BEULAH CAPITAL

Australian Equities Income Portfolio

Quarterly Fact Sheet | September 2021

L3, 163 Eastern Rd, South Melbourne Vic 3205
T +613 9270 9170 **F** +613 8080 5983
W beulahcapital.com

Beulah Capital Pty Ltd
ABN 72 079 169 127
AFSL 330951

beulah

Investment Approach

The portfolio aims to outperform the S&P/ASX 100 Accumulation Index over a rolling 5-year period.

INVESTMENT STRATEGY

The portfolio invests in a concentrated portfolio of securities in some of Australia's largest 100 ASX listed companies. The portfolio is constructed to provide both an income stream and long-term capital growth from an investment in 20 to 25 of Australia's largest companies.

Universe

This investment strategy provides access to some of Australia's largest listed companies generating consistent and above average dividend yields on an after tax (including franking credits) basis.

INVESTMENT CATEGORY
Australian Shares

MINIMUM INITIAL INVESTMENT
$50,000 on a standalone basis

MINIMUM SUGGESTED TIME FRAME
7 Years

Performance

	1 Month	3 Months	6 Months	1 Year	3 Year (p.a.)	5 Year (p.a.)	Since Inception (p.a.)
Australian Equities (Income)							9-Mar-12
Income Return	0.95%	1.94%	2.88%	5.16%	5.57%	5.80%	5.91%
Capital Return	-2.21%	0.60%	6.22%	21.79%	0.75%	0.75%	4.19%
Model Portfolio Return	**-1.26%**	**2.54%**	**9.10%**	**26.95%**	**6.32%**	**6.55%**	**10.10%**
S&P/ASX 100 Accum Index*	-1.85%	1.56%	10.16%	30.94%	9.91%	9.54%	12.27%
Relative Performance	*0.59%*	*0.98%*	*-1.06%*	*-3.99%*	*-3.59%*	*-2.99%*	*-2.17%*
Franking Credits	0.39%	0.72%	0.90%	1.55%	1.78%	1.89%	1.99%
Total Return inc. Franking	**-0.86%**	**3.25%**	**10.00%**	**28.50%**	**8.10%**	**8.44%**	**12.09%**

Performance Notes

1: All Benchmark and Model returns are calculated assuming dividends are reinvested
2: Returns greater than 12 months are annualised
3: Returns are calculated before transaction, portfolio and MDA fees as these differ pending what platform the investment is held
5: Returns and holdings may vary between investors given the nature and timing of beneficial ownership under an MDA structure
6: This document is for marketing purposes only
7: Past performance is not an indication of future performance
*8: *From 1 June 2018 the Australian Equities Income benchmark changed from the S&P/ASX 100 Industrials Accum Index to the S&P/ASX 100 Accum Index*
9. Inception date is 9 March 2012

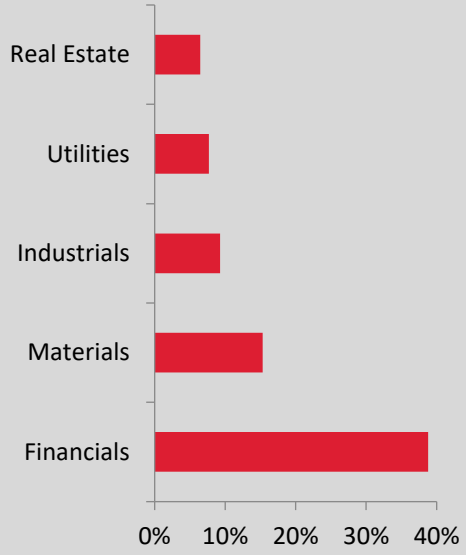
Franking Credits - Franking credits may be earned when a company pays a dividend. Where recoverable, these would represent a real return from the Portfolio.

Top 5 Stock Holdings

Company	Allocation %
Stockland Group	6.34
Commonwealth Bank	6.18
Transurban Group	5.78
Telstra	5.67
National Aust Bank	5.21
Total	**29.18**

Holdings as at 30 September 2021

Sector Allocation



Key Portfolio Features

Key Portfolio features	
1yr Fwd Portfolio Cash Yield	5.73%
1yr Fwd Portfolio Gross Yield	7.32%
1yr Fwd Portfolio P/E Ratio	14.60x
Percentage of cash held	13.60%

Top 5 Performers

Company	Contribution to performance %
Ausnet Services	1.36
Sydney Airport	1.17
Spark Infr Group	0.86
Medibank Private	0.53
Suncorp Group	0.44

Worst 5 Performers

Company	Contribution to performance %
Fortescue Metals	-1.50
BHP Group	-0.99
Magellan Financial	-0.65
Rio Tinto	-0.64
Stockland	-0.27

Market & Economic Review

The September quarter could be described as a tale of two halves, which began with great optimism, but ended under a cloud of uncertainty. In July, markets were buoyed by stronger-than-expected US earnings and this theme also emerged throughout European equities. It was a familiar scene across developed markets, with gains driven by health care and technology stocks. However, emerging markets were in for a rude shock. Having already been battered by the fast-spreading Covid-19 Delta variant, China's crackdown on its private technology firms and private education sector saw widespread selling.

As August rolled around, it was Australia's turn to put on an earnings show, which was headlined by a surge in dividends. Indeed, August marked the 11th consecutive monthly gain for domestic shares and the best consecutive monthly run since 1943 – the only previous time a streak of this length has happened. Meanwhile, US equities delivered their seventh straight monthly advance (the longest winning streak since January 2018), as share buyback announcements exceeded pre-Covid levels.

But, like all good things, the euphoria came to an end in September as mounting risks began to loom large. There was widespread selling across all regions thanks to ongoing negative news out of China led by an impending default by indebted property developer Evergrande; rising bond yields on increased talk of the US Federal Reserve (the Fed) tapering its asset purchasing program (QE); and a near stalemate in the US debt ceiling debate, which threatened to derail the global recovery.

In fixed income markets, the European Central Bank (ECB) announced a reduction in the pace of its asset purchases, but in contrast to the Fed and Bank of England, stressed that this was not the beginning of a process of tapering purchases down to zero. Elsewhere, credit markets began the quarter strongly as implied default risks broadly declined, but this completely reversed as economic data began to point to much slower growth following the June quarter peak.

However, an energy market rally was perhaps the main event to emerge during the quarter. Coal prices forged fresh records as ongoing tight supply in China was exacerbated by a lack of mining investment and pandemic-induced import constraints. Two-thirds of China's provinces were reported to be rationing power and many factories closed or reduced production. Households fell into darkness and streetlights were turned off in numerous cities. In Europe, a surge in natural gas prices amid inventory shortages also led to an energy crisis, with Russia seen as the culprit. Meanwhile, rising fuel prices were just one problem in the UK, where supply was hampered by a shortage of truck drivers, many of which were forced to return to eastern Europe following the Brexit deal. This often led to lines of cars queuing for petrol that stretched well over a kilometre.

On the economic front, inflation appeared to reach a crescendo in the June quarter as prices were well above levels recorded from a year earlier in both Australia and the US. Higher petrol prices and supply chain disruptions were the main contributors. Central banks painted this as a temporary phenomenon, but as supply-side constraints continued, markets began to revise inflationary expectations higher.

Rising wages also fed into the price rises as economies continued on a path towards reopening. Reports of labour shortages became more common in both skilled and unskilled segments of the market, as cheaper non-resident labour remained locked out of many countries. In the US, there was a sigh of relief as legislation was passed in a bid to avoid a partial federal shutdown and keep the government funded until December 3rd. There are concerns that this could merely be delaying a crisis as political parties dig in on a dispute over how to raise the government's borrowing cap before a potentially catastrophic default.

Portfolio Review

The Portfolio returned 2.54% during the September quarter. With the addition of franking credits, the Portfolio delivered a grossed-up total return of 3.25%. The September quarter was characterised by takeover activity, which provided a solid boost to returns. Sydney Airport (SYD) and Spark Infrastructure (SKI) received buyout proposals that prompted a surge in stock prices and led to the sale of these positions following significant gains.

Portfolio Review (cont.)

Both holdings were top performers during the quarter and Ausnet Services (AST) also performed well given its attractive asset base.

Weak performers during the quarter were BHP Group (BHP) and Fortescue Metals Group (FMG), with the collapsing iron ore price driving down profit expectations. Magellan Financial Group (MFG) was also a weak performer, with the market concerned about the poor performance of some of its funds, including its flagship fund.

The Portfolio remains well diversified and, despite the strong recovery of the broader market, the 1-yr forward cash yield continues to improve. Despite holding a higher cash position than usual, the Portfolio cash yield at 30 September 2021 stood at 5.73%. With the addition of franking credits, the Portfolio's grossed up yield is above 7.3%.

Outlook

There was a significant slowdown in global economies throughout the third quarter. China stopped to a crawl and, along with the US, has seen its growth forecasts downgraded by the IMF. In Australia, austere lockdowns across its most populous states proved to be a bitter economic pill, with many businesses inadequately compensated by various income replacement schemes. Businesses were further hampered by a mismatch of workers in areas that could reopen, along with the effects of a cautious relaxation of restrictions.

While the deployment of vaccines throughout Australia has reached breakneck speed, in many other regions there has been a noticeable slowing. Further complicating matters, has been the obvious drop-off in immunity from the current batch of vaccines. This situation has allowed the more contagious Delta variant to spread rapidly, even across highly vaccinated populations. Fortunately, the new wave of cases has not translated into serious illnesses and deaths at anywhere near the same levels we saw throughout 2020 and the first half of this year. For the reopening of economies to continue in earnest, it seems that a booster program will need to be rolled out in the near term and improved vaccines will have to be developed over longer horizons.

In any case, the pandemic is having disruptive economic effects that look set to continue well into next year. Policy-induced labour supply constraints are posing a conundrum for a wide range of employers. In the US, recent jobs growth has been underwhelming at the same time as quit rates have skyrocketed. It seems that many workers have been afforded an opportunity through temporarily increased welfare payments to demand higher pay, change jobs, or sit out of the labour market altogether. The implementation of vaccine mandates has reiterated this effect, with the health care and education sectors seeing record levels of churn.

A similar dynamic is playing out in Australia, as the NSW and Victorian lockdowns have led to significant job losses and a slump in workforce participation. The net result of this has been little change to the headline unemployment rate, but a surge in hidden unemployment. Women and part time workers are the hardest hit cohorts, especially those unable to work from home. Similar dynamics have played out in the UK and parts of Europe, with some commentators coining this: "the great resignation".

However, much of the market's focus has been on inflation and the extent to which it will prove transitory or otherwise, thereby influencing important policy decisions. Inflation may have peaked in most regions during the June quarter, but has remained elevated largely due to supply-side shortages and stronger services demand as economies have reopened. In Australia, the less volatile underlying measures of the CPI grew at an annualised rate of 2.8% in the September quarter. This measure is up from 2% p.a., despite the reimplementation of restrictions that slowed services inflation.

While inflation is also on the rise in the UK and Europe, most attention is being paid to the US, where inflationary expectations are rising among consumers and producers, and annual wages growth looks set to exceed 5%. All this while industrial capacity utilisation is above 75% and rising – despite strong investment in physical capital. History would suggest that periods of persistent high inflation in the US have coincided with at

Outlook (cont.)

least 4% wages growth and 80% capacity utilisation. With energy prices and housing costs rising, and food prices reaching ten-year highs during September, we expect that our medium-term projection of a 2.5% to 3% consumer inflation rate in the US will take longer to achieve. Similarly, flatter trajectories towards lower domestic inflation are also anticipated, but we remain of the view that consumer prices in Australia will fall to 2% to 2.5% over the medium term.

With the recent supply-constrained global slowdown occurring in an environment of elevated prices, market talk about stagflation is becoming more commonplace. Given that budget deficits are shrinking (providing a negative fiscal impulse), monetary policy looks set to begin tightening, house prices are soaring and energy prices are rising, we could be entering a stagflationary period. However, we are expecting growth to pick up later this year and into next year, which would mean that only a brief period of stagflation might potentially occur. Indeed, most markets would be prepared to look through this.

But, if circumstances arose (e.g., new vaccine-resistant Covid variants) that continued to hamper growth and kept prices rising at current rates, markets would not be expected to react favourably to this. Previous stagflationary periods have typically coincided with bear markets and have seen investors flee companies that are unable to protect margins, while being far less prepared to hold stocks that trade at exorbitant multiples. Bond markets would also likely struggle in such an environment as there would be pressure for higher interest rates to help contain inflation.

For the time being, we see advantages to remaining invested in risk assets, while maintaining low duration positions in fixed income, with a preference for income generation from higher quality credit exposures. However, a catastrophic (uncontained) default from Evergrande, or a downgraded US credit rating, are among factors that would require this view to be revisited.