Providence
Independent Investment Advisory

Activity Report

June 2019 - August 2019

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About this Report

Information Only, No Action Required

As part of our ongoing commitment to being a trusted partner for our clients, Providence reviews a number of products each month, searching for investment opportunities that fit our clients' individual requirements. Being an independent company, each opportunity is assessed solely on its merits regarding risk and return.

True to Providence's promise of transparency and independent analysis, we share the basis of our decisions with our clients in this Activity Report.

Acceptances

1. Mandala Clarion Hotel Fund

1. Mandala Clarion Hotel Fund

Located 6.4km north-east of the Mackay CBD, the Clarion Hotel is a 4.5-star 79-room hotel complex, sitting in the Mackay Marina Complex. The asset has all the normal hotel amenities - 2 function rooms, gym, pool, restaurant, 50 car parks - but it is fair to say that there have been minimal capital improvements made since its completion. As an investment there are two clear areas to consider, and with that in mind the below has been split into a review of both the operating business, and the underlying asset value within the larger site area.

The hotel was purchased for $9.2m which is considerably less than replacement value of $24.5m. The manager has shown strong ability for "turn arounds" of hotels in previous funds, which was evident in our due diligence in terms of improving the hotel operating business. Outside of the P&L though and following our site visit of the hotel and its facilities, we see ample value attached to the site, along with several operational areas which after discussion with Mandala and following the site visit we see significant scope for improvement. We have participated for selected clients depending on the appropriateness for portfolio's and level of illiquid assets being held.

Declines

1. Fortius Central Park
2. Argus Property Partners – Health Hub Morayfield
3. Stirling Capital – Office Property Syndicate
4. Bridge Multi-Family Real Estate Fund IV
5. Gresham Royalties Fund

1. Fortius Central Park

Although we have a high level of confidence in the fund manager, we are not looking to add to our retail exposure in property at this stage of the cycle.

2. Argus Property Partners – Health Hub Morayfield

We reviewed a closed end single asset trust which would invest in an integrated healthcare facility located in Morayfield Queensland. Given our current exposure to direct property and existing exposure to healthcare, coupled with not having a relationship with the manager, we have declined participating in this fund.

3. Stirling Capital – Office Property Syndicate

We do not currently have a relationship with the underlying fund manager, and significant time would be required to establish one. We have our preferred panel of property advisers, built up over our 20 years of investing. Our current weighting to direct property is quite full and we are keeping our powder dry.

4. Bridge Multi-Family Real Estate Fund IV

We met with Dan Stranger from Bridge Investment Group regarding their US Multi Family Real Estate Fund. We believe the projected returns from multi-family real estate in the US are attractive and have shown resilient qualities over the long term, with lower volatility relative to equity risk given the operating yield providing income. However, investing in global direct property requires considerably more due diligence given the lock up period involved, investing in illiquid assets offshore, in addition to product structuring risk (e.g. tax) and currency risk.

5. Gresham Royalties Fund

We met with James Morrison from Gresham to discuss their new Royalties Fund. We are unable to make comment on the fund due to confidentiality terms, however we have declined participation as we have existing exposure to royalties within client portfolios.

Presentations

1. Sage Capital
2. Delft Partners - Global Listed Infrastructure
3. Ausbil - 130/30 Focus Fund
4. Causeway - Private Debt Fund
5. Antler - Early Stage Venture Capital
6. Partners Group - Private Loans Fund
7. Legg Mason Western Asset – Macro Opportunities Bond Fund
8. Trinetra – EM Growth Fund
9. Pimco Solutions
10. Ausbil – Global Essential Infrastructure Fund
11. Media/Tech Fund ACT (audience, content, technology)
12. BCA's Monthly Summary
13. Schroders Fixed Income presentation
14. BCA Global Asset Allocation
15. JP Morgan 3rd Quarter Update
16. JP Morgan Strategy Session in July "The Asian Century"
17. BCA Geopolitics Webcast
18. Schroders Update Session - Macro, Equities and Fixed Income
19. Providence Education Series

1. Sage Capital

We met with Sage Capital portfolio manager Sean Fenton, to discuss their proposed funds – an equity long short fund and a market neutral fund. For over ten years, Sean previously managed funds successfully for Tribeca Alpha Plus fund with a strong track record. We believe the previous fund's track record in terms of manager alpha would be transferable as the previous staff and quant/qualitative processes remained consistent. At the time of our review, the business has not started operating so we will review the funds again once the products are finalised.

2. Delft Partners - Global Listed Infrastructure

Robert Swift, portfolio manager from Delft Partners presented their Global Listed Infrastructure Fund. The strategy seeks growth and income by diversified investments across global listed infrastructure companies. The fund has performed strongly - 17.1% p.a. since inception in Dec 2016, albeit with a short track record. With interest rates being supressed by Central Banks globally, steady income producing strategies such as infrastructure or property have performed strongly with investors seeking positive yield above nominal government bond rates. We are in process of reviewing several infrastructure and other alternative strategies on behalf of our clients.

3. Ausbil - 130/30 Focus Fund

Gian Pandit (portfolio manager) provided us with an update on the Ausbil 130/30 Focus Fund. The fund is an active extension, long short manager, that can use shorts from less preferred domestic stocks to fund additional long exposure on their preferred stocks. The fund benefits from macroeconomic analysis in addition to strong analyst coverage and ESG capability from Ausbil. The fund has delivered strong returns (e.g. 9.2% for 1 year, 14.2% p.a. for 3 years and 10.3% p.a. over 5 years). We like that the fund is able to use shorts in down markets and ability to raise cash to 20% to dial down equity risk. Gian believes it is one of the most difficult times to invest; when companies are priced at elevated levels and the coming reporting season requires earnings to meet/beat consensus estimates.

4. Causeway - Private Debt Fund

We met with portfolio managers Tim Martin and Mike Davis from Causeway Partners to discuss their new Private Debt Income Fund which commenced in December 2018. The manager has previously run several iterations of private debt since 2003, over three separate funds which have each performed well despite going through the GFC. The new fund will predominantly be invested in senior secured loans, high up the capital structure, with preference for short term loans. With RBA cutting rates to 1%, investments with yield become more attractive to investors provided that the risk being taken is understood, which in this case includes default rates, recovery assumptions, structuring of loans, diversification etc. We are currently in due diligence phase of this very new fund.

5. Antler - Early Stage Venture Capital

Anthony Millet from Antler met with us regarding an early stage venture capital fund. We like that the fund will be highly diversified with a strong Investment Committee and due diligence process to bring together new businesses. The segment of pre-venture capital has not been an investible market as there has not been financial products to provide capital to early stage businesses and the higher degree of risk for investors. We believe the process of the new Antler fund is different in addressing the issues of pre-venture capital – namely diversification, funding and strong due diligence of business models. We are currently in due diligence phase regarding the investment process, structure of the fund, expected returns, risk and people involved.

6. Partners Group - Private Loans Fund

We met with Partners Group co-founder Urs Wietlisbach regarding their Private Loans fund expected to list on the ASX as a Listed Investment Trust later this year. We commend the manager for providing retail investors ability to access diversified global private loans, which has been traditionally available only to wholesale and institutional investors. The product is targeting to return RBA cash + 4%, by investing in primarily senior secured loans (first lien) and a small allocation to subordinated debt and special situations. One of the benefits of Partners Group listing this vehicle is their size, managing $118bn in AUM with $24bn towards private debt investments, which leverages their existing capability to manage this product. We are internally reviewing the product relative to other Private Debt opportunities.

7. Legg Mason Western Asset – Macro Opportunities Bond Fund

We met with Jon Baird, Portfolio Manager of the Western Asset Macro Opportunities Bond Fund. The fund aims to maximise returns within a volatility budget of 10% by employing a macroeconomic trading strategy to implement a concentrated and opportunistic portfolio of exposures. The manager tends to employ a long-term fundamental value approach to portfolio construction within predominantly fixed income securities. The mandate has fairly wide risk parameters associated with duration and the securities that it can invest in. We are continuing our review of this product relative to a number of other fixed income opportunities that we have seen recently.

8. Trinetra – Emerging Markets Growth Fund

We met with Tassos Stassopoulos, Portfolio Manager of the Trinetra Emerging Markets Growth Fund. Trinetra have recently launched an Australian Unit Trust that will initially be a 'feeder fund' into the Trinetra EM Growth UCITS ICAV. We believe the research approach, risk management and portfolio construction of the portfolio is of a very high calibre, however we are unlikely to allocate to emerging markets at this stage of the cycle. We will continue to monitor Trinetra as it builds its presence in Australia and develops a longer-term track record for the Australian Unit Trust.

9. Pimco Solutions

Providence met with Pimco Solutions to discuss their risk management platform and framework. Discussions are early stage and ongoing regarding a quarterly review to help identify risks within client portfolios. At this stage, we are impressed by their capacity to decompose return into various risk factor exposures and identify those factors that have helped diversify risk historically. We will continue to run this analysis on a quarterly basis to provide input into Investment Committee meetings and inform asset allocation decisions.

10. Ausbil - Global Essential Infrastructure Fund

Tim Humphreys, Jonathan Reyes and Natasha Thomas from the Ausbil Global Essential Infrastructure Fund team met with Providence. As the name suggests, the fund is focused on essential infrastructure that tends to provide stable cashflows through the economic cycle. We were impressed by the team and the robust process behind investment decisions. Whilst we agree that their defined universe of essential infrastructure tend to have compelling characteristics, we raised questions around the reduction in the investable universe. Our due diligence continues with the team as we look to find consistent return streams for portfolios.

11. Media/Tech Fund ACT (audience, content, technology)

This is a new fund and concept - looking to invest and access new and emerging media interests with an aim to deliver uncorrelated returns. Fund 1 is seeking to raise $10m and to make 8-10 investments. The fund's objective is to be media centric, global, stage agnostic and has an investor-first approach. The managers of the fund intend to only invest in companies whereby they can take an 'active management' role. The focus will be on early stage investments. Target returns are ~25% IRR with an investment horizon of ~5 years from the end of the overall investment period (likely lock up therefore ~7 years). While the managers appear well-versed and experienced in this space (all with deep media/content/platform industry knowledge), as an essentially 'new' fund, it is too early and too small scale for us to invest in. It remains an interesting and concentrated space and we will monitor the progress of the manager and the original fund.

12. BCA's Monthly Summary

The BCA message continues to signal the belief that global inflation will continue to slow, which will allow for the continuance of an easing monetary policy stance by central banks. With advanced economies having an average core inflation level of ~1.5% the recent global economic slow-down is likely to continue for a time and exert downward pressure on prices. They do, however, see a prospect for an improvement in global growth in the second half of 2019 driven by the following:

- widening fiscal deficits
- easing of Chinese credit trends
- and an improvement in US consumers real income levels.

They see this growth being assisted by a continuation of an easing in both fiscal and monetary policy and some already improving signs of global liquidity conditions. They also noted that if global growth does pick up, the US FED is unlikely to cut rates by the ~90bps (at the time) implied by the current market pricing of the Fed Funds Futures rate. They see a window for owning stocks remaining open for 9 - 12 months but noted an expectation of an elevated level of 'churn' in the next 3 – 6 months. They noted the risk of a sharp but temporary correction is elevated at present.

13. Schroders Fixed Income Presentation

This presentation highlighted a scenario whereby bond returns in a recessionary environment or lowering yields made an ongoing investment in bonds attractive on the belief that official interest rates will move lower (as in Australia for example). The rational was that by being exposed to government bonds, an investor would participate in both income generation and capital appreciation as bond values would rise, reflecting a falling interest rate environment. Whilst acknowledging the likelihood that Australia's official interest rates appear to be headed lower, Schroders noted that recent stimulus measures in Australia are yet to fully play out. They also highlighted the following measures to reflect upon: $7.5bn of tax cuts (Schroder's suggested this is equivalent to ~50bps of easing), 50bps of official interest rate cuts and APRA's easing of loan conditions.

14. BCA Global Asset Allocation

We attended a webcast hosted by Garry Evans, Chief Global Asset Allocation Strategist. BCA believe the current scenario in the US is akin to 1998, thus the FED cut perhaps once (soon) but not by 4 times as is currently priced by the market to occur over the next 12mths. BCA feel that global government bond yields have probably hit the bottom or are close to it. Do they see upside in US equities at this point? Upside from here is somewhat limited, as a lot of multiple expansion already has occurred. They remain mindful of the potential of an increase in Chinese stimulus and the implications this would have for global equities (another upward pulse). BCA have recently become more positive on Australian equities and have, as a result, increased their Australian equities weighting to neutral as a hedge against China reflation. BCA are still of the view that a pick-up in global activity in H2 is likely. They also noted that a bottoming of the global cycle will/ would see an end to the USD appreciation.

15. JP Morgan 3rd Quarter update

JP Morgan see the current environment as a time for a bit of de-risking. They are of the view that yields have probably fallen a bit too far for now and may increase slightly. A 'worry' point for JP Morgan at present is the prospect of political error and the implications this may have for markets overall. JP Morgan expect one or two 'insurance' rate cuts in USA, which is fewer cuts than currently priced by the market. With regards to the RBA and Australia, they are expecting a likely pause in any further rate cuts for now as the RBA will wish to 'see what happens'… however downside bias for RBA remains. JP Morgan remarked that investors are paying up for income and they caution this approach as they still see scope for an Australian equities correction in the short to medium term.

More broadly with regards to the global economy, they noted that weakness appears to be contained at the manufacturing PMI level (a view shared by many economists). As a result, this is likely to see sub-trend growth but not a recession any time soon. There remains some pillars of support, few signs of imbalances generally and households are healthy so US economy can continue ticking over. While inflation remains low, it is not disinflationary and central banks can remain accommodative and do not have to worry about inflationary consequences at this stage.

16. JP Morgan Strategy Session in July "The Asian Century"

JP Morgan highlighted the changing investor landscape for China i.e. via the MSCI Indices China has moved from being essentially 'non investible' to becoming the largest investible component within Asia over the last 20 years. China has now overtaken the USA in terms of the number of listed companies, hence, the investor opportunity landscape regarding China has fundamentally changed. JP Morgan highlighted the importance of having an investment exposure in China to the industries where people spend more money as the Chinese society becomes more affluent; consumption, healthcare, technology and automation. JP Morgan noted the 'opening up' of the A-Shares (Chinese companies listed on the Chinese exchange rather than via the Hong Kong exchange) market which has created opportunities to invest directly in businesses that will benefit from China's growth. JP Morgan noted the importance of being exposed to the businesses that sell directly to the Chinese consumer. By only concentrating investment towards China via H-shares, investors only access the largest state-owned/government owned companies with Chinese exposure, not the entrepreneurial companies that are now listed on the A-Share index.

17. BCA Geopolitics Webcast

We attended a BCA webcast hosted by Matt Gertken (Geopolitical Strategist), Marko Papic (Consulting Editor), Roukaya Ibrahim (Editor/Strategist) and Mathieu Savary (Chief Strategist). The BCA house view is that the business cycle will extend, and bond yields will rise, thus the best position is to remain in equities. BCA do however expect increased volatility re: policy uncertainty over the European summer as liquidity will likely be lower. In the short to medium term, BCA see three negative catalysts:

1. China has not retaliated yet to the blacklisting of Huawei and five other Chinese tech companies
2. Trump imposes tariffs on the remaining ~$300bn of Chinese imports to the USA
3. The USA has not yet taken action on point 1 above, as yet.

Possible positive catalysts that BCA can identify include Chinese stimulus and the bottoming of the credit impulse (which if sustained will be favourable for Chinese and global growth in H2). So far China has managed to calibrate enough stimulus to offset tariffs. BCA also noted the prospect of a more aggressive Chinese stimulus if tariff talks break down. BCA appear to be far more focused on the USD now and note that the movement of the dollar is now key to monitor. Their view is that if the USD stabilises and slows it will likely aid H2 global rebound. They also cautioned that if the USD continued to rise then “all bets are off” and any global recovery is at risk.

18. Schroders Update Session - Macro, Equities and Fixed Income

Regarding the Australian equities market Schroders noted the Japanese bid for Dulux (recent international lead M&A in Australia with Nippon bidding for the listed Australian paint producer). In a low returning global investment environment, the Japanese bid indicated that they are happy to accept say a ~5% return (vs. say 7% return being achieved for shareholders pre-bid). Why so? Yield is becoming an increasingly scarce resource. Dulux is viewed by Schroders (and the Japanese it would appear) as a sustainable business with no need for fundamental changes to the business to continue to achieve that ~5% return (at the bid price). Schroders remarked that this ~5% return for Dulux (at the bid price) is a lot better than other options in such a low interest rate environment.

With regards to the broader Australian share market, they highlighted that Australian 10yr bonds at ~1.8% implies a PE (price/earnings) multiple of ~50x for the bond market as at today. In their view, this helps put things into context when you are paying ~18-20x for equities. Schroders, being more of a ‘value’ style manager, note that investors in equities are far more focused on non-yield (i.e IT/Tech) stocks at present. They noted for comparison, IT stocks are trading on earnings yields of ~2.7%. This compares to an earnings yield of ~10.5% for Financials, ~9.8% for Materials and 9.7% for Consumer services. Hence, Schroders are focused on where they believe there is sustainable yield.

The Schroders Global Equities presentation again focused on the value/growth argument and Schroders note that more than 90% of all global investment managers have a current bias to growth. Their overall message was that they saw the December market reactions as a warning sign and are positioned accordingly (cautiously). The Schroders Global Funds top 3 holdings are Anglo American, Standard Chartered and South32 which plays into the remark above about where they see value. They also see value in the UK at a country exposure level and are now underweight the USA from a global position.

The Schroders Absolute Return and Fixed Income presentation highlighted Japan being cheap relative to history. Schroders are attracted to Japan as they see potential for corporate governance reform possibly leading to a release of value within Japanese corporates. In the UK they see some deep value hiding in some of the “mega caps”. They also noted their view that in the UK, small/mid cap single product companies who are not well capitalised will likely be the biggest Brexit losers. With regards to Australian listed Hybrids, they see them as expensive and noted the pending Federal election may bring some pricing volatility as hybrid could be re-priced in a non-franking credit environment.

19. Providence Education Series

We hosted Providence Education sessions in Melbourne on *Concepts of Investment Management*, *Asset Allocation and Portfolio Construction* and U*nderstanding Equites (shares).* We are committed to assisting younger adults and others who would like more investment knowledge. Our next educations sessions are to be held in Sydney and Melbourne. Please let us know if you or a family member would be interested to attend.

Appendix 1: Providence Investment Committee

Steven Crane

Steven has over forty years of investment experience having started in financial markets in the early 1970's. He has held such positions as Senior Portfolio Manager and member of the Asset Allocation Committee at AMP. For seven years he was the Chief Executive of ABN Amro. Steve currently holds a number of board positions, including Chairman of nib holdings limited, Director of Australian Pipeline Limited, Chairman of the Taronga Conservation Society Australia and Chairman of Global Valve Technology Pty Limited.

Chris Grubb

Chris has held senior fund management and broking positions within the Jardine Fleming Group in Japan, Hong Kong and Singapore. He was also a Director of Jardine Fleming Ord Minnett and Chairman of Investor's Mutual and Investor Web and is currently a Director of several Asian-focused investment funds. He also chairs Boardroom Australia and is a Director of Boardroom Limited in Singapore. Chris also acts as an executive coach.

Stephen Roberts

Stephen has over 40 years of experience as an economist and financial markets strategist in banking, broking and funds management. He has worked as Chief Economist with Equitilink and UBS. He worked on the Secretariat of the Australian Financial System Inquiry (Campbell Committee) in 1980, helping draft recommendations that led to the deregulation of the Australian financial system. He is an honours graduate in Monetary Economics from the London School of Economics.

Peter Hooker

Peter has held such positions as an Industrial Analyst at BZW Australia (now ABN Amro), Director reporting to Head of Research, was on the Equities Executive Committee and Director and Head of Industrial Research. He has a B.Sc. in Chemistry, B.E. in Chemical and Materials Engineering, and Graduate Diploma in Finance and Investment. He has over 25 years of experience in investment markets.

Jonathan Pain

Jonathan has 30 years of international investment experience. He has held such positions as Chief Investment Strategist of HFA Asset Management, Chief Investment Officer of Rothschild Australia Asset Management, Head of Investments at Gulf International Bank in Bahrain and Chair of the International Asset Allocation Committee at Paribas Asset Management in London. He holds a joint honours degree in Economics and Politics from Keele University and a Masters degree in the Economics of Finance and Investment from Exeter University.

Ian Wenham

Ian has over 30 years of experience in equity research, investment strategy and portfolio management. He has held such positions as Equity Analyst with Meares and Philips and Research Director of BZW Australia covering equity strategy and industrial research. He was also Regional Research Director with BZW Asia and Director of Asian Research at Lehman Brothers Asia where he chaired the Investment Policy Committee and was the firm's supervisory Analyst for the Asia-Pacific Region. He has also managed strategic global equity investments for the Lowy Family Private Fund. He currently heads his own investment firm.

Richard Nicholas

Richard has over 30 years of experience in private client portfolio management in London, Hong Kong and Australia. Richard started his career with Deloittes in London before cutting his investment teeth with the Rothschild family. He was the founding Research Director at S&P Fund Research UK and Investment Director at Hill Samuel Pacific in Hong Kong. He has also held senior positions with Hambros Pacific in Hong Kong, Alliance Capital in Asia and ANZ Private Bank. He is currently Director at Peak Investment Partners.

Marc Wait

Marc has over twenty years of investment experience. he began his career in Sydney with HSBC and Citigroup Global Asset Management (CGAM) managing Fixed Income and Money Market portfolios. Marc has also held positions in London with CGAM as a Fixed Income Portfolio Manager and Fidelity International where he was the Group Leader, Short Dated Bonds and chaired the Fixed Income Asset Allocation meetings for the firm. Marc was subsequently the Head of Treasury at the Abu Dhabi Investment Authority. Marc has a B.Agr.Ec(Honours) from the University of Sydney and is a Chartered Financial Analyst.

Grant Patterson

Grant has over 30 years of experience in equity markets. Prior to forming Providence he was a Director of ABN Amro and Head of Retail Broking. He has also held other senior positions such as Senior Institutional Dealer, Head of the Sydney Institutional Dealing Desk and also Head of Corporate Liaison. Grant is currently an Ambassador of the ASX Refinitiv Charity Foundation.

Michael Ogg

Michael has over 20 years of experience in investments, starting his career at JPMorgan Investment Management in London in the early 90s. In Australia, Michael worked for AMP Asset Management holding senior roles in Institutional Equities and for Deutsche Bank as a Client Advisor in Private Banking. Michael has an MA (Honours) Economics from Aberdeen University.

Stephen Christie

Steve has over 20 years of investment and finance experience, including as Director and Head of Private Wealth for Ord Minnett, Chairman of the Ord Minnett Investment Committee and Head of Asset Allocation for Goldman Sachs JBWere Private Wealth Management. Steve holds a PhD in Applied Finance and is a Trustee Director and Chairman of the Investment Committee of major industry super fund QSuper.

James Smith

James has over 20 years of investment market experience (cash equities). Prior to joining Providence, he held the position of Deputy Head of Domestic Sales at CIMB Securities (Australia) and was a member of the CIMB Equities (Australia) Management Committee. He has also held positions as Director - Sales at RBS, ABN AMRO and Sales at Deutsche Bank. James was responsible for Melbourne Sales/Account management in his previous roles over the last decade and in the last two years, was also responsible for New Zealand.

Safe Passage

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