oracle
ADVISORY GROUP

# QUARTERLY UPDATE

ISSUE 37 - SEPTEMBER 2023

MARKET UPDATE >>

MODEL PORTFOLIOS >>

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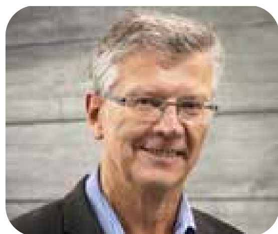
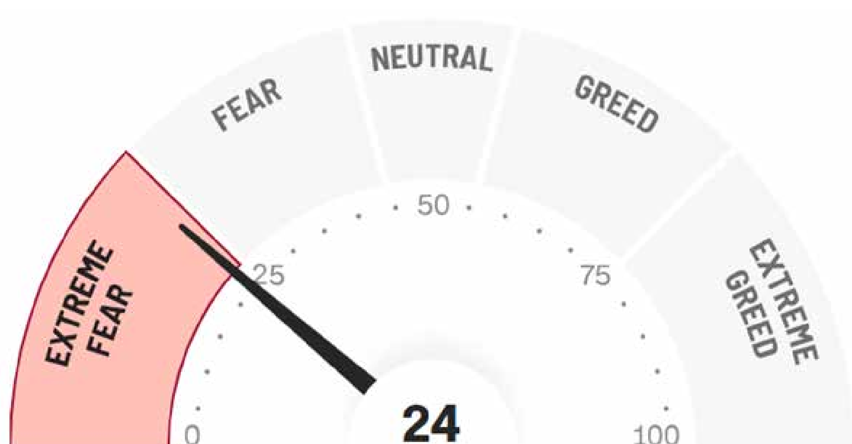
# Oracle Market Update



**By Peter Durbin**
Chief Investment Officer

**2023 continues to surprise. In the closing days of 2022, one of the most difficult years for markets on record, there was nothing but pessimism. In August, I wrote internally to our staff that "though the economic outlook has not exactly improved, some markets are in the midst of another raging bull market". Today, only 2 months later, the CNN Fear and Greed Index has swung from Extreme Greed in late July to Extreme Fear in early October and these 2 months the S&P 500 is down 6.6%, the ASX All Ordinaries Index is down 4.9%, and the MSCI All Country World is down 5.8%.**

## Fear and Greed Index




*Source: CNN Business*

The Fear and Greed Index seeks to capture the mood or sentiment in the S&P 500 market by gauging:

- Market momentum (measured by the moving average of the index),
- Stock price strength (measured by the number of stocks at 52 week highs),
- Stock price breadth (measured by the number of stocks that are rising vs falling),
- Options ratios of the number of investors betting on a market fall vs a market rise,
- Market volatility, (measured by price fluctuations expected by investors, per the CBOE Volatility Index, or VIX)
- Safe haven demand (measured by the 20 day performance of equities vs Treasury Bonds, which perform well in times of fear and uncertainty),
- Junk bond demand (another measure of preference for safety, measured by the difference in yield between higher risk non-investment grade (or "junk") bonds vs investment grade bonds).

In early October, only junk bond demand suggests an environment of Extreme Greed, all others are in Extreme Fear territory.

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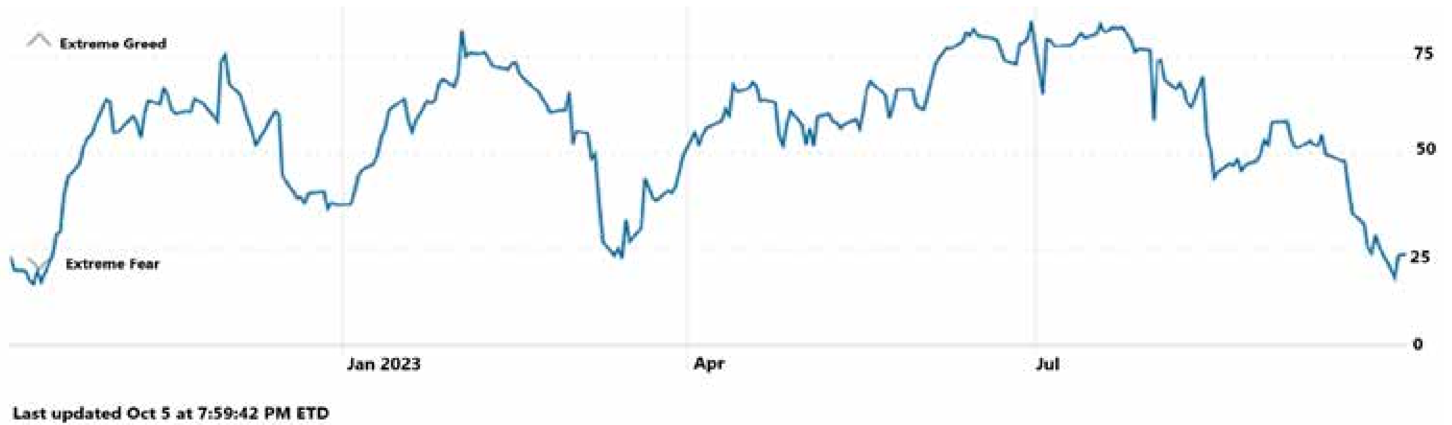
# Oracle Market Update




To chart the movement of the Fear and Greed Index is to tell the story of the market movement through the year. The year started in “Fear”, but by late February sentiment had already improved to “Extreme Greed” before falling to “Extreme Fear” in early March when US regional banks looked unstable. The Fear of a banking crisis gave way to AI-driven Extreme Greed, and remained there until late July, at which point bond yields started increasing and the US Federal Reserve, despite not raising rates, made it clear that rates would remain higher for longer. Even though the Fed has been saying this all year, the market finally began to believe them resulting in a savage selloff in markets to the Extreme Fear environment we now find ourselves in.

Other factors also likely played a role in the current tumult, with industrial action in the US auto industry, the possibility of another US government shutdown, student loan repayments being reinstated, and higher oil prices all combined with Powell’s comments.

Why spend so much time talking about this index? And why today? The answer is that while Mr Market has been as manic-depressive as ever in 2023, the companies inside the index (and our portfolios) have continued to run their businesses. They have continued to invest for the future. And they have continued to grow their profits (hopefully).

Normally we talk about multiples in this context, but the Fear and Greed Index gives a good second opinion. However, the two tend to move together. In times of optimism, stock prices will be bid up such that the ratio of share prices to their expected earnings will increase (the forward P/E ratio) and in times of pessimism will decrease.

The following chart shows how this plays out. The red bars denote the time when the Fear and Greed Index troughed inside Extreme Fear and the green bars when it peaked inside Extreme Greed.

*Source: Oracle Investment Management, FactSet, CNN*

*Continued over the page*

What it shows is the futility of trying to time the market, because the mood of the market can turn on a dime and it will take prices with it. But it won't take valuations. You might be asking "What's the difference?" The difference is huge. "Price is what you pay, value is what you get". So said Ben Graham to Warren Buffett, as quoted in the 2008 Berkshire Hathaway Annual Letter. In other words, the value of the business doesn't change just because the mood of the market changes the share price.

We are often asked for our view on where markets are going. I think the Fear and Greed index would discredit anyone trying to answer that question with any seriousness. Who would have predicted at the start of the year that the collapse of Silicon Valley banks would cause an international banking crisis that would weigh heavily on markets? Some would, and I'm sure some did, but to call those who did a minority would be overstating it. And who would have predicted the release of ChatGPT would lead to an artificial intelligence bonanza? AI is not a new theme, and those who invested in it before 2023 did very well. But the timing of this AI-fueled rally was unlikely to be predicted by many. And finally, who would have predicted that the market would finally heed Fed chair Jerome Powell's warning that higher rates are here to stay? Now I'm certain this was a larger cohort, but again, it would have been difficult to predict the timing of when this would occur.

My point is that these are not entirely unpredictable events. And some investors will have portfolios positioned ready for them. But all of them? And in order? If you had positioned a portfolio for one, then the other, then the other, you would have looked insane because you would have had to shift your portfolio between extremely bearish to extremely bullish several times within 9 months. And this is the key takeaway: to time the market successfully you not only have to get your exit right, you have to get your reentry right too. What is the point of getting a short-term sell call right only to miss the right time to reenter the position, only to see the price end up higher than when you sold?

It is better to be confident in the company you own and stick it out through the difficulties and obstacles. Not only will this help you sleep better at night, but you won't be interrupting compounding with things like taxes and transaction fees (but that is a discussion for another day). Better yet, history shows that the best time to buy is when the market is in times of Extreme Fear. I could pull out some more well-trodden quotes like buying when there is blood on the streets or being greedy when others are fearful, but I will instead quote Morgan Housel from a recent podcast entitled Rules of the Money Game. Rule 23 is this:

*"Past success always seems easier than it was because you know how the story ends".*

He goes on to say that it is easier to quote Warren Buffett than to do what he does. What Buffett does is invest very dispassionately with a rigorous emphasis on business quality and strict adherence to company values. It is not easy to buy in times of market fear because there is always a reason the market is acting jittery. If you only want to invest in times when everything looks rosy, guess what? You will pay a premium for the privilege.

In times of fear, it is all too easy to agree with sentiment and sit on your own because the market may go lower. In all likelihood, it will. But to invoke a Bill Ackman maxim, the lowest average cost wins. Buying in times of fear may lead to short-term loss, but greatly increases the likelihood of long-term gain because you are buying when stocks are in the proverbial bargain bin.

Mr. Market is currently in quite the mood and our response is as follows: we will continue to do what we always do. We will be responsible stewards of your capital, with which you have entrusted us. When the market presents good opportunities, we will happily take them, but we won't be beholden to Mr. Market's emotional state and we won't be following the madness of the crowd just because sentiment has shifted, because eventually, it will shift again.

# Oracle Global Equities Portfolio Update

**Johan Snyman**
Portfolio Manager

**The Global Equities Portfolio finished the third quarter of 2023 with a loss of 1.91%, relative to our benchmark, the MSCI ACWI ex Australia (in A$). It was a tough July and August, with some improvement in September, with a marginal relative outperformance in the last month of the quarter under review.**

On a 12-month basis, the Global portfolio has advanced by **21.1%**, a relative outperformance of **2.4%**.

The portfolio has been subjected to sector diversification the last twelve months and today the 30 stocks in the portfolio are spread across a vast array of industries, both consumer and non-consumer industrials, plus financial services inclusive of fintech and three investment companies, of which two are European based. It represents a significant change from September 2020, when the Global portfolio was comprised of 18 stocks, and the top-10 positions accounted for 64% of the portfolio – today such percentage is 48.

During the Quarter under review, we have completed an exercise to determine the revenue contribution per region of the Global portfolio, on a weighted basis. **North America** has the highest contribution, with Berkshire Hathaway, CSX and Lowe's Companies having the highest company contributions. **Asia Pacific** has the second highest contributions, with Qualcomm, Taiwan Semiconductor Manufacturing Co Ltd (TSMC) and Yum China having the highest company contributions.

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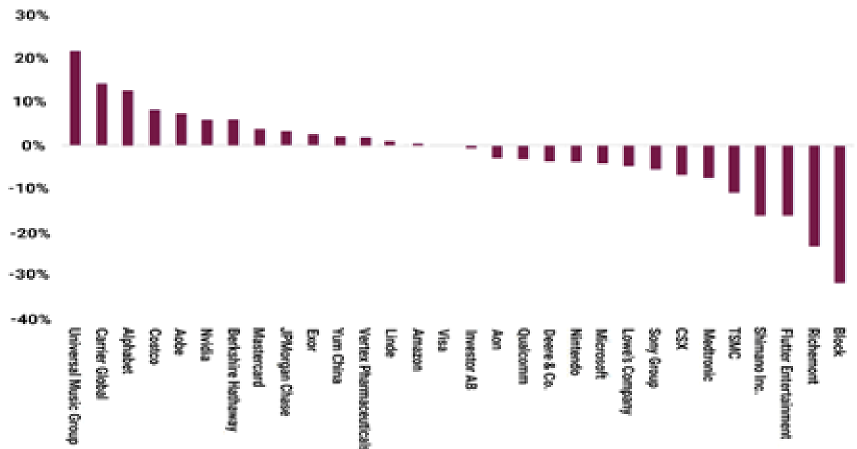
## Portfolio Performance

| Rolling | Global Equities Portfolio | Benchmark (MSCI All Country World Index) | Outperformance |
|---|---|---|---|
| 3 month | -2.31% | -0.40% | -1.91% |
| 6 month | 5.14% | 5.76% | -0.62% |
| 1 year | 21.06% | 18.65% | 2.41% |
| 2 year p.a | -1.04% | 2.60% | -3.64% |
| 3 year p.a | 4.96% | 9.98% | -5.02% |
| 5 year p.a | 7.40% | 8.55% | -1.15% |
| **Since Inception p.a (1 March 2016)** | **9.59%** | **11.08%** | **-1.49%** |

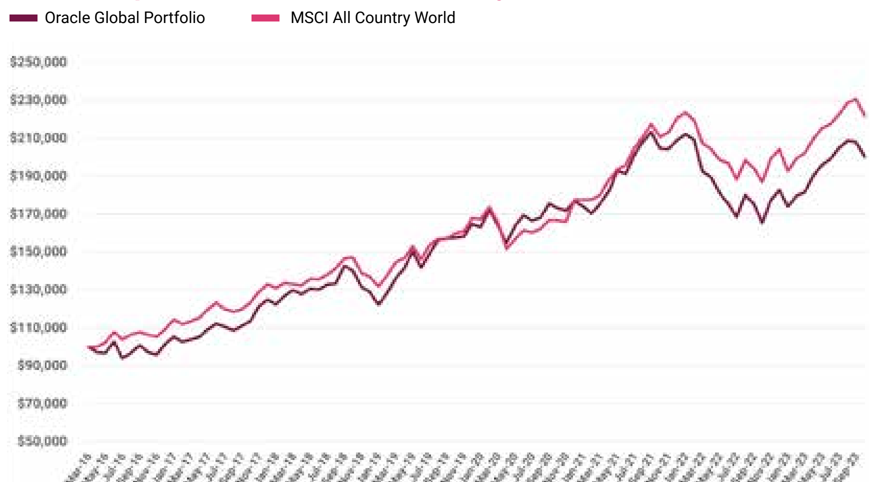
## Three months to September 2023




## Comparative Performance

### Global Equities vs MSCI All Country World (since inception)

Oracle Global Portfolio    MSCI All Country World

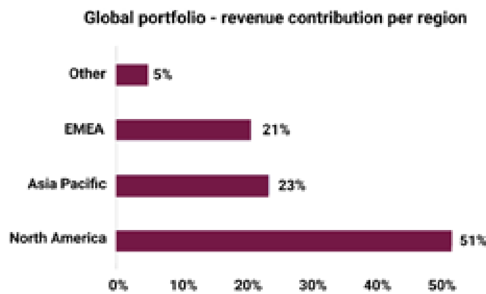


# Oracle Global Equities Portfolio Update

TSMC makes for an interesting analysis – 94% of revenue is derived from selling to customers in Asia Pacific, whilst 90% of manufacturing or production is concentrated in various plants in Taiwan.

Reading the book "Chip Wars" gave us good insight into how US foreign policy in the 70s and 80s first benefited Japan in establishing a fletching semiconductor industry and then how manufacturing of semiconductors given the transition to the "fabless" business model in semiconductors in the 80s resulted in the US losing its edge and set the stage for TSMC to emerge as the market leader. More recently, geo-political risk mitigation has resulted in TSMC plants currently under construction in Japan and the US and early stages of reviewing potential expansion in Germany.

The largest company contributions in **EMEA** are Aon, Flutter and Shimano – the contributions are far less concentrated




compared to North America and Asia Pacific.

During the Quarter, we initiated three new positions in **Sony Corporation** (SONY), **Carrier Global** (CARR) and **Nvidia** (NVDA). It takes the tally of companies in the Global portfolio to thirty, a very different scenario to twelve months ago (nineteen companies in the Global portfolio at the end of September 2022). In the meantime, we have sold out of Bristol-Myers Squibb (BMS) and General Mills (GIS).

We initiated a position in **Sony** at the beginning of the Q. Sony is a household name and its history dates to ("only") 1946 – after the end of World War II ("WWII"), Masaru Ibuka started a radio repair shop in Tokyo. In 1955, the predecessor (Tokyo Tsushin Kogyo) of Sony released Japan's first commercially produced transistor radio. Today Sony is a leading player in Entertainment (Music and Movies and Games), Semiconductors and Consumer Electronics. Our Bull case for Sony, from an investment thesis perspective, is for the company to revisit its corporate structure and set the Semiconductor (or ISS division), free on

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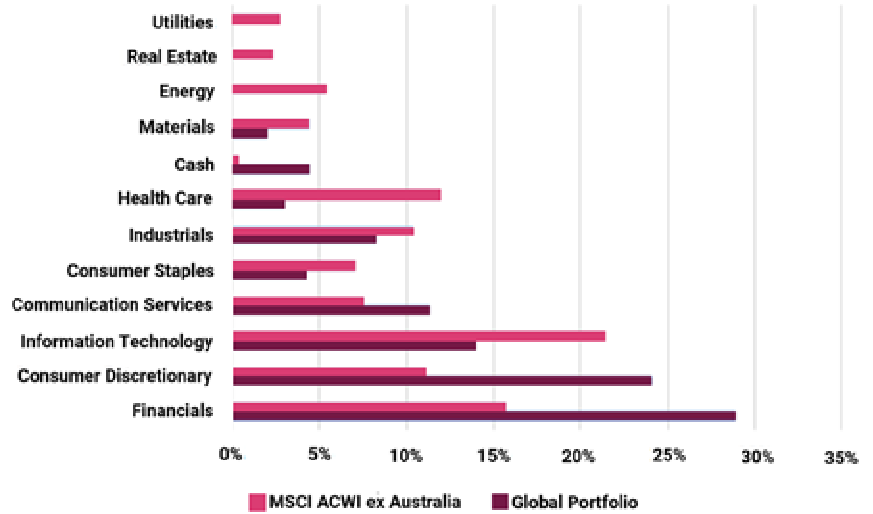
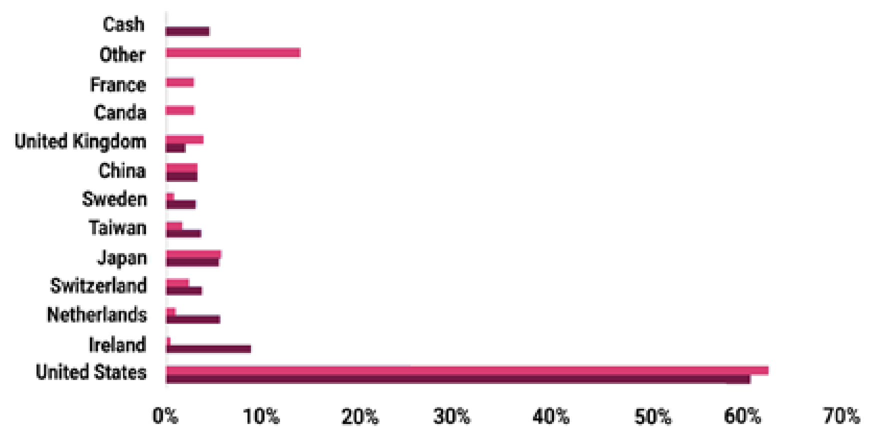
## Market Segments

### Oracle Global Portfolio v MSCI ACWI ex Australia




## Geographic Exposure




## Funds Under Management (since inception)

# Oracle Global Equities Portfolio Update

its growth path.

The ISS division is the world's leading player in image sensors, an industry no different to IC memory, that operates as an oligopoly and appears undervalued on a sum-of-the-parts (SoTP) basis and hence a potential value unlock for Sony shareholders if an ISS spin-off happens. In the meantime, our Discounted Cash Flow (DCF) valuation implies the stock is trading at ~30% discount to fair value.

The position in **Carrier Global** was initiated towards the end of August. The company is a leading player in heating, ventilation, air conditioning and refrigeration (or HVACR). The investment thesis for Carrier Global rests on energy transformation and the drive to zero carbon emissions, as well as the structural change in the company, moving from a cyclical company to a more structural company because they acquired Viessmann in Germany. The Viessmann acquisition moves the company into a larger focus on heat pumps, which offer several advantages over other systems including air conditioners (energy efficiency, heating capability, versatility, and cost savings). Viessmann provides energy and climate solutions with 22 production centres in 12 countries – although German-based, more than 55% of revenue is generated outside Germany. The product portfolio of Viessmann is across the HVACR spectrum, including solar photovoltaic, battery storage, hot water, grid, and energy management. This solution set, particularly the solar PV and battery storage, and particularly in Europe, is likely to be high growth as Europe seeks to achieve energy security and reduce reliance on Russian gas.

The position in **Nvidia** was initiated late in the Q. It is never easy to open a position in a stock that has appreciated ~250% in the last 12 months. However, we go back to our previous quarterly newsletter and the quote from Philip Fisher:" – *If the growth rate is so good that in another ten years, the company might well have quadrupled, is it really of such great concern whether at the moment the stock might or might not be 35% overpriced?*

Our Nvidia investment thesis focused on the high level of Research and development (R&D) to sustain the company's leading position in discrete graphic processing units (GPUs), the core technology in modern computer graphics and accelerated computing. Whilst gaming has been a key value driver for Nvidia (in the past), we expect artificial intelligence (AI) to emerge as the next key value driver – advanced large language models (LLMs) require significant memory and computing power to train and operate that clusters of powerful GPUs are necessary.

Another key aspect of our investment thesis is how Nvidia has been expanding its accelerated computing ecosystem in which hardware, software and solutions are brought together to create unique value for the markets/verticals served by Nvidia. As such, the company has emerged with Industry-leading margins, which we believe it can sustain over the medium to longer term, compared to AMD and Intel, the two primary competitors in CPU and GPU (not that CPU is a focus area for Nvidia). Finally, there is the impressive allocation of capital with a sound balance sheet, intensive R&D programs, and appropriate shareholder distribution.

Besides the three new positions in Sony, Carrier Global and Nvidia in the Quarter under review, we added to the Global portfolio's weighting in Yum China (YUMC).

It was the attractive valuation of Yum China that caught the eye –the investment case is very much about the KFC rollout. On the outlook, the company is guiding for between 1,000 and 1,300 new stores in 2023 (calendar and financial). Impressively, the company continued to roll out stores throughout the Covid-19 pandemic and now has 55% more stores than in 2019. With hindsight, the initial purchase of Yum China two and a half years ago (May 2020) was not well timed, and it was only in the Quarter under review that the stock started to deliver a positive relative (against the benchmark) performance.

The Global portfolio had two exits in the Quarter under review. Both stocks were within the "slow growers" basket of the portfolio, to borrow from Peter Lynch.

In the case of Bristol-Myers Squibb, reasons we decided to exit, despite the huge potential for a value unlock, included 1) the resignation of the CEO in the midst of executing a five-year plan; 2) the pace with which one blockbuster drug (Revlimid) is losing sales due to loss-of-exclusivity (LoE), which caught the company (and us by surprise); 3) disappointing growth rates in new drugs; and 4) slow growth now becoming no growth in 2023 as per most recent guidance. In short, the "boxes" for our investment thesis had more "crosses" than "tick marks".

Our second exit was General Mills. Simplistically speaking, there are two reasons why a stock does not compound and outperform (relative) its benchmark – 1) bought at the wrong price (little or no margin of safety compared to the fair value); and 2) the playbook as per investment thesis goes belly up. It is fair to say we bought General Mills at the wrong time which makes for a challenge to compound and outperform the benchmark.

| Top 10 Performers | Portfolio Position | 3 month Performance |
|---|---|---|
| Universal Music Group N.V. | 2.89% | 20.5% |
| Carrier Global Corp. | 2.11% | 14.5% |
| Alphabet Inc. Class A | 6.04% | 12.9% |
| Costco Wholesale Corporation | 4.20% | 9.4% |
| Adobe Incorporated | 2.80% | 7.5% |
| NVIDIA Corporation | 1.01% | 6.1% |
| Berkshire Hathaway Inc. Class B | 5.12% | 6.0% |
| Mastercard Incorporated Class A | 4.53% | 4.0% |
| JPMorgan Chase & Co. | 4.17% | 3.5% |
| EXOR N.V. | 2.69% | 2.9% |

# Oracle Global Equities Portfolio Update

| Portfolio Overview | |
|---|---|
| **Investment Manager** | Oracle Investment Management Pty Ltd |
| **Investment Objective** | To provide investors with long-term capital growth and tax effective income. The portfolio aims to outperform its benchmark over a rolling 7-year period. |
| **Investment Strategy** | To use active bottom up stock selection, focusing on buying quality securities at reasonable prices. The securities are assessed as meeting our investment criteria of strong earnings growth and as likely to provide attractive returns to investors. |
| **Benchmark** | MSCI ACWI ex Australia in A$ (unhedged) |
| **Investment Universe** | Primarily large cap international securities listed on major international exchanges. Portfolio may invest in listed ETFs. |
| **Recommended Investment Period** | 3-5 years |
| **Minimum Initial Investment** | $50,000 |
| **Inception Date** | 1 March 2016 |

| Portfolio Characteristics | Portfolio | Index |
|---|---|---|
| Price Earnings Multiple | 22.1 | 17.5 |
| Historical -EPS growth - 3 years | 19.7% | 10.6% |
| 12-month Forward Earnings Growth | 10.7% | 21.0% |
| Forward - EPS Growth - 3 years | 19.0 | 13.5% |
| Price Earnings Forward - 1 year | 20.0% | 14.5 |
| PEG Ratio | 2.7 | 0.83 |
| Divident Yield | 1.4% | 2.7% |
| Return on Equity (RoE) | 24.6% | 12.3% |
| Beta | 1.04 | 1.03 |
| Number of Constituent | 30 | 2,352 |

*Please see the Important Information disclaimer on the back page.*

# Oracle Australian Equities Portfolio Update

**George Kurian**
Portfolio Manager

**The Australian Equities Portfolio returned -3.71% for the September 2023 quarter, underperforming the benchmark S&P/ASX 100 Accumulation Index by -3.0%.**

*"Markets can remain irrational longer than you can remain solvent"* - John Maynard Keynes

The Keynes irrationality quote above is an apt reminder to us about the long history of the irrationality of Mr Market. And true to that past track record, markets have been on an irrational tour this quarter, especially in September. However, there was a method to its madness this time around. Interest rate-sensitive stocks which were severely marked down for about 18 months now, were once again marked down. The key reason is that markets are continuously increasing interest rate expectations, even after having large repricing of rate expectations over the past 20 months or so. However, as per the International Monetary Fund, Global headline Inflation is expected to decline from 8.7% in 2022 to 6.8% in 2023 and 5.2% in 2024. The core inflation is also forecasted to decline over the next two years. While the actual inflation numbers are anyone's guess, given slowing global growth and aggressive central banks, we expect the inflation and interest rates to trend down over the next two years.

What do you do when Mr Market becomes moody and pessimistic and turns bargains into super bargains? Like any smart family on shopping trips, we stock up. Hence, we have been buying high-quality stocks at very large discounts. Due to the rising rates, the markets have not only decreased the growth expectations of quality stocks but also reduced the expected excess return duration of those stocks. In most market environments, high-quality stocks such as we have in the portfolio, trade at premium prices.

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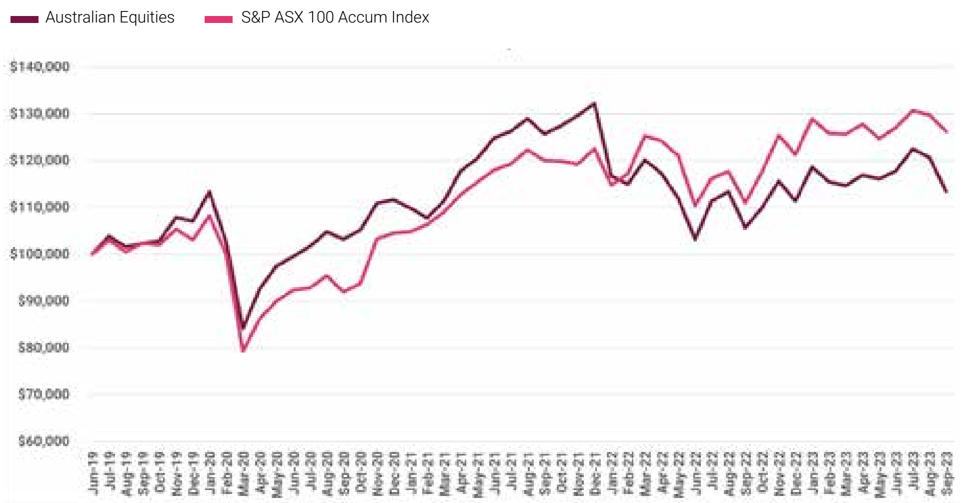
## Portfolio Performance

| Rolling | Australian Equities Portfolio | Benchmark (S&P ASX 100 Accumu Index) | Outperformance |
|---|---|---|---|
| 3 month | -3.71% | -0.71% | -3.00% |
| 6 month | -1.09% | 0.47% | -1.56% |
| 1 year | 7.32% | 13.68% | -6.36% |
| 2 year p.a | -5.00% | 2.54% | -7.54% |
| 3 year p.a | 3.19% | 11.14% | -7.95% |
| Since Inception p.a (1 July 2019) | 3.00% | 5.62% | -2.62% |

*Benchmark data is of S&P/ASX200 Accumulation Index prior to 1/7/2022.*

## Comparative Performance

### Australian Equities vs S&P ASX 100 Accum Index (since inception)




## Funds Under Management (since inception)

Nevertheless, due to the market's fixation on high rates, and its extrapolation of current high rates into perpetuity, we can buy these high-quality stocks at very attractive prices and yields, and 'de facto' lock-in attractive returns for the future. Hence unlike the Keynesian speculator alluded to in the quote above, who gets worried when the markets become irrational, we have been actively welcoming market irrationality by building up key stock positions.

### BOUGHT

**Block (SQ2):** A great example of our buy-the-fear process in action was in Block. Block, which is run by ex-Twitter CEO Jack Dorsey, has two major business lines Cash App and Square. Cash App is now a financial supermarket in the US with 54 million monthly transacting active users, and Square is now a payment processing and software service provider with operations in the US, Australia, the UK, and many other European Countries. When we took the initial position in May, we estimated that the market was only capturing the near-term cashflows, but not the large growth option of the outer years. This is because Block is not an ordinary business, but an exceptional business with large value in the 'tail' because of its highly scalable, high fixed costs and low variable costs business model. However, with the recent sell-off, the market is now not even capturing the near-term cashflows accurately to calculate the fair value of the Block. To understand Block's valuation now, no telescope is needed, even sleepy eyes will do. Hence, we have increased our position in Block and made it a top-10 position in the portfolio.

**Incitec Pivot (IPL)**: In the last quarterly letter, we asked whether 1+1 <1 for Incitec Pivot. Yes, said the nutty Mr Market at the time. No, says the professor Mr Market now. If you recall, Incitec has two divisions viz. the Explosives division and the Fertilizer division. Due to the difficulties with the Fertilizer division, the market valued the entire company below the valuation of the Explosives division itself. This inefficiency is now being progressively corrected and the stock has since re-rated. However, there was a time lag between Mr. Market moving from foolish to the sagehood phase and so we were able to top-up our initial Incitec positions at 1+1<1 prices.

**ResMed (RMD)**: Voila!! The world will be finally cured of that heavy burden multitudes carry in their Abdomens and Posteriors! At least that is the view of sellers who have sold down ResMed to multi-year lows. Their logic is as follows: The new weight loss-esque drugs like Ozempic and Wegovy, would mean no need for ResMed's Sleep Apnea devices. Once people become hale and hearty, they sleep like babies, so who wants a cabled mask that pumps air into your nose in the middle of the night? The problem with these bear arguments is that these drugs are not primarily designed for weight loss, they are for diabetic patients who are severely overweight to control their blood sugar levels. The weight loss is just a secondary benefit as the drug suppresses the appetite. Moreover, these drugs have moderate side effects ranging from nausea and diarrhea to more severe ones like pancreatitis and suicide ideation. Medical experts reckon only about 10-15% of weight loss comes from these medications, and patients will put the weight back on if they ever come off these drugs (not to mention the increased incentive to feast for the palate addicted). Many cases of Sleep Apnea are not linked to obesity but to bone structure and genetics. Moreover, the cost of these drugs is estimated to be about US$16,000 per annum vis-à-vis a one-off cost of US$1000-1500 plus consumables for ResMed's Airsense 11. Most health insurers in the US are still not covering this weight loss medication. Given that ResMed's valuation multiple significantly shrunk due to this weight loss scare, we have significantly increased the position in this stock.

**Atlas Arteria (ALX)**: What do you do when a $200bn giant stalks an Aussie with French Connection? We piggyback. The suitor is the Aussie infrastructure giant IFM. The target is Atlas Arteria. IFM has now taken a nearly 23% stake in Atlas as a prelude to a full takeover. Atlas also has several other drivers such as attractive valuation, leverage to falling rates due to its long-term contracts, inflation-adjusted toll road pricing, and concession extension/modification potential for the toll road APRR in France. Atlas also has about a 7% safe dividend yield, and so it is as if we are paid to wait for the courtship to begin. Hence, we initiated a new position in Atlas this quarter.

**CSL Limited (CSL):** CSL sold off after their half-yearly results. This was primarily because their guidance for FY24 was below the lofty consensus expectations. The key reason was the slow return to normal after COVID in its Behring business (about 63% of total revenues) as fees paid to blood donors were still at elevated levels when compared to historical levels. Markets were also worried about the generic competition in the recently acquired Vifor business (iron injectables). However, we view these as very short-term issues. There is some time lag between the blood taken and the blood used in CSL's Immunoglobulin products. Moreover, CSL has an enviable pipeline with about a dozen new products in late-stage trials, which if approved, would be launched over the next 4 years. This includes 3 potential blockbuster candidates such as a second heart attack prevention drug, a calcification inhibitor of arteries, and an expansion of their existing blood coagulation drug into trauma-related bleeding indication. Hence, we consider this sell-off as a rare buying opportunity in one of the top 3 biotechs in the world, and so have made CSL our largest portfolio position.

**WiseTech (WTC)**: Does patience pay in the stock market? It certainly did with WiseTech. After we bought WiseTech earlier in the year, the stock raced away to new highs without giving us the chance to build a full position. Hence, for months we were on the sidelines wistfully wondering whether we would get a second chance. Indeed, the patience paid off as we got a second chance to build a full position in WiseTech, as it sold off after the FY23 results due to short-term margin issues from the recent acquisitions. However, these acquisitions are strategic as they expand WiseTech's reach into new verticals such as rail supply chain management and intermodal logistics. We think adding these domains makes the 'network effect' stronger in their main CargoWise software. Hence, we added to our position.

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# Oracle Australian Equities Portfolio Update

## SOLD

**Washington H. Soul Pattinson (SOL)**: Soul Pattinson has been a great performer for the portfolios and gave a defensive bulwark for a long time. However, in that defensive process, it became offensively overvalued. Despite the many attractively valued stocks in the market at this cyclical low point, it took some strength in our soul to swap Soul given that it is the brainchild of the Milner family, one of the most famous investing families in Australia.

**Commonwealth Bank (CBA)**: While CBA has provided attractive returns to the portfolio for a long time, it is now the most overvalued big bank on ASX. CBA, notwithstanding its high-quality management team, would likely struggle to show major upside to their profit estimates especially now as their net interest margins have peaked and as high interest rates are now likely to cause increased loan arrears. We have been reducing the overvalued banks for a while now, and moving into the undervalued REIT sector, where stocks are still trading at a significant discount to their net asset values.

**BHP (BHP)**: With more than 10% weight in major ASX indices, 'The Big Aussie' towers above all other stocks on ASX. However, this also exposes the Achilles heel of Indices. These BHP-laden indices are sure to severely decline if BHP were to ever enter an iron ore bear market. We are now close to precisely such a scenario, as we have now more and more indications that Iron ore prices have peaked for this cycle. Iron ore prices are now oscillating between the US$100-120 levels, and even the promises of Chinese property stimulus have failed to sustainably increase iron ore prices. Meanwhile, iron ore supply, which is predominantly from the Aussie majors, is increasing at about 3% p.a. and demand is likely to see flat growth at best. Hence, we are likely to see an iron ore 'surplus' in 2023 and 2024. In the long term, with increased supply from new mines like Simandou in Africa, iron ore is likely headed into a serious downturn. Hence, we have significantly reduced our exposure to BHP when compared to the major indices.

**APA Group (APA)**: We sold out of APA over our concerns that gas is just a transition fuel and lack of growth opportunities in their core gas networks would incentivize management to pursue senseless acquisitions outside of their competencies. This exit proved timely as APA subsequently announced a deal to purchase Alinta's power assets in Pilbara for about $1.8bn funded by a mix of shares and debt, and the stock has significantly de-rated now.

**Suncorp (SUN)**: We exited Suncorp after the Australian Competition and Consumer Commission blocked the deal to sell Suncorp Bank to ANZ. While ANZ is appealing the decision, we believe it is now very difficult to overturn the decision. Moreover, Suncorp has ridden the premium hike cycle very well over the past 12 to 18 months, and we think most of the premium upside is now priced into the stock. Hence, we choose to rotate into more undervalued stocks.

**Cochlear (COH)**: Cochlear is one of the most innovative Australian companies. While we are great fans of Aussie innovation in the portfolio, Cochlear's ace 30% run this year had to be balanced with our conservative valuation sensibilities. The growth rate for this 'Steady Eddy' stock accelerated this year due to clearance in COVID backlogs. These backlogs are now mostly cleared, and so the EPS growth rate should mean revert to a mid-teens. As the stock is trading at high multiples and not discounting the imminent slowdown, we decided to exit the stock.

**ANZ Group (ANZ)**: ANZ rebounded from the deeply oversold levels earlier this year, and so we took the opportunity to trim some of the position to fund other buys.

In the market downturns, it is easy to lose focus. While we were well ahead of the indices Year to date (YTD) till the end of August, at the end of September we are behind. This is because, notwithstanding the gains for the year, we chose to build some major positions such as ResMed and Block, which we think were significantly undervalued. However, Mr Market disagreed and marked down those two positions, along with some other rate-sensitive names in the portfolio. It is important to note that we initiate positions with an aim towards outperforming over rolling 3- and 5-year time periods. If we don't initiate new positions when the markets are selling off, the short-term performance would look good, but this would significantly lower the long-term returns of the portfolio. An analogy would be the game of Cricket, where top teams continue to play their game irrespective of some quick wickets in the middle order. Hence, we have been batting for you looking for undervalued situations in the stock market irrespective of Mr Market's extreme mood swings. Given the quality of stocks available and the attractive pricing of these stocks due to the current fear in the market, we remain confident about the future returns.

| Top 10 Performers | Portfolio Position | 3 month Performance |
|---|---|---|
| Carsales.com | 1.54% | 19.8% |
| Cochlear | 1.25% | 18.2% |
| Altium | 1.06% | 17.7% |
| Domino's Pizza | 3% | 15.7% |
| Incitec Pivot | 5.06% | 13.8% |
| REA Group | 0.94% | 9.8% |
| Wesfarmers | 2.39% | 9.8% |
| ANZ Group | 3.78% | 8.2% |
| Santos | 1.39% | 7.8% |
| Goodman Group | 2.24% | 6.6% |

# Oracle Australian Equities Portfolio Update

## Portfolio Overview

| | |
|---|---|
| **Investment Manager** | Oracle Investment Management Pty Ltd |
| **Investment Objective** | To provide investors with tax effective income, dividends and capital growth. The Portfolio aims to outperform its benchmark over a rolling 3 to 5 year period. |
| **Investment Strategy** | To use active stock selection to invest in quality businesses. The businesses are assessed as meeting our investment criteria of a high return on equity, growth potential and their ability to consistently deliver dividends to investors. |
| **Benchmark** | S&P/ASX 100 Accumulation Index |
| **Investment Universe** | Companies listed on the ASX that have a market capitalsation similar to those in the S&P/ASX 100 Accumulation Index. |
| **Recommended Investment Period** | 3-5 years |
| **Minimum Initial Investment** | $25,000 |
| **Inception Date** | 1 July 2019 |

| Portfolio Characteristics | Portfolio | Index |
|---|---|---|
| Price Earnings Multiple | 22.1 | 17.4 |
| Earnings per share growth (3-year CAGR) | 22.6% | 15.9% |
| Long term earnings per share growth | 9% | 7% |
| Return on Equity (ROE) | 9.8% | 11.7% |
| Dividend Yield | 3.9% | 4.4% |
| Operating Margin | 22.3% | 17.2% |
| Gearing (Debt/EBITDA) | 2.6x | 1.8x |

*Please see the Important Information disclaimer on the back page.*

# Oracle Emerging Companies Portfolio Update

**Jack Magann**
Portfolio Manager

**The Emerging Companies Portfolio returned 4.46% for the third quarter of 2023. This compares to our benchmark, the S&P ASX Small Ordinaries Accumulation Index, which was down -1.94% over the same period. This equates to outperformance of our benchmark by 6.40%.**

We have discussed previously that the Small Companies universe is in a prime position for active managers. After investors moved up the market cap spectrum in 2022, or out of equities altogether, we were left with high-quality small-cap companies trading at heavily discounted prices. The chart below highlights that the gap between small and large caps is yet to close. With reporting season in August, we had strong returns from our companies that beat expectations, which led to our outperformance in the market. With the index lagging our portfolio we are seeing companies that we don't own starting to look very interesting from a valuation perspective. We expect to add new positions to the portfolio over the next few months. We are also looking to add to some of our existing positions which we believe remain undervalued.

*Credit: Spheria Asset Management*

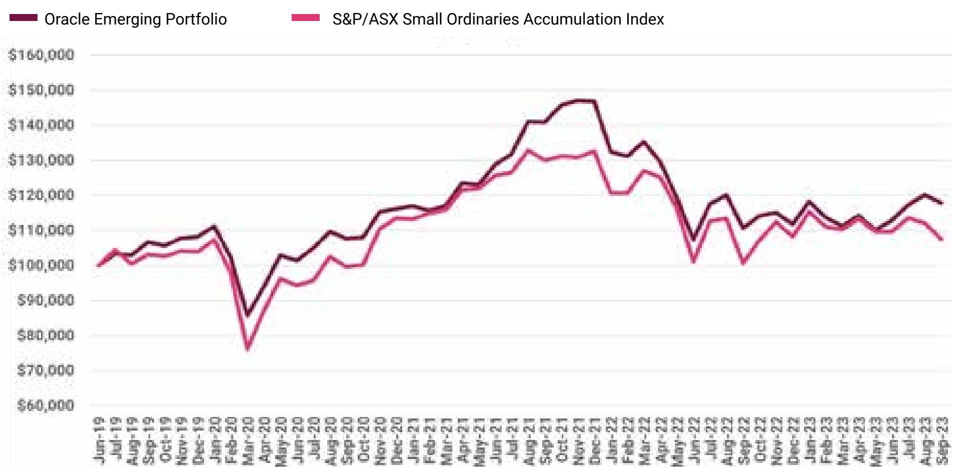
*Continued over the page*

## Portfolio Performance

| Rolling | Emerging Companies Portfolio | Benchmark (S&P/ASX Small Ordinaries Accumulation Index) | Outperformance |
|---|---|---|---|
| 3 month | 4.46% | -1.94% | 6.40% |
| 6 month | 5.95% | -2.47% | 8.42% |
| 1 year | 6.49% | 6.84% | -0.35% |
| 2 year p.a | -8.53% | -9.04% | 0.51% |
| 3 year p.a | 3.06% | 2.57% | 0.49% |
| **Since Inception p.a (1 July 2019)** | **3.95%** | **1.73%** | **2.22%** |

## Comparative Performance

### Emerging Companies vs S&P/ASX Small Accum Index (since inception)




## Funds Under Management (since inception)

# Oracle Emerging Companies Portfolio Update

**Aussie Broadband** was one of our best results during reporting season and the share price rose 38% during the quarter. Since listing in 2020, Aussie has grown from being unprofitable with 100,000 customers to recording 700,000 customers and making a profit of $37m in FY23. This is a high-quality management team that continues to execute.

The difference between Aussie and the big players in broadband, such as Telstra, Optus & TPG, has been Aussie's ability to win the high margin customers. They have achieved this through providing high-quality customer service to customers seeking out high-speed broadband. It is difficult to comprehend how customer service can provide such a moat for Aussie Broadband as they continue to win market share from their larger competitors. However, when you think about the size of Telstra and Optus, transforming the culture in the customer service departments of these two companies would be an immense job. As Aussie has focused on creating this culture from the beginning, it is embedded in the company allowing them to outperform their peers over the past 4 years.

Aussie has also moved into two new segments in recent years, business and enterprise. This shifts the risk away from Australia's revenue and profits being concentrated on the residential broadband market. As Aussie has now completed its fibre rollout nationally, the business and enterprise businesses can utilise this and produce higher margins than the residential business.

In early October Aussie made a bid to buy **Symbio**, a company we have previously owned, at a value of $271m. The bid centres around Aussie bringing Symbio's tier-1 network into the company to better service their enterprise and wholesale customers. This could see Australia's enterprise and wholesale business become 50% of group EBITDA. If the bid is successful it is expected to be accretive to earnings within 1-year.

We have faith in this founder-led management team that they will continue to execute the company's growth plans, providing strong returns for shareholders.

We have had two companies within the portfolio receive takeover offers during the quarter, being Pacific Current and Energy One.

We increased our position in **Pacific Current (PAC)** by 3% during the September quarter. This decision was made after the company received a takeover offer from Regal Funds Management, which was quickly followed by an announcement from GQG Partners that they also intended to make an offer. We thought there could be a bidding war between the two firms for Pacific Current as GQG has vested interests in making this deal, however, Regal has now pulled out of the bid.

We believe GQG will still make an offer as PAC owns 4% of GQG, after funding their setup in 2016. The CEO of PAC is also an independent director on the GQG board, so the companies have a strong history. Given that PAC manages GQG's fund distributions in the US, GQG would be unwilling to see this company sold to another party, placing their business model at risk.

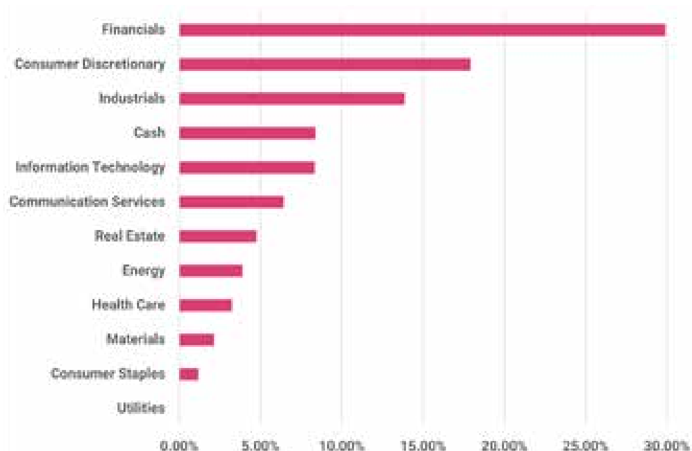
Another factor in GQG's willingness to take over PAC will be the liquidity in their stock. As it stands GQG's liquidity is low, due to high inside ownership, preventing it from entering the major indices on the ASX. If they were to buy PAC, they could then sell the 4% stake of GQG shares that PAC owns into the market, increasing liquidity and potentially the stock price.

*Continued over the page*

| Top 10 Performers | Portfolio Position | 3 month Performance |
|---|---|---|
| Energy One Limited. | 0.87% | 83.96% |
| Baby Bunting Group Ltd. | 1.26% | 57.67% |
| Pacific Current | 4.14% | 36.50% |
| Aussie Broadband. | 3.12% | 37.92% |
| Karoon Energy Ltd. | 2.36% | 34.01% |
| Kip McGrath Education Centres. | 1.40% | 32.63% |
| Pro Medicus Limited. | 2.17% | 27.30% |
| Seven Group Holdings. | 6.59% | 27.30% |
| Premier Investments. | 2.44% | 23.40% |
| Yancoal Ltd. | 1.55% | 20.96% |

| Portfolio Characteristics | Portfolio | Index |
|---|---|---|
| Price Earning Multiple | 17.9 | 15.2 |
| Forward earnings per share growth (1 year) | 9.5% | 5.5% |
| Earnings per share growth (3-year CAGR) | 10.3% | 9.7% |
| Return on Equity (ROE) | 9.6% | 6.1% |
| Dividend Yield | 3.7% | 2.07% |
| Dividend Growth | 7.5% | 1.77% |
| Gearing (Net Debt/EBITDA) | 1.67x | 2.06x |

## Sector Breakdown



# Oracle Emerging Companies Portfolio Update

PAC disclosed to the market that they believe a "fair" net asset value (NAV) for the group to be $11.92. This NAV is based on fair value estimates used by PAC on investments that are held on their balance sheet at historical cost. A bid at or above this price would provide a return of >20% for shareholders.

The second takeover offer received was for **Energy One**, a provider of energy trading software that has a big tailwind behind them as the race to net zero heats up. With new, smaller, energy projects like wind and solar farms coming online, Energy One's software will be required for these projects to sell energy into the wholesale market. This is why it is no surprise that Energy One has received a takeover offer from STG, a global investment firm.

While we are happy with the 44% premium offered in the takeover bid, we wouldn't be unhappy if the company remained on the ASX. This company will scale well from here as it increases its services globally and the operational leverage of the company gains momentum. While the share price of Energy One was up 84% to the end of the quarter, we believe there is still value to be extracted for shareholders. We do note that the due diligence period for STG has been extended twice by Energy One and are awaiting an announcement from the company this week.

## BOUGHT

**Pacific Current Group - Add 3.0%**

We increased our position in Pacific Current (PAC) by 3% during the quarter. The group had received a takeover offer from Regal Funds Management. The takeover announcement from Regal was quickly followed by an announcement from GQG stating they intended to make an offer for Pacific Current Group. Given that Pacific Current Group manages GQG's fund distributions in the US, GQG would be unwilling to see this company sold to Regal and risk its business model. PAC management also mentioned on their earnings call that there are now more than two interested bidders and expect final offers by mid-October. It looks like we are now in a bidding war and given NAV is estimated at $11.92 per share, we should see 15%+ returns from here. Pacific Current Group is now one of our largest holdings at 4.5%.

## SOLD

**Adairs Limited - Full Sell**

We took the opportunity to sell out of Adair's during the quarter after the share price bounced back after the sell-off in consumer discretionary companies. While the bad news may be priced into the company, we believe that poor trading conditions in-home product retailers will persist throughout FY24.

**Argosy Minerals - Full Sell**

A small lithium miner in the salt lakes of Argentina. Operations have taken slower than expected to ramp up and we are seeing a similar them across all lithium brine producers. Given these difficulties and the small scale of Argosy's potential production, we sold out of our position during the quarter.

**Core Lithium - Full Sell**

A small lithium miner in the Northern Territory. The company announced during the quarter that the grade of lithium that has initially been mined is lower than forecast. This has caused problems with the company as they will be unable to meet the obligations of a term sheet they signed with Tesla.

**Nick Scali Limited - Full Sell**

As with Adair's, we took the opportunity to sell out Nick Scali during the quarter after the share price bounced back after the sell-off in consumer discretionary companies. Given that Nick Scali has higher priced items than Adair's they may be hit harder during the consumer spending slowdown. In saying that, Nick Scali has a great history of producing high returns on capital so we wouldn't be surprised to see the company back in the portfolio in future.

**Smartgroup Corporation - Trim -3%**

Smartgroup has been one of our best performers in 2023, but we believe the share price may have run ahead of the business fundamentals. Smartgroup is a low-growth company operating in a mature industry. We have held on to a 2% position in Smartgroup as there is a tailwind with new government EV incentives in novated leasing and the capital-light nature of the business allows them to payout a high dividend ratio.

## Portfolio Overview

| | |
|---|---|
| Investment Manager | Oracle Investment Management Pty Ltd |
| Investment Objective | To provide investors with long-term capital growth and tax effective income. The Portfolio aims to outperform its benchmark over a rolling 3 to 5 year period. |
| Investment Strategy | To use active stock selection to invest in quality businesses. The businesses are assessed as meeting our investment criteria of high return on equity and earnings growth and as likely to provide attractive returns to investors. |
| Benchmark | S&P/ASX Small Ordinaries Accumulation Index |
| Investment Universe | All companies listed on the ASX plus managed funds. The Portfolio will include a range of mid-sized capitalization companies. |
| Recommended Investment Period | 3-5 years |
| Minimum Initial Investment | $10,000 |
| Inception Date | 1 July 2019 |

*Please see the Important Information disclaimer on the back page.*

# Oracle Fixed Interest Fund Update

**Ashley Cox**
Portfolio Manager

**The Oracle Fixed Interest Fund gained 2.18% for the quarter ended 30 September, outperforming the benchmark gain of 1.26%. The month of September, pleasingly, saw the fund gain 0.57% during a difficult period for fixed income, as the benchmark fell 0.58%.**

Interest rates moved higher during the quarter. Oracle investors benefit from these higher moves as the fund is invested predominately in Floating Rate Notes. This means that as rates continue to rise, the coupons we receive also move higher. Driven by global central banks guiding the market that further rate rises are likely to be required, the market accepted the likelihood that rates would remain "higher for longer". Inflation concerns dominated, sending Australian 10-year yields 0.46% higher and US 10-year yields 0.73% higher for the quarter.

Higher rates drove a general "risk off" theme in most asset classes globally, with the S&P500 Index dropping 4.87% in September, and the tech-heavy NASDAQ down 5.81%. Despite this, major bank-subordinated bonds were keenly sought, with prices rising over the quarter. This price increase benefits Oracle, as we maintain significant holdings in these bonds. As noted below, we took advantage of this strength to sell some subordinated bank bonds that had performed very well, and to make room for future new issuance, which we expect to come at higher interest rates.

In such an environment, it is pleasing that the Oracle Fixed Interest Fund has produced such strong positive returns for investors.

August saw a large number of fixed income issues from the banks. A weaker Australian dollar encouraged several offshore banks to issue bonds in the local market, at premiums to the domestic banks. NatWest Markets priced a 5-year $600m Senior Unsecured deal @ Bank Bill Swap Rate +1.73%, an initial yield of 5.875%.

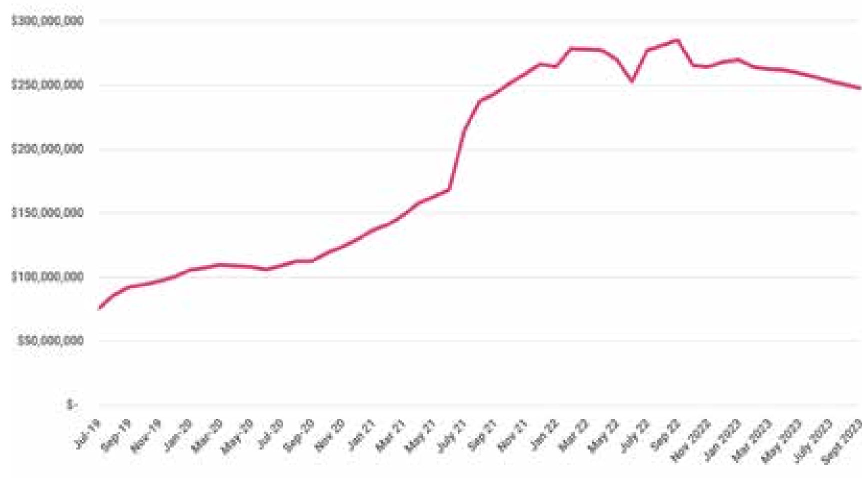
*Continued over the page*

## Portfolio Performance

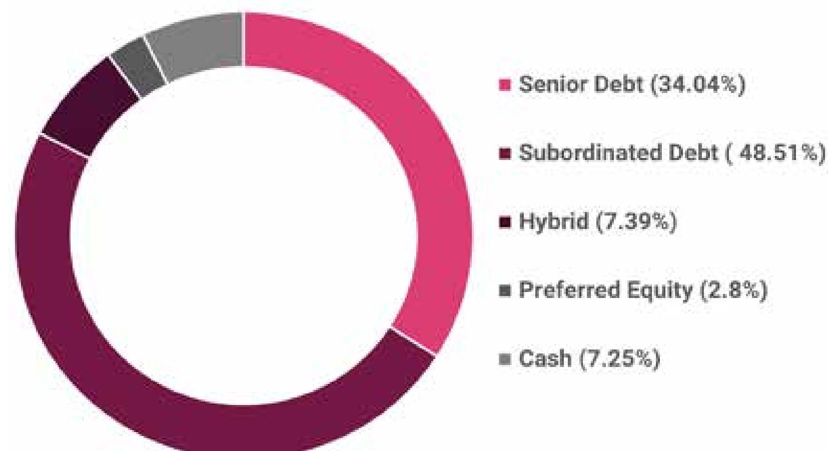
| Rolling | Fixed Interest Fund | Benchmark (Bloomberg Ausbond Credit 0+Y Index) | Outperformance |
|---|---|---|---|
| 3 month | 2.18% | 1.26% | 0.92% |
| 6 month | 3.29% | 0.10% | 3.19% |
| 1 year | 4.59% | 4.69% | -0.10% |
| *Since Inception (1 Dec 2021) | 0.73% | -1.79% | 2.52% |

**The Fixed Interest Fund performance data is from 1 December 2021*

## Funds Under Management




## Bond Type by Weight



# Oracle Fixed Interest Fund Update

Suncorp came to the market late in September, issuing a $600m Floating Rate Note with a 2034 maturity, but callable in 2029 at a margin of 2.35% over 3 3-month Bank Bill Swap Rate. The first coupon was set at 6.489%. We maintain the view that rates will remain higher for longer, and as such, this bond fits well with our strategy of buying quality floating-rate securities, that benefit as rates remain high, or continue to rise.

During the month we executed the trades below:

**BOUGHT**

- We continue to add to our existing position in NUFARM FINANCE (NZ) LIMITED, a junior subordinated perpetual note, offering a coupon of 3.9% above BBSW. The running yield on this bond is around 8.75%
- We have been adding to our holding in Centuria Fund 2, senior bonds offering a floating rate coupon of BBSW + 4.25%. The current running yield on these bonds is around 8.50%.
- We bought the above-mentioned Nat West Markets, a senior unsecured bond, offering a floating coupon of BBSW + 1.73% for A-rated debt. The current running yield on these bonds is 5.87%.
- Bank of Queensland Tier 2 Subordinated debt (callable 19 May 2027) – we added to our existing position at a discount to par, running yield of just over 6.00% (BBSW +1.75% coupon).
- We bought BNP Paribas Tier 2 Subordinated Floating Rate Note at a yield to call of roughly 7.00%, with around 3 years to call date.
- We participated in the Suncorp Tier 2 Floating Rate Note paying a coupon of quarterly BBSW + 2.35%

**SOLD**

- Macquarie Bank Capital Notes 3, Floating rate Hybrid
- Societe Generale 4.875 Fixed rate Perpetual AT1 Subordinated (Callable 12 Dec 24)
- BNP Paribas 4.50 Fixed rate Perpetual AT1 Subordinated (Callable 10 Jan 25)
- UBS Group AG 4.375 Fixed rate Perpetual AT1 Subordinated (Callable 27 Aug 24)
- We continue to take advantage of market liquidity to reduce our Australian Unity fixed-rate perpetual bond position.
- We sold a small holding in AMP subordinated Floating Rate Note, opting to exit ahead of the November call date.
- We sold CBA April 2032 Tier 2 subordinated Floating rate note taking advantage of elevated market levels
- We sold NAB August 2032 Tier 2 subordinated Floating rate note taking advantage of elevated market levels
- Sold Credit Union Australia Feb 2027 Senior FRN, had performed well, and was yielding roughly 5.50%, we saw better buy opportunities.

| Top 10 Holdings | Weight |
|---|---|
| RABO 7.074 10/26/32 '27 FRN | 5.73% |
| Ampol Limited 02 Dec 81 FRN (Call 19 Mar 2027) | 5.37% |
| CBA 14 Apr 32 FRN (Call 14 Apr 27) Sub | 4.74% |
| Avanti 22 Nov 25 FRN (Call 22 Nov 23) Senior Sec | 4.31% |
| Latitude Group | 4.22% |
| AMP Bank Ltd 07 Oct 32 FRN (Call 07 Oct 27) Sub | 4.11% |
| Heartland Australia Group Pty Ltd | 4.04% |
| LIBERTY FINANCIAL PTY 05 Apr 27 | 3.60% |
| Newcastle Coal Infrastructure Group (NCIG | 3.59% |
| Suncorp 01 Dec 38 FRN (Call 01 Dec 28) | 3.19% |

| Portfolio Overview | |
|---|---|
| Investment Manager | Oracle Investment Management Pty Ltd |
| Investment Objective | To provide a return comprised of a secure and predictable income stream with moderate capital growth. The Portfolio aims to outperform the Bloomberg AusBond Bank Bill Index on an annual basis. |
| Investment Strategy | To invest in credit securities from companies with strong management, and balance sheets that display characteristics such as sufficient liquidity and low levels of gearing. Diversification is achieved mainly through investment in securities across a range of industries. |
| Investment Universe | The Portfolio will primarily comprise of Australian Fixed Income including corporate bonds, listed sub-debt, listed hybrids, term deposits and cash. Dependent on market conditions the Portfolio may also invest in international corporate bonds and government bonds. |
| Recommended Investment Period | 3 years |
| Minimum Initial Investment | $25,000 |
| Inception Date | 1 December 2021 |

*Please see the Important Information disclaimer on the back page.*

# Oracle Property Securities Portfolio Update

**Jack Magann**
Portfolio Manager

**The Oracle Property Securities Portfolio returned -3.20% for the quarter. This compares to our benchmark, the S&P/ASX 300 Property Trust Index, which returned -3.04%. Listed property had shown signs of bouncing back at the start of the quarter after a trying 18 months. However, investor optimism dwindled in September as bond yields climbed higher with rate cut expectations being pushed back.**

Goodman was in our top three performers during the quarter as they released positive FY23 results. The group reported that operating earnings increased 16%, compared to the previous financial year. Goodman discussed in their earnings release that they are significantly under market value in their leases in the US, Australia and Europe due to high demand in the industrial sector. Given rental contracts are coming up for review this will provide an uplift to group earnings moving forward.

Goodman also announced a strategic plan to move strongly into data centres. The group is planning to have 3GW of capacity by the end of FY24 and 4GW the year after. For context, this is more than 10x the current capacity of NextDC. Around 30% of the group's $13bn WIP is already in data centre projects, so Goodman is wasting no time entering this space.

In early September we entered a new position in **Charter Hall Social Infrastructure REIT** (CQE). CQE has 77% of its property in the childcare sector with the remaining in government-backed social buildings, e.g., TAFE's and government medical centres.

The decision was made to take a position in CQE as they trade at a 33% discount to NTA. This compares to the pure play childcare REIT of ARF which trades at an 8% premium.

*Continued over the page*

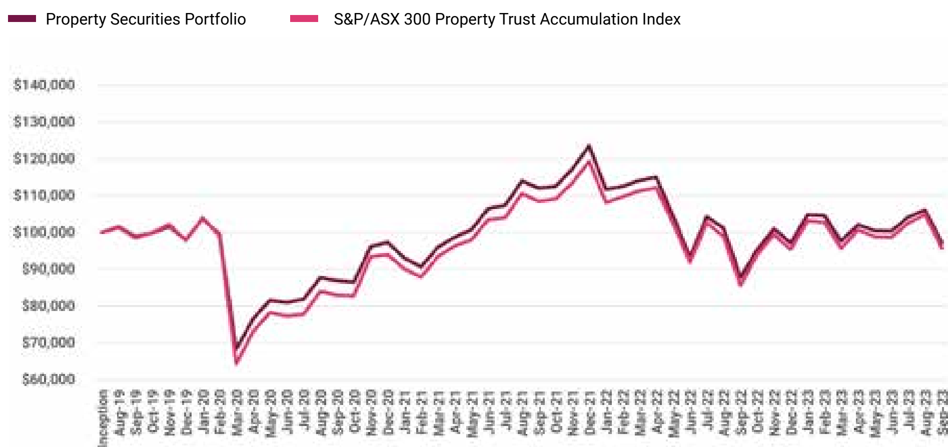
## Portfolio Performance

| Rolling | Property Securities Portfolio | Benchmark (S&P/ASX 300 Property Trust Accum Index) | Outperformance |
|---|---|---|---|
| 3 month | -3.20% | -3.04% | -0.16% |
| 6 month | -0.48% | 0.02% | -0.50% |
| 1 year | 10.67% | 11.95% | -1.28% |
| 2 year p.a | -6.85% | -6.03% | -0.82% |
| 3 year p.a | 3.81% | 4.89% | -1.08% |
| Since Inception p.a (1 August 2019) | -0.68% | -1.04% | 0.36% |

## Comparative Performance

### Property Securities vs S&P/ASX 300 Property Trust Accum Index

(since inception)




## Funds Under Management (since inception)

# Oracle Property Securities Portfolio Update

Should there be such a big valuation gap between the two because CQE has 23% of property outside of childcare? We don't believe so given the quality of tenant in the other 23% of the portfolio (the government always pays their rent). We believe the gap between ARF and CQE will close, with CQE moving closer to book value. Over what time period this will occur is unknown, but we are happy to collect the 6% p.a. dividend yield while we wait.

We discussed our decision to add to **Abacus Property Group** during the last quarterly newsletter. At the time we said:

*One position in our portfolio is what we call a "special situation" investment. The upcoming de-stapling of Abacus Property Group (ABP) is expected to play out in the third quarter of 2023. The Abacus Property Group REIT is made up of two portfolios, one being commercial office and retail, and the second being the self-storage property business, Storage King.*

*As it stands Abacus Property Group is trading at a 27% discount to their net tangible assets (NTA). Management plans to create shareholder value by de-stapling the storage portfolio (with the ASX code - ASK) and listing it as its entity. The price of the new ASK REIT has been set at a 10% discount to NTA, so we have already seen 50% of the ABP portfolio close the gap to NTA from 27% to 10%. With the only other pure-play storage REIT on the ASX, National Storage REIT, trading at a 4% discount to NTA we could see this gap close further.*

The de-stapling has now occurred, and the two REITs are trading as separate entities. While it is early days there has so far been no closing of the gap between share price and Net Tangible Assets (NTA) as both REITs have drifted down with the overall property index.

The commercial office portfolio now trades at a 50% discount to Net Tangible Assets. Despite the negative talk around office space occupancy and further devaluations expected, this discount is too high due to the evidence in recent commercial office property being sold, which has been completed between 10-20% discounts to book value. This is a big variance between the 50% discount we are currently paying for ABG's portfolio.

The Storage King REIT has declined since listing and is now trading at a 31% discount to Net Tangible Assets. This compares to key competitor National Storage, which now trades at a 12.5% discount to Net Tangible Assets. We believe Storage King has a superior portfolio to National Storage as they have a stronger concentration of properties in major cities, where land and space is scarce. Given the tailwinds behind self-storage properties (Australia is one of the highest urbanised countries in the world and population growth is forecast at record levels), we think the discount of 12.5% for National Storage is fair compared to what ASK is trading at.

We continue to believe our thesis will play out in the coming months. It may take some patience to realise value in this trade, but we are happy to wait given the upside on offer for shareholders.

*"The stock market is designed to transfer money from the active to the patient,"* Warren E. Buffett.

### BOUGHT

**Charter Hall Social Infrastructure REIT (CQE) – BUY 2%**

### SOLD

**Centuria Industrial REIT (CIP) – FULL SELL**

We sold out of CIP to fund our buy of Charter Hall Social Infrastructure REIT. Considering we have large exposure to industrial property through Goodman, we decided to sell out of Charter Hall Social Infrastructure REIT as we wanted to gain exposure to childcare property within the portfolio.

## Portfolio Overview

| | |
|---|---|
| **Investment Manager** | Oracle Investment Management Pty Ltd |
| **Investment Objective** | To provide investors with long-term capital growth and income.<br>The portfolio aims to outperform its benchmark over a rolling 3 year period. |
| **Investment Strategy** | To use active bottom up stock selection, focusing on buying quality companies at reasonable prices. The securities are assessed as meeting our investment criteria of strong earnings growth and as likely to provide attractive returns to investors. |
| **Benchmark** | S&P/ASX 300 Property Trust Accumulation Index |
| **Investment Universe** | Listed ASX Securities that invest in and or Manage Property Investments. Portfolio may invest in listed ETFs. |
| **Recommended Investment Period** | 3-5 years |
| **Minimum Initial Investment** | $25,000 |
| **Inception Date** | 1 August 2019 |

# Oracle Property Securities Portfolio Update

| Portfolio Characteristics | Portfolio | Index |
|---|---|---|
| Price/Funds From Operations Multiple | 13.3x | 13.9x |
| Funds From Operations Per Share Growth – 3 year avg | 0.02% | 0.03% |
| Return on Equity (ROE) | 15.3% | 14.8% |
| Return on Equity (ROE) – 3 year avg | 13.7% | 13.3% |
| Dividend Yield | 7.1% | 6.9% |
| Dividend Growth – 3 year avg | 0.2% | 0.1% |
| Gearing (Debt/Equity) | 38.6% | 44.7% |
| Price to Book (forward estimate) | 0.92x | 0.91x |

| Top 5 Performers | Portfolio Position | 3 month Performance |
|---|---|---|
| HealthCo Wellness REIT | 1.90% | 11.79% |
| Ingenia Group | 1.20% | 6.98% |
| Goodman Group | 30.07% | 6.88% |
| Dexus Industria | 1.45% | 1.18% |
| RAM Essential Services Property Fund | 1.83% | 0.88% |

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# Oracle Ethical Balanced Portfolio Update

**Luke Durbin**
Portfolio Manager

**For the quarter ended September 2023, the Ethical Balanced Portfolio returned 0.24%, which is 1.18% higher than the Morningstar Balanced benchmark, which returned -0.94% for the quarter.**

In what has been a very tumultuous quarter for equity markets worldwide, we are pleased to have ended the quarter in positive territory when most equity and fixed income indices have ended the quarter negative.

Performance for the quarter was centred around the communications and discretionary sectors, with utilities, information technology, and real estate being the biggest drag on performance.

Information Technology has been the best performing sector in markets this year so it is somewhat not surprising to see it take a breather. In the case of the portfolio, it has been our small position in SolarEdge Technologies (SEDG-US) that was the main contributor to the negative performance in the sector.

**SolarEdge (SEDG-US)** has come under pressure as a result of new legislation in California that has changed the credit that solar owners in the state receive for exporting their excess energy onto the grid. The new regime is a highly variable credit system with the credit received dependent on the time of day, month, and year, more closely aligning the scheme to economic supply and demand factors. On the face of it, it looks like a reduction, but when used in conjunction with a smart battery that can determine the optimum time that energy should be consumed compared to exported, a resident can benefit from the new system. This has been articulated by management but has been lost on the market, as has the fact that Europe is flying as a result of the desire to improve energy security across the continent.

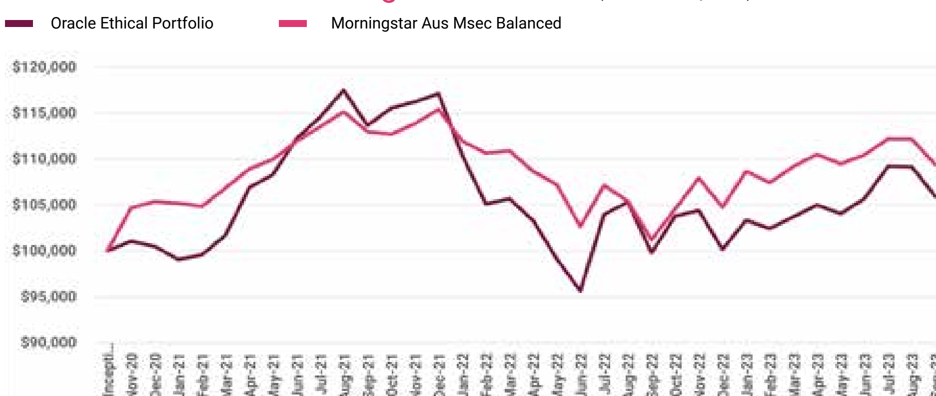
## Portfolio Performance

| Rolling | Ethical Balanced Portfolio | Benchmark (Morningstar Balanced) | Comparative Performance |
|---|---|---|---|
| 3 month | 0.24% | -0.94% | 1.18% |
| 6 month | 2.17% | 0.19% | 1.98% |
| 1 year | 6.15% | 8.08% | -1.93% |
| 2 year p.a | -3.46% | -1.60% | -1.86% |
| **Since Inception p.a (1 November 2020)** | **2.00%** | **3.13%** | **-1.13%** |

## Comparative Performance

### Ethical Balanced vs Morningstar Balanced (since inception)

Oracle Ethical Portfolio | Morningstar Aus Msec Balanced




We added to the position near the end of July and if the share price continues to fall, we believe the company will represent even better value than it does today and we will add further.

Our utilities exposure is solely represented by **Brookfield Renewable (BEPC-US)**, a leader in the renewable energy space with diversified revenue streams across the world and energy technologies such as hydro, wind, and solar. Brookfield Renewable has a long track record of generating returns for shareholders via their target of producing double digit growth in funds from operations (FFO). A proxy for cash flow that is widely used by real estate trusts and infrastructure companies – as well as 6% growth in the dividend. To date, we have not seen anything that suggests 2023 will be the first year for them to not achieve this. The most likely reason for the sell-off is the recent rapid rise in bond yields. Infrastructure companies like Brookfield tend to be viewed as "bond proxies" by the market, which means, that when the company has a steady yield (which BEPC does, as discussed above), the company is priced like a bond, so when competing yields increase, the yield on these bond proxies must also increase. For yields to increase prices must decrease. This makes it attractive for new buyers but is unfortunate for current holders as their yield remains at their buy price and are faced with a capital loss, at least temporarily.

Worth a brief comment, too, is **ResMed (RMD-AU)**, whose share price has come under pressure recently. ResMed reported strong revenue growth in August, however, the gross margin was lower than expected. This spooked the market into a large drawdown.

*Continued over the page*

# Oracle Ethical Balanced Portfolio Update

The market also seems to be concerned about the potential impact that weight-loss drugs such as Ozempic could have, since Ozempic treats both diabetes and is known to reduce weight, both of which are afflictions that also impact those with sleep apnea. The market may also be concerned about Philips, a competitor of ResMed who had a massive product recall a few years ago. Philips is likely to re-enter the market soon, potentially undercutting ResMed on price to regain market share. All of this is contributing to a lower share price for ResMed. Our view is that the market remains massive for sleep apnea sufferers and ResMed continues to have a very compelling offering. Diabetes and obesity are only a segment of ResMed's customers and are not the only cause of sleep apnea anyway. It also may take Philips years to regain the trust of consumers after such a disastrous recall (just ask Cochlear who went through the same thing over a decade ago). We view this as an opportunity to buy a wonderful company at a good price.

On a positive note, **Kip McGrath Education Centres (KME-AU)**, part of the Consumer Discretionary sector, enjoyed a rebound after underperforming for most of the year, ending the quarter as the best performer. The market has been sceptical of its US expansion, via the acquisition of Tutorfly, following revelations that competition in their markets was a lot fiercer than they expected, requiring heavier levels of investment. While Tutorfly still made a loss for the year, it was more than made up for in the strength of the corporate centre business and a strong outlook with contracted sales in the US more than doubling for the FY24 year. While fiscal 2023 ended as another year of overpromise and underdeliver for the company, the opportunity is large for KME to continue expanding both locally and overseas and now has the technology stack to do so with little incremental investment required.

The next best performer is a relative newcomer to the portfolio in **Pro Medicus (PME-AU).** Pro Medicus provides cloud-based image storage and visualization software to radiologists. The key benefit of the software is that it "streams" the diagnostic images as the user views them, rather than downloading the entire set at once, which both enables the medical professionals to view images remotely and saves immense amounts of time because the large and full data sets are not downloaded in completion, only on an as needed basis per image. Pro Medicus is founder led and has one of the most consistent sales growth records on the ASX. And there appears to be plenty of growth still in its future, which is the subject of this quarter's strong performance: a 10-year US$140 million contract for their software. It is these sorts of contracts that enable the company to have net profit margins of nearly 50%, and returns on invested capital of nearly 70%, both of which have been steadily growing. This sort of quality does not come cheap with an eye watering forward price/earnings multiple of about 109x, however, when viewed with a long horizon and valuing the business based on free cash flows, it looks more reasonable than you might otherwise think.

We tend to dedicate most of the space in the quarterly newsletters to the equities portion of the portfolio because there is more to talk about.

However, in September we made several changes to the fixed income component of the portfolio, which we believe will be to the benefit of investors.

## BOUGHT

**Metrics Master Income Trust (MXT-AU)**

Metrics Credit Partners are specialists in private credit investing, constructing funds for investors and lending this capital to private Australian companies to grow their businesses. Metrics is the largest non-bank lender in the country, providing an alternative avenue for exposure to Australian corporate lending outside of the banks. Metrics Credit Partners is the listed vehicle for Metrics in the form of a listed investment company (LIC), which means ASX investors can access Metrics funds simply by buying shares on the ASX. Metrics Credit Partners invests these funds across a range of its credit funds, which pay out regular income to investors. Performance has been strong, outperforming its target of an RBA cash rate of +3.25% since inception in 2017. The Ethical portfolio bought a 4% position in Metrics Credit Partners.

**Nufarm Finance Floating Rate Note Perpetual (NFNG)**

Nufarm has been in the portfolio for some time, however at only a 2% position. Nufarm is a leading manufacturer of agricultural products such as crop protection and innovative seed technology products, which are key enablers to more efficient food production and will be critical to ensuring food stability in the coming decades of population growth. Nufarm has made large strides in its sustainability, including aligning with the United Nations' Sustainable Development Goals such as World Hunger, Responsible Consumption, and Life on Land. Nufarm is paying a coupon of 7.66%, which is the highest in the portfolio. Through the quarter we doubled our position to 4%.

## SOLD

**Macquarie Bank Ltd Capital Notes 2020 (MBLPC)**

These Macquarie Bank hybrids have been trading at a premium to their face value (of $100), which means investors who buy today are receiving a lower yield than the coupon payment and investors who bought the notes at face value have made a capital gain. We believe the notes are likely to be called by Macquarie in December 2025, and if they are called, holders at the time will be forced to sell and receive the face value of $100. This reduces the yield on the notes considerably – by our calculations by about 2.7% per annum – and would make it one of the lowest-yielding fixed-income securities in the portfolio. Macquarie Bank hybrids were sold to make way for the higher-yielding securities discussed above.

**ANZ Capital Notes 2021 - Floating Rate (AN3PI)**

AN3PI currently has a net yield of 5.12%, which makes it the lowest-yielding security in the fixed-income sleeve of the portfolio. These hybrids were sold to fund higher-yielding securities discussed above.

# Oracle Ethical Balanced Portfolio Update

| Portfolio Overview | |
|---|---|
| Investment Manager | Oracle Investment Management Pty Ltd |
| Investment Objective | To provide investors with long-term growth and to outperform the Consumer Price Index + 3% over the medium term (5 years). |
| Investment Strategy | To invest across a broad range of investment sectors and to provide a balance between capital growth and capital preservation. Oracle use an active bottom up stock selection process, focusing on buying quality securities at reasonable prices. The securities are assessed as meeting both our investment criteria of strong earnings growth and ethical criteria of positive social, environmental and governance factors. |
| Investment Universe | Listed ASX Securities, cash, ETF's, corporate bonds, short term money market securities, international securities, listed sub-debt, listed hybrids and listed property investments. |
| Recommended Investment Period | 5 years |
| Minimum Initial Investment | $50,000 |
| Inception Date | 1 November 2020 |

| Top 10 Performers | Portfolio Position | 3 month Performance |
|---|---|---|
| Kip McGrath Education Centres | 1.4% | 28.5% |
| Pro Medicus | 1.3% | 25.7% |
| Universal Music Group | 2.5% | 20.5% |
| Bapcor | 1.6% | 15.5% |
| Alphabet Class C | 4.1% | 12.9% |
| Airbnb | 2.9% | 12.7% |
| Laserbond | 1.9% | 12.2% |
| REA Group | 2.1% | 9.8% |
| Wesfarmers | 0.6% | 9.8% |
| Costco Wholesale Corp | 3.3% | 9.4% |

| Selected Investment Holdings | Ethical Theme | Weighting |
|---|---|---|
| Darling Ingredients | Waste Minimisation | 1.7% |
| Franklin Electric | Clean Water | 3.1% |
| Euronext | European market infrastructure | 1.4% |
| SolarEdge Technologies | Smart Solar Inverters | 1.5% |
| Vertex Pharmaceuticals | Cystic Fibrosis Treatment | 2.5% |
| Brookfield Renewable Corp | Renewable Energy | 2.9% |
| AirBNB | Accommodation Platform | 2.7% |
| Rockwool | Energy Efficient Buildings | 1.2% |

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# Diversified Managed: Capital Stable Portfolio

The Capital Stable Portfolio suits investors seeking a diversified portfolio that invests primarily in defensive assets with low volatility, reliable yield and a focus on capital preservation.

Investors in this portfolio are forgoing the potential for higher returns over the long term for relative security.

| Asset Class | Neutral |
|---|---|
| Cash | 10% |
| Fixed Income | 60% |
| Property Securities | 5% |
| Aus Emerging Companies | 0% |
| Aus Equities | 15% |
| Global Equities | 10% |

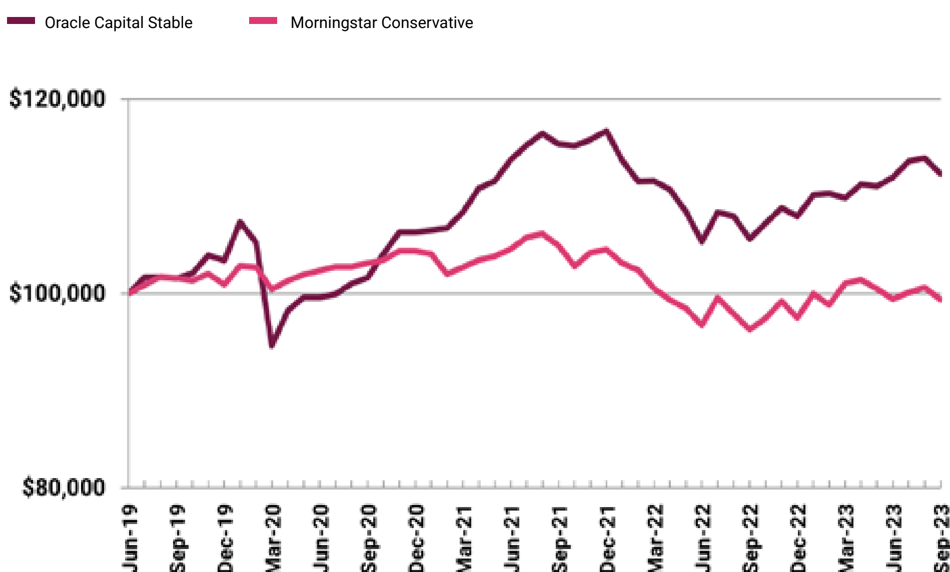
| Investment Fee (% per annum) | |
|---|---|
| Capital Stable Portfolio | 0.6% |

## Portfolio Performance

| Rolling | Oracle Capital Stable | Benchmark (Morningstar Aus Msec Conservative) | Comparative Performance |
|---|---|---|---|
| 3 month | 0.36% | -0.06% | 0.42% |
| 6 month | 2.29% | -1.66% | 3.95% |
| 1 year | 6.35% | 3.23% | 3.12% |
| 2 year p.a | -1.32% | -2.67% | 1.35% |
| 3 year p.a | 3.38% | -1.23% | 4.61% |
| Inception p.a. (1 July 2019) | 2.78% | -0.15% | 2.93% |

## Comparative Performance

### Oracle Capital Stable vs Morningstar Capital Stable (since inception)

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# Diversified Managed: Conservative Portfolio

The Conservative Portfolio suits investors seeking a diversified portfolio that invests primarily in defensive assets with low volatility, reliable yield and a focus on capital preservation.

Investors in this portfolio are foregoing the potential for higher returns over the long term.

| Asset Class | Neutral |
|---|---|
| Cash | 5% |
| Fixed Income | 50% |
| Property Securities | 5% |
| Aus Emerging Companies | 0% |
| Aus Equities | 25% |
| Global Equities | 15% |

| Investment Fee (% per annum) | |
|---|---|
| Conservative Portfolio | 0.65% |

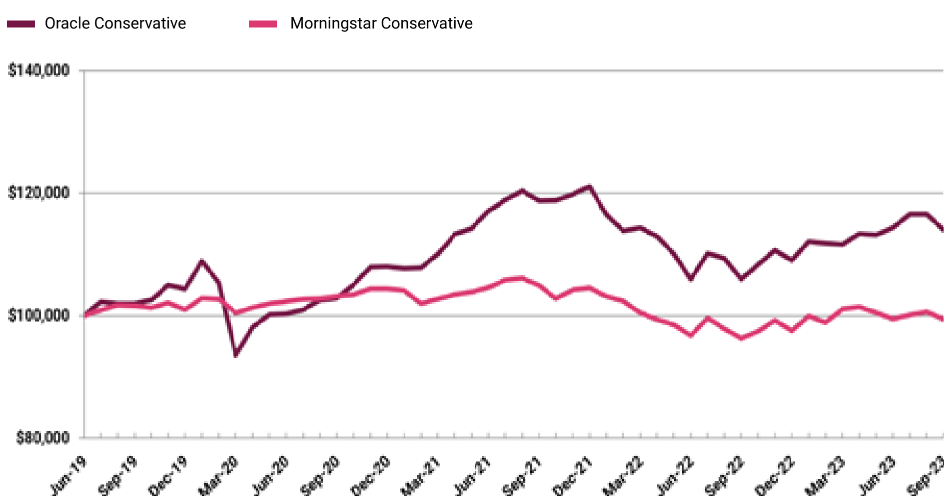
## Portfolio Performance

| Rolling | Oracle Conservative | Benchmark (Morningstar Aus Msec Conservative) | Comparative Performance |
|---|---|---|---|
| 3 month | -0.33% | -0.06% | -0.27% |
| 6 month | 2.12% | -1.66% | 3.78% |
| 1 year | 7.60% | 3.23% | 4.37% |
| 2 year p.a | -2.02% | -2.67% | 0.65% |
| 3 year p.a | 3.48% | -1.23% | 4.71% |
| Inception p.a. (1 July 2019) | 3.13% | -0.15% | 3.28% |

## Comparative Performance

### Oacle Conservative vs Morningstar Aus Msec Conservative

(since inception)

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# Diversified Managed: Balanced Portfolio

The Balanced Portfolio suits investors who require a balanced portfolio, diversified across all major asset classes, seek capital growth over the medium to long term with a moderate level of income, accept a moderate degree of volatility associated with a relatively higher exposure to growth assets and are prepared to invest for the minimum investment timeframe.

| Asset Class | Neutral |
|---|---|
| Cash | 4% |
| Fixed Income | 36% |
| Property Securities | 6% |
| Aus Emerging Companies | 9% |
| Aus Equities | 20% |
| Global Equities | 25% |

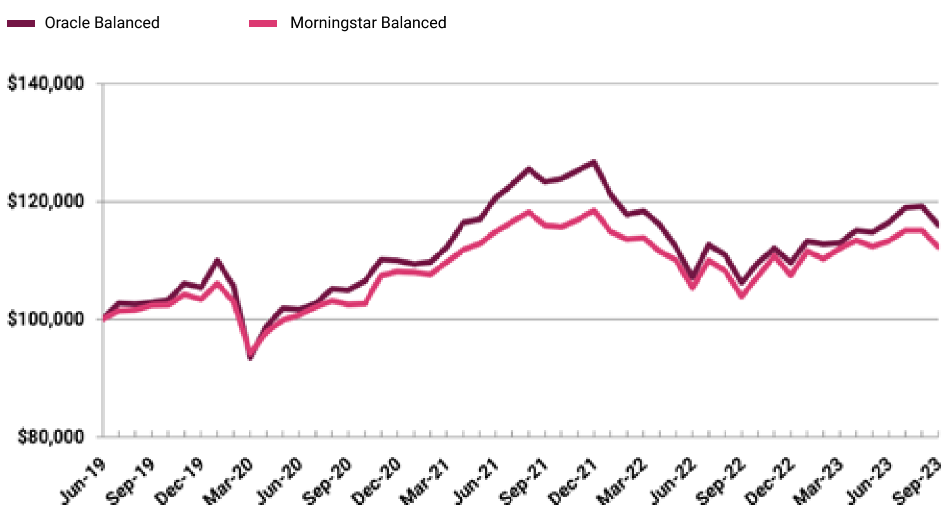
| Investment Fee (% per annum) | |
|---|---|
| Balanced Portfolio | 0.7% |

## Portfolio Performance

| Rolling | Oracle Balanced | Benchmark (Morningstar Aus Msec Balanced) | Comparative Performance |
|---|---|---|---|
| 3 month | -0.34% | -0.94% | 0.60% |
| 6 month | 2.75% | 0.19% | 2.56% |
| 1 year | 9.31% | 8.08% | 1.23% |
| 2 year p.a | -3.01% | -1.60% | -1.41% |
| 3 year p.a | 3.42% | 3.09% | 0.33% |
| Inception p.a. (1 July 2019) | 3.57% | 2.76% | 0.81% |

## Comparative Performance

### Oracle Balanced vs Morningstar Balanced (since inception)

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# Diversified Managed: Growth Portfolio

The Growth Portfolio suits investors who seek the potential for a relatively high level of growth and a modest level of income, accept a higher level of short-medium term capital volatility as a trade-off for long-term capital growth and are prepared to invest for the minimum investment timeframe.

| Asset Class | Neutral |
| --- | --- |
| Cash | 2% |
| Fixed Income | 24% |
| Property Securities | 10% |
| Aus Emerging Companies | 11% |
| Aus Equities | 19% |
| Global Equities | 34% |

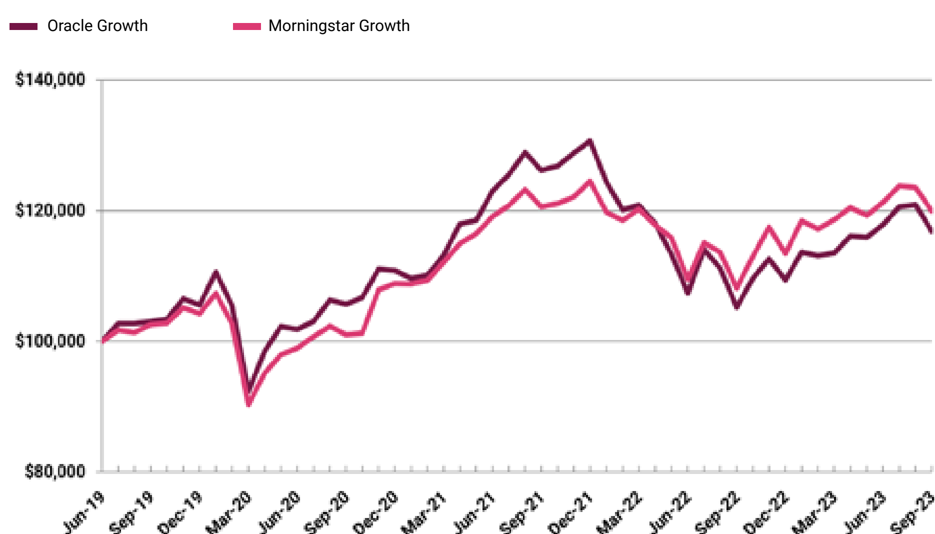
| Investment Fee (% per annum) | |
| --- | --- |
| Growth Portfolio | 0.75% |

## Portfolio Performance

| Rolling | Oracle Growth | Benchmark (Morningstar Aus Msec Growth) | Comparative Performance |
| --- | --- | --- | --- |
| 3 month | -0.86% | -1.05% | 0.19% |
| 6 month | 2.90% | 1.12% | 1.78% |
| 1 year | 11.06% | 10.92% | 0.14% |
| 2 year p.a | -3.78% | -0.28% | -3.50% |
| 3 year p.a | 3.40% | 5.89% | -2.49% |
| Inception p.a. (1 July 2019) | 3.73% | 4.38% | -0.65% |

## Comparative Performance

### Oracle Growth vs Morningstar Growth (since inception)

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# Diversified Managed: High Growth Portfolio

The High Growth Portfolio suits investors who seek a relatively high level of growth on investment capital, accept a high level of short-medium term capital volatility as a trade-off for long-term capital growth and are prepared to invest for the minimum investment timeframe.

| Asset Class | Neutral |
|---|---|
| Cash | 2% |
| Fixed Income | 0% |
| Property Securities | 10% |
| Aus Emerging Companies | 20% |
| Aus Equities | 24% |
| Global Equities | 44% |

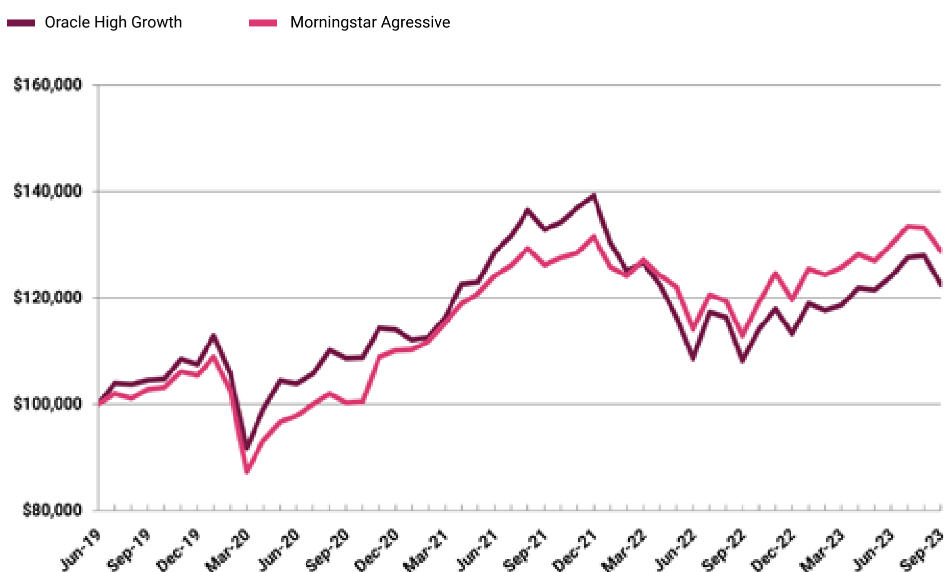
| Investment Fee (% per annum) | |
|---|---|
| High Growth Portfolio | 0.85% |

## Portfolio Performance

| Rolling | Oracle High Growth | Benchmark (Morningstar Aus Msec Aggressive) | Comparative Performance |
|---|---|---|---|
| 3 month | -1.30% | -1.03% | -0.27% |
| 6 month | 3.24% | 2.41% | 0.83% |
| 1 year | 13.21% | 14.12% | -0.91% |
| 2 year p.a | -3.99% | 1.03% | -5.02% |
| 3 year p.a | 4.07% | 8.70% | -4.63% |
| Inception p.a. (1 July 2019) | 4.88% | 6.13% | -1.25% |

## Comparative Performance

### Oracle High Growth vs Morningstar Aggressive (since inception)

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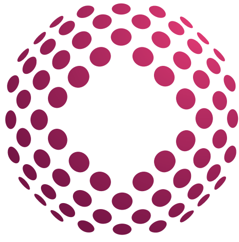

oracle
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## Responsible Entity & Issuer - Investment

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