THE SIX-MONTHLY BEANSTALK AUSTRALIAN SHARES REPORT

Report No. 35
Period: Jan-Jun 22

Performance: Underlying Portfolio	Quarter	6 months	1 year	2 years	3 years	4 years	5 years	7 years	10 years
Pre-tax return	-12.8%	-3.3%	1.4%	22.7%	4.7%	3.6%	5.1%	7.4%	10.9%
ASX 300 Accum. Index	*-12.2%*	*-10.4%*	*-6.8%*	*9.4%*	*3.4%*	*5.4%*	*6.9%*	*7.0%*	*9.2%*

* All returns are unaudited. Returns greater than one year are annualised. Beanstalk returns are net of entry and total portfolio exit brokerage costs (0.3% assumed). Zero cash assumed. Returns are pre-fees.

The Underlying Beanstalk Australian Shares Portfolio declined in value for the 6 months to June 30, 2022. It produced a pre-tax loss of 3.3%. These returns are before management fees*. The portfolio outperformed the ASX 300 Accumulation Index for the 6 months to 30 June. Below, a table sets out the best and worst performing stocks in the portfolio over the period.

Best and Worst Performing Stocks**	
Best Performing Beanstalk Australian Shares	Woodside Energy (up 45.2%) AGL Energy (up 34.4%) Sigma Healthcare (up 31.4%)
Worst Performing Beanstalk Australian Shares	Southern Cross Media (down 48.7%) HTE Limited (down 46.7%) Nine Entertainment (down 37.3%)

** A technical attribution list can be provided upon request.

Economic comment

An acceleration of inflation and the accompanying rise of interest rates led to sizeable market declines across the globe. The invasion of Ukraine by Russia, a global energy crisis and ongoing pandemic supply chain disruptions fueled inflation. US stocks led declines with markets there down 20% and the NASDAQ falling almost 30%. Asian markets outperformed and the Nikkei only declined 8.3%. The UK market was down 1.2%. The Australian dollar rallied against most major currencies other than the US dollar. As war in Ukraine and energy crises raged around the world, commodities soared especially across the bulk sector. Oil rallied 43% and thermal coal rose 123%. Inflation pushed Australian 10-year bond yields to a 3.66% close. At one stage yields reached in excess of 4.10%, the largest rise in yields experienced for some time.

The Federal Reserve Board (FED) views the current economic recovery as faster than expected. Job reports have been firm, participation rates are rising and unemployment has reached 3.6%. Apart from recent slowing in response to higher rates, activity surveys have been indicating above trend growth. The FED raised rates to the range of 0.75% to 1.0% and followed on with a 75bps hike in June with more expected at following meetings. The Fed shelved any thoughts that price increases were transient. Inflation went on to reach its highest reading since 1981 for the March report at 8.5%. The April reading printed at 8.3% sowing optimism that inflation had peaked. This optimism was dashed when the May inflation reading came in at 8.6%! Upon the exclusion of energy and food inflation the number did decline, nevertheless, inflation expectations continued to climb.

Pandemic disruptions and a covid-zero policy have led the IMF to downgrade Chinese growth from 5.6% to 4.4% in 2022. Complicating matters has been the administration’s attempts to deleverage the property sector. Pandemic shutdowns such as that seen in Shenzen and Shanghai are draining on growth and adding to the world’s inflationary supply chain problems. China is likely to experience negative GDP growth for the June quarter. Retail sales and industrial production have declined with Shanghai undergoing further restrictions just after having opened from its recent strict closures. Infrastructure investment which is less Shanghai dependent is growing strongly. This will still not be enough to prevent an overall contraction.

The Japanese economy contracted slightly in the first quarter. Covid-restrictions impacted growth with business investment declining and higher imports subtracting from GDP. A lifting of restrictions since has seen the Japanese leading economic index rise to a four-month high. Encouragement has also come from a planned 10 trillion yen stimulatory supplementary budget.

The European and UK economies continued forging ahead. In the UK, unemployment fell to 3.7%. In the Euro area it declined to 7%, the lowest number ever published! Europe and the UK experienced inflation readings above 7%. The Bank of England raised rates to 1.25%. Europe has yet to embark on a cash rate tightening cycle. The UK is experiencing weaker growth (from higher inflation) and a cost of living crunch at the same time. The European Central Bank (ECB) has been less proactive than the BOE in dealing with inflation. As a laggard to raise rates, the

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ECB appears to see inflation as supply driven and not demand driven. Cynically, this might appear a convenient argument if attention is drawn to its heavily indebted southern states. It appears, in the initial stages, that the ECB has taken a more dovish approach relative to other central banks.

The Reserve Bank of Australia (RBA) concluded bond purchases, implemented in response to the pandemic, on the 10th of February. The bank went on to increase interest rates by 25bps in May, 50 bps in June and another 50bps in early July with further increases expected in coming months. The current benchmark rate sits at 1.35%. Suddenly, the RBA is removing accommodative policy in a rush placing the central bank firmly behind the curve. The RBA is forecasting an inflation reading of 7% late in 2022. Economic growth for Australia is expected to be robust for the remainder of the year and this is reflected in the unemployment rate that prints at a low of 3.9%. The participation rate is rising and employers are unable to find an adequate quantity of labour. This is an environment of strong economic growth! Real interest rates in Australia are still below zero and business investment appears to be gradually moving forward. The energy crisis in Europe and the war in Ukraine has boosted Australia's national income. This is also alleviating pressure on the budget.

On the 21st of May a federal election was held in Australia. The outcome of this nationwide vote was to install a new labour government to power with Anthony Albanese replacing Scott Morrison as the new Prime Minister.

Commentary on Australian equities

The February reporting period exceeded expectations with outlooks positive and dividends higher. Companies benefited following a rebound from lockdowns. Inflation was more prominent across commentaries. Price increases for energy and freight were widespread as reported by **Ansell**, **Nick Scali** and **Amcor**. Supply chain disruptions were especially challenging for inventory management as experienced by **Breville** and **Wesfarmers**.

Companies such as **Wesfarmers** experienced margin pressure from higher inflation and pandemic cost increases. Many other companies, including **James Hardie** and **Westpac** still benefited using an increase in pricing or reductions in the cost base. The economic rebound itself gave **Nine Entertainment**, **Seek** and **REA Group** the ability to leverage existing assets.

The second half reporting period is likely to ride the bow wave of resource and banking stocks. Commodity prices have been robust and short-term rate increases combined with cost measures are likely to assist the lending sector. Economic growth remains firm. A buoyant consumer sector is expected to underpin growth. Aside from the commodity and banking sectors, business profitability outcomes will be industry specific. In many sectors, companies will complain of planning fatigue as volatile conditions impact on inventory and cost management. These conditions include pandemic induced supply constraints and soaring energy prices borne through capital rationing across the carbon energy sector.

Excluding the banks and commodity producers, there is expected to be a larger portion of the listed market experiencing margin pressure than previously. Price increases, economic growth and cost reduction programs will continue to assist. The dividend environment should be progressive.

Outlook statements are expected to focus on direct and indirect impacts of inflation on business.

Best Performing Stocks for 12 months per FTSE Australian Index		
Whitehaven Coal	up 150%	Not in Beanstalk Portfolio
Allkem	up 59%	Not in Beanstalk Portfolio
Pilbara Minerals	up 58%	Not in Beanstalk Portfolio

Worst Performing Stocks for 12 months per FTSE Australian Index		
Magellan Financial Group	down 76%	Not in Beanstalk Portfolio
Platinum Asset Management	down 65%	Not in Beanstalk Portfolio
Appen	down 59%	Not in Beanstalk Portfolio

The Beanstalk Australian Shares Portfolio represents compelling value. Modeling work across the portfolio reveals post-tax internal rates of return on average to be in excess of 23%.

Gas, Water and Multiutilities and Real Estate Investment Trusts are sectors displaying good relative value in the Australian market. Valuations in Construction & Materials, General Retailers, Beverages, Food & Drug Retailers, Industrial Transport and Pharmaceuticals are less attractively priced. Specific stocks trading at low levels include HTE Ltd, Nine Entertainment and Adelaide Brighton Cement.

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Industry Capital Environments and Capital Flows

Industries providing **more favourable** **capital environments** for investors include beverage and tobacco product manufacturing, wine, packaging, electricity (dispatchable capacity), gas, food retailing, engineering construction (contractors and materials), building construction, paper, forestry, specialty finance, financial planning, banking, general insurance, media, pharmaceuticals, oil & gas, LNG, thermal coal, diamonds, services to mining, petroleum and chemical manufacturing, machinery and equipment manufacturing, metal product manufacturing and tourism. **Less favourable** industries include the real estate, food, minerals & metals (excluding thermal coal, diamonds and silver), infrastructure, transport, services to transport, pathology, private health and community services and automotive sectors.

Wood product manufacturing and services to agriculture have been removed from the unfavourable list in line with ABS data. Technology should be added to the unfavourable list. This reflects the extremely low cost of capital for this industry and its importance for incremental capital allocation in a relative sense.

Manufacturing generally, warehousing and storage have been moved to the favorable list. This is corroborated by ABS data. It is also reflective of supply chain constraints, especially globally, which have effectively removed inventory chain management infrastructure from the system. ABS data suggests transport equipment manufacturing and wood paper product manufacturing should be added to the favourable list. Global grain stocks have been depleted due to poor harvests from La Nina, low planting levels and war in Ukraine. These commodities are added to the favourable list. Similarly, high energy costs have shut sizeable smelting capacity for Aluminium and Nickel placing remaining capital owners in a favourable position with respect to their capital investments. Finally, Motor Vehicle Retailing is added to the favourable list.

Beanstalk Australian equities – Portfolio changes

Portfolio turnover returned to more average levels following previous elevated activity. Resources, utilities and defensive holdings were reduced in favour of domestic cyclicals, healthcare and financials. These transactions served to reduce US dollar exposure. New healthcare and building material positions were added to the portfolio. Small capitalisation exposure in the portfolio increased.

Resource and utility positions were trimmed into a strengthening market allowing funds to be added to a low weighting in financials and healthcare.

Sims Metal Management, **Woodside Petroleum** and **Origin Energy** experienced strong share price rallies. This strength was largely driven by an uplift in the sale price of commodities including scrap metal, crude oil and LNG. Outlook statements were positive and each company rewarded shareholders with either increased dividends, buy backs or both. The portfolio rebalanced by reducing the oversized positions into these share price rallies.

The sale of **Sims Metal** was made after the receipt of a sizeable dividend. An acquisition of **Westpac** with these sale proceeds entitled the portfolio to a decent fully franked dividend post **Westpac's** March-end interim results. **Westpac** has considerable levers to pull in terms of cost and capital management. Economic and capital pressures imposed during covid have significantly reduced and this, together with sales of businesses, have created conditions for improving dividend payments and higher returns.

Proceeds from **Origin Energy** and **Woodside Petroleum** were invested into **AMP Limited**, **Southern Cross Media** and **Sigma Healthcare**. The liquidation of **Metcash** provided further funding to the **Sigma Healthcare** acquisition.

AMP's share price took another step down in January, reaching a price below 90cps. This reflected frustration from investors as the company again requested patience. The portfolio purchased additional holdings on the basis that such disappointment was already discounted in the share price and that a forthcoming split of the business would provide tangible valuation signposts.

In May, **AMP's** share price rallied towards $1.20. The catalyst was the gradual realisation of value through piecemeal sales of its Collimate Capital business. These sales culminated in up to $2.5 billion of value. There is now significant pressure on the company to return in excess of 40cps of capital to shareholders. The portfolio trimmed its oversized position with funds applied to **Sigma Healthcare**.

The sale of **Metcash** represented the final parcel of that stock to exit the portfolio. Beanstalk has been reducing its position in **Metcash** for some time while banking generous dividends and enjoying strong share price growth. The portfolio's sale proceeds represented four times the price paid back in 2015 when many commentators claimed that the business was going into bankruptcy, supposedly squeezed by large format stores. These existential criticisms paid no regard to the relevance of the 'local' footprint of IGA stores. A sound and well managed business with a

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stock price providing good compensation, **Metcash** made way for an investment offered at a significantly larger discount, **Sigma Healthcare**.

Holdings of **Sigma Healthcare** were increased further in May. Funding this time was provided by **AGL Energy**. The company rallied 60% following purchases in November. This lifted its weighting to an oversized level that required adjustment. Investors began to ponder the energy crisis in Europe, the war in Ukraine and the importance of energy security. Electricity prices were also climbing steeply from low levels. Adding further to the upside were two takeover proposals involving **Brookfield**. These proposals were rejected with the latest price of $8.25 deemed as undervaluing the business. The company pushed ahead with its demerger plans only to find it lacking requisite shareholder support. The CEO and Chairman have announced that they will step down leaving the market to speculate further on takeover possibilities.

The new position, **Sigma Healthcare**, was added to the portfolio following a large share price decline in response to a profit warning. Implementation of the company's enterprise resource planning (ERP) program suffered covid-related setbacks. This impacted sales negatively and added extra costs. The share price had fallen 17% upon release of the announcement and 40% since the highs of the year. The ERP program and cost setbacks that have plagued **Sigma** through the opening of its new warehouse are expected to have a short-term impact. Vikesh Ramsunder, who took over the CEO role recently, is focused on reclaiming lost market share and ensuring that customers are not let down again. The new warehouse facility should allow significant volume growth and margin expansion in the medium term. At the current heavily discounted price and with the brand loyalty on display, **Sigma Healthcare** represents an attractive investment.

Additional holdings of **Southern Cross Media** were acquired after the market's negative response to a weak cash flow number. Hesitancy from advertisers into the new year also weighed as Omicron created uncertainty around supply chains and the ability of businesses to invest short-term with confidence. The share price had fallen 26% since this result was released. Such a large fall appeared to be an over-reaction. The cash flow number reflected a covid-related deferral of payments from the prior period leading to higher tax and supplier cash outflows in the first half of FY22. Weakness in cash flow largely reflected timing differences. The company declared a strong dividend and has undertaken a buy-back program.

Further supplementing these purchases of **Southern Cross Media** were sales of holdings in the media company **NZME**. This business has seen a significant rally in its share price after reducing debt, resuming dividend payments and undertaking share buy-backs. **NZME** has interesting growth opportunities in the digital space. Further revenue opportunities should arise as the company seeks to leverage its traditional assets into the digital world. This includes claims for substantial compensation from large digital users of its content such as Facebook and Google. The company's strong share price provided an opportunity to increase positions into a discounted **Southern Cross Media**.

The final transaction of the period involved the liquidation of **Tabcorp Holdings** to purchase a new position, **Adelaide Brighton Cement**.

The **Tabcorp** position was purchased during the onset of the pandemic in March 2020. The portfolio liquidated its position following a strong run in that company's share price after emerging from lockdowns. The sale was made prior to a demerger of the business into two separate companies: the wagering and lottery businesses. This demerger followed numerous expressions of interest from outside parties to purchase the company. **Tabcorp** responded to these approaches by deciding to split these businesses and list them separately on the exchange. It believed that shareholders would gain maximum value in this way as the market would pay more for the businesses as separate entities than it was currently paying for them as a combined entity. The twenty-share limit on the portfolio set in train the search for a post-tax arbitrage solution given the pending issuance of script for the standalone lottery business.

The most effective solution was to sell the entire **Tabcorp** position, rather than sell another stock in the portfolio to make way for the additional lottery script. **Adelaide Brighton Cement** provided a value accretive alternative.

Adelaide Brighton produces and distributes cement, lime, concrete, aggregates, masonry products and industrial minerals. It has a leading or large share in the markets in which it operates. The company looks to have been oversold following covid, wet weather shutdowns and concern in the building sector from rising interest rates. Its exposure to non-residential construction is high. The infrastructure pipeline is large and a shortage in apartment stock provide a demand outlook that would appear sustainable even with higher interest rates. Share price depreciation appears to be overdone.

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Outlook - Australian equities

The Australian shares underlying portfolio has a higher and increasing exposure to domestic conditions than international conditions. It favours a weaker Australian dollar (is exposed to the USD, euro, pound and $NZ), retains strong balance sheet flexibility in the aggregate, benefits from rising commodity prices and has a low exposure to long-duration stocks and rising bond yields. The portfolio's exposure to housing is below benchmark. Beanstalk is focused on balancing the portfolio in a tax-effective manner while redeploying funds into those equities trading at highly attractive discounts to valuations.

The Australian equity market has fallen over 14% since its highs of the 21st April 2022. This move has been in response to a reassessment of the speed with which the RBA is expected to raise its benchmark rate. The cash rate currently sits at 1.35% and the inflation rate is 5.1%.

Heightened inflation, the cause of central bank activity, is likely to gradually decrease as demand is contained, energy prices stabilise and investment alleviates capacity constraints. Equity markets will greet this outcome positively, adjusting downwards expectations of more rapid rate increases.

Even in the circumstance of more persistently elevated levels of inflation, investors should know that real interest rates are still well below 0%. In combination with a 14% fall in market prices and attractive valuations, select equities continue to provide a solution toward real wealth creation and preservation.

The 14% decline in the market has invoked fears of an imminent recession. Interest rates are still some way from neutral levels, and as discussed, these heights may not be reached as quickly as initially anticipated by the market. Monetary conditions are stimulatory.

The Australia economy remains healthy. Unemployment is at very low levels providing a driver of consumption. Household budgets are not currently a concern and consumers have savings accumulated over the pandemic years. Business investment is showing some signs of life and state fiscal programs are active. Australian terms of trade are providing a positive shock to national income. Just as an example, 26Mt of wheat is expected for export in 2022-23 which is significantly above average levels and at prices that are exceptional.

The Australian economy and equity market remain well supported in both activity and monetary terms. This support should largely be corroborated by company earnings.

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BEANSTALK Investment Management

The Beanstalk Australian Shares Portfolio

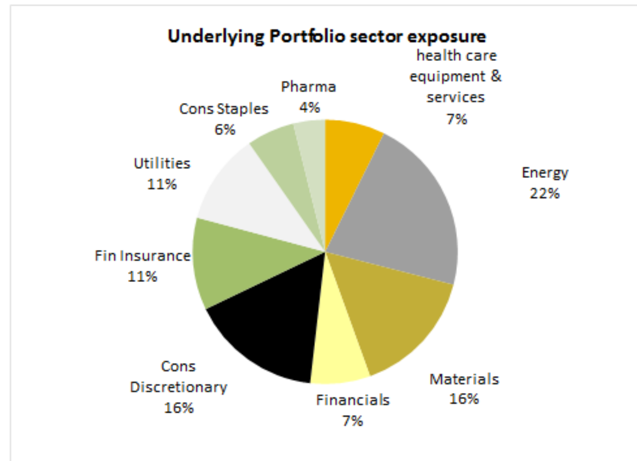
PROFILE OF A $125,000 HYPOTHETICAL PORTFOLIO

CLIENT: **AEQ Underlying Portfolio**

PORTFOLIO VALUE: **$ 173,005** as at 30-Jun-22
(include $ paid out as income - for year only)

PERIOD SUMMARY	30-Jun-21 to 30-Jun-22
Unaudited pre-tax return	1.4%
Unaudited post-tax return	0.0%
UNAUDITED CUMULATIVE RETURNS	
- pre-tax *	122.6%
- post-tax (assuming liquidation)	109.6%
Tax payable/(losses available):	$ 2,405

* incl. Initial broker acq'n cost to establish portfolio



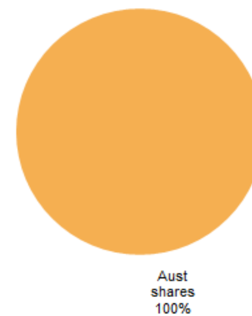
For a hypothetical Underlying Portfolio (excl. income)

Aust shares	***100%***
WPL	$ 19,062
ORG	$ 16,835
WBC	$ 5,832
AWC	$ 8,263
AVG	$ 9,650
MYX	$ 6,417
AGL	$ 18,431
ABC	$ 4,870
AMP	$ 14,668
BEN	$ 6,286
NUF	$ 4,127
SIG	$ 12,128
FBU	$ 3,303
SXL	$ 6,249
SGM	$ 5,082
APN	$ 3,694
NZM	$ 3,864
SGR	$ 5,037
SUN	$ 4,050
NEC	$ 7,756
	$ 165,604

Fixed interest	**0%**
-Govt bonds	0%
-Corporate debt	0%
	$ -
Listed property	**0%**
	$ -
International shares	**0%**
	$ -
Cash	***0%***
	$ -

Fund summary

Aust shares	$ 165,604
Internat'l shares	$ -
Fixed interest	$ -
Listed property	$ -
Cash	$ -
Total	$ 165,604



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