth-style and smaller cap companies than the market index. Typical Growth sectors such as technology have low- or no carbon emissions and therefore rank favourably on metrics favoured by the market. On the other hand, many Sustainability funds simply exclude carbon-emitting energy companies, manufacturers and utilities, which are representative of sectors that are more often considered Value-style.

Our Sustainable Equity strategy is one of the few Value-style tilted Sustainability strategies in the Australian market. Given the current environment, this is important for two reasons:

- Avoiding certain sectors and being positioned in a more Growth-style portfolio can leave investors exposed to a style bias that we believe may soon unwind as per the discussion in the sections above.
- To facilitate real change and improve the future, we need to have a seat at the table in these types of sectors as active owners. Excluding sectors that are 'bad' and only investing in sectors that are already 'good' takes away the opportunity to work with companies to move them towards more sustainable practices, and also benefit financially from that shift.

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For income, results show importance of quality

One thing that stood out in company results was the stark difference between the high quality, more defensive names versus those with lower quality.

This is what we would expect to see at a slowing point in the cycle. Companies with lower barriers to entry, less pricing power have more vulnerability and are more likely to suffer in a downturn.

For us, quality is a key measure of risk from the perspective of the portfolios that we manage for income-focussed investors. High-quality companies that have solid earnings are more likely to be able to sustain higher dividends, grow income distributions to match rises in the cost of living, and be less volatile than the wider equity market.

We do not think we have seen the worst of it yet, so a focus on fundamental quality at this point in the cycle is very important.

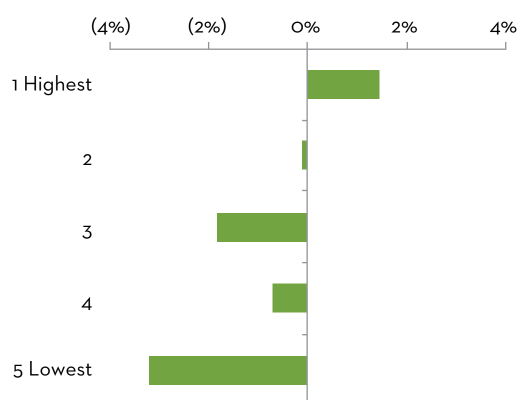
Regarding dividend payout ratios

Interestingly, we did see that broker expectations for dividends were relatively resilient during the reporting season, seeing upgrades even though EPS forecasts were down.

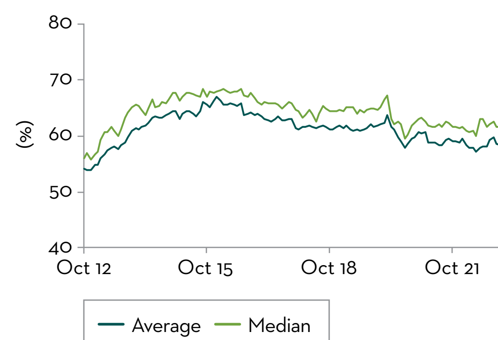
We note that Australian company payout ratios are still very low compared to history, having continually fallen for the last seven years. This is despite the ongoing strength of Australian company balance sheets and debt levels, which fell significantly during Covid. This current low level of payout ratio means that there is ample capacity to sustain dividends and for the companies with stronger balance sheets, capacity to grow dividends. As we work through the cycle of peak rates, we expect dividends to resume their growth trajectory again.

Inflationary stress on working capital and capex will likely have a greater impact on the lower quality, more capital-intensive companies. For our income portfolios, we are looking for companies that can support fundamentally higher payout ratios over time.

Reporting score by Analyst quality (average)



S&P/ASX 200 pay out ratio



Past performance is not a guide to future returns.

Source: Martin Currie Australia, FactSet as of 28 February 2023. Chart data is for the S&P/ASX 200 Index. See further definitions on page 2.

Capital management choices reflect rule changes

Franking is of course very important to many Australian shareholders, and given recent government changes around the treatment of off-market buy backs, the preferred method to return capital to shareholders is now becoming special dividends. We saw this from several companies during reporting season, and no new off market buys back.

Patrick Potts
Research Analyst

The changes announced remove the differences between on- and off-market buybacks in terms of the tax treatment. Off-market buybacks will no longer be able to distribute a franked dividend as part of the compensation to shareholders and the CGT liability will likely be similar between on- and off-market buybacks. Hence the Government forecast to recoup a significant level of forgone tax revenue from the changes.

Read more about the change the legislation in my recent ***article***.

We see this new focus on special dividends as a positive for shareholders seeking to maximise dividend income, as investors can receive the full value of the dividend and franking without any associated capital losses.

Summary

The February company reporting season has shown us that while a consumer slowdown is starting to occur, the consumer is still showing resilience in spending and company revenues remain strong.

Inflation pressure is showing through in the cost line, but wage inflation is still to come through. The unfortunate message from company results is that interest rates will likely need to go higher to really nip inflation in the bud.

Expected earnings growth for the next twelve-months is now closer to zero, but there is still a strong contrast across the sectors. The potential uncertainty of capital funding availability for companies with lower quality balance sheets in the wake of the SVB collapse will bring added uncertainty.

So, the question remains, are we looking over the edge of an earnings recession, a real GDP recession, or both?

Whatever flavour of recession arrives, we have been positioning our portfolios for this outcome for quite a period of time, lowering the beta of our portfolios, and focussing on companies that can grow earnings and dividends in the higher rate environment and not be exposed to valuation risk.

We continually adjust our portfolios based on the information we are getting from sources, which include reporting season results, company meetings and engagements. These are all a valuable opportunity to gain deeper insight and hone our investment thesis for each company.

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- Investing in foreign markets introduces a risk where adverse movements in currency exchange rates could result in a decrease in the value of your investment.
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- Smaller companies may be riskier and their shares may be less liquid than larger companies, meaning that their share price may be more volatile.
- The strategies mentioned may invest in derivatives (index futures) to obtain, increase or reduce exposure to underlying assets. The use of derivatives may restrict potential gains and may result in greater fluctuations of returns for the portfolio. Certain types of derivatives may become difficult to purchase or sell in such market conditions.
- Income strategy charges are deducted from capital. Because of this, the level of income may be higher but the growth potential of the capital value of the investment may be reduced.

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