eInvest Income Generator Fund (Managed Fund)

ASX: EIGA

Monthly Report December 2022

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	3 Years (% p.a.)	Since Inception^ (% p.a.)
Income Distribution	0.5	1.6	3.2	9.3	6.9	7.6
Capital Growth	-3.1	6.6	4.4	-6.0	-1.7	-2.1
Total Return	-2.7	8.2	7.5	3.3	5.1	5.5
Franking Credits#	0.1	0.2	0.4	3.2	2.7	3.2
Income Distribution including Franking Credits	**0.6**	**1.8**	**3.6**	**12.5**	**9.6**	**10.8**
Benchmark Yield including Franking Credits*	0.2	0.9	3.6	5.8	5.1	5.5
Excess Income to Benchmark#	**0.4**	**0.9**	**0.0**	**6.7**	**4.5**	**5.3**

^Inception date was 7 May 2018. Fund returns are calculated using net asset value per unit at the start and end of the specified period and do not reflect the brokerage or the bid ask spread that investors incur when buying and selling units on the ASX. *Benchmark yield is calculated based on the difference between the return of the S&P/ASX300 Franking Credit Adjusted Daily Total Return Index (Tax Exempt) and return of the S&P/ASX300 Index. #Franking credits are an estimate only, as tax components will only be known with certainty at the end of the financial year. Past performance is not a reliable indicator of future performance.

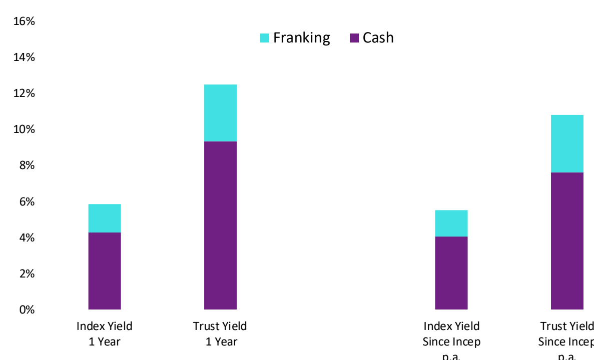
Overview

Markets ended the year on a soft note, with persistently high inflation and hawkish commentary, dashing hopes that Central Banks would pivot to a more accommodative stance and towards monetary tightening. This saw all major global markets finish the month lower, reversing much of the previous month's gains.

The Australian market was also weaker in December, with the ASX300 Accumulation Index finishing the month down -3.3%. All sectors delivered negative returns, however, the Metals & Mining sector (-0.8%) again performed best, driven by expectation of a pick-up in Chinese commodity demand as their economy reopens.

EIGA is currently targeting a 5% increase in FY23 net monthly distributions to 1.8 CPU. Based on the unit price at the start of the financial year, this equates to an annualised cash distribution yield of around 6.2% or 8.8%, including franking credits.

Distribution Yield



Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Fund Characteristics

The objective of EIGA is to provide investors with an attractive level of tax effective income, paid via monthly distributions. EIGA aims to provide a gross distribution yield, adjusted for applicable franking credits, above that provided by the S&P/ASX300 Franking Credit Adjusted Daily Total Return Index (Tax-Exempt).

Portfolio Manager
Stephen Bruce

EIGA FUM
$32 million

Distribution Frequency
Monthly

Inception Date
7 May 2018

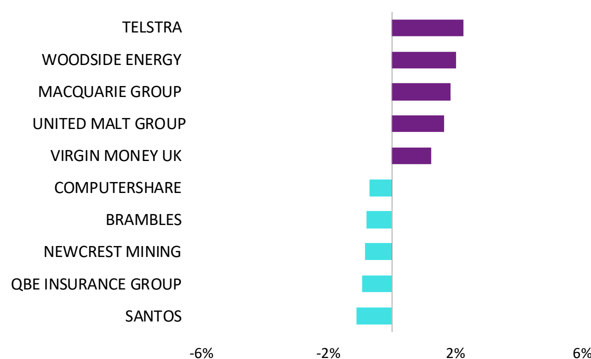
Fees
0.80% (incl. of GST and RITC)

Portfolio Characteristics – FY23	Fund	Market
Price to Earnings (x)	13.8	14.8
Price to Free Cash Flow (x)	13.0	13.4
Gross Yield (%)	6.2	5.5
Price to NTA (x)	2.7	2.8

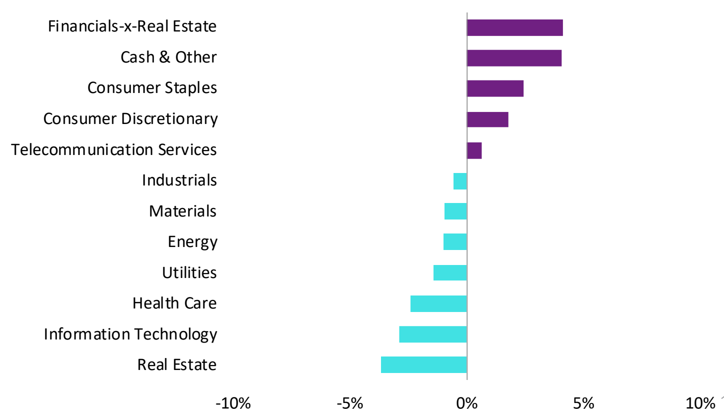
Source: Perennial Value Management. As at 31 December 2022

The above figures are forecasts only. While due care has been used in the preparation of forecast information, actual outcomes may vary in a materially positive or negative manner.

Top 5 Over / Underweight Positions vs Index



Sector Active Exposure vs Index



Fund Review

EIGA returned -2.6%, including franking credits and after-fees in December, outperforming the market by +0.7%. For the past 12 months EIGA has returned +6.5%, outperforming the market by +6.7%. This highlights the Fund's leverage to the value rotation currently underway as interest rates rise.

Key positive contributors to performance included the Fund's resources holdings, with the prospects of Chinese reopening seeing strong rallies in the prices of iron ore (+15.7%) and other commodities. This pushed the bulk miners higher, with Rio Tinto (+6.2%), Fortescue Metals (+5.8%) and BHP (+0.2%). These stocks have been very strong performers over the last 12 months, rising an average of +28.9%, compared to the market which declined by -2.6%.

Virgin Money UK (+7.9%) continued its recovery, as the political situation in the UK stabilised. We have previously written that, while the economic outlook in the UK is highly uncertain at present, the bank is well-positioned, with provisions for loan losses well above pre-COVID levels and significant surplus capital. Subject to regulatory approval, the company could potentially return up to GBP375m to shareholders in late 2023. This equates to around 15% of the current market cap of the company. Combined with the fact that the company is trading on less than 0.5x book value, then there is likely to be significant upside to the share price.

United Malt (+3.9%) continued the recovery which began with its full-year result last month. While, as expected, the result was very poor, it is clear the headwinds that the company has faced over the last several years from COVID-related lockdowns and supply chain disruptions, to the failure of the Canadian barley crop, are now behind them. As a result, earnings are expected to rebound strongly over the coming years. Further, the global malt industry is consolidating, mirroring the consolidation that has occurred amongst their brewer customers. It is highly likely that United Malt will be party to this at some point.

Telstra (+3.0%), outperformed over the month. We view Telstra very much as a stock for the times, offering a combination of solid defensive characteristics, a reasonable valuation and an attractive and sustainable dividend yield. Earnings growth has resumed following the completion of the NBN roll out, and the key mobiles market is increasingly rational, with the merger of Vodafone and TPG creating an oligopoly market structure.

The major banks declined over the month, falling an average of -4.0%. While operating conditions are currently positive, with expanding interest margins and strong credit quality, the market is looking ahead to when the economy begins to slow next year. While this will present headwinds to the banks, we note that they are all in very strong financial positions, with historically high levels of capital and large provisions for any increase in bad debts that may occur.

The main detractors over the month were stocks exposed to the consumer and the housing market. Gaming machine manufacturer, Aristocrat Leisure (-12.9%), was softer on the prospect of lower spending as the economy slowed. Building materials company, James Hardie (-9.6%), also declined as data showed that rapidly increasing US mortgage rates are crimping demand for new homes. However, we remain very confident on the longer-term outlook for these businesses, each of which is well-managed and holds a very strong position in its market.

Fund Activity

During the month, we reduced our holding in NAB, bringing our bank exposure back to index levels. Proceeds were used to add Transurban to the portfolio. At month end, stock numbers were 33 and cash was 4.1%.

Distribution

In order to provide a regular income stream, the Fund pays monthly distributions. We aim to pay equal cash distributions each month, based on our estimate of the dividend income to be generated over the year. Franking credits, surplus income and any realised capital gains will then be distributed, as per usual, with the June distribution.

Looking to the current financial year, while the economic outlook is more uncertain, most companies are in good financial shape, and we expect healthy dividends. The Fund is currently forecasting a 5% increase in FY23 monthly net cash distributions to 1.8 CPU. Based on the month end unit price, this represents an annualised cash distribution yield of 6.2% or 8.8%, including franking credits.

We do not expect the same level of off-market buy-backs or special dividends in the coming year compared to the high level seen in FY22, as many companies have now restored their balance sheets to their desired gearing ranges.

Outlook

Global growth is clearly slowing, as interest rates rise and economies grapple with the impacts of high inflation and energy supply problems. However, we believe that this will be offset to some extent by the benefits to economies as COVID disruptions continue to recede. While economic data is mixed, and varies greatly from region to region, unemployment rates are very low in most major markets. The Australian economy is performing particularly strongly and will continue to be a key beneficiary of the strength in commodity markets. However, there are a number of potentially significant changes in the global economic and political backdrop, from the return of inflation and the change in the interest rate cycle, to rising geopolitical tensions. As a result, the level of uncertainty is elevated, and a degree of caution is warranted.

This view is expressed in the portfolio through holding a combination of stocks with cyclical leverage, as well as stocks with solid defensive characteristics. Importantly, the portfolio is positively leveraged to improving growth, higher inflation, and rising interest rates. Within the cyclical part of the portfolio, this is achieved through overweight positions in the Resources, Financials and Consumer Discretionary sectors. In the defensive part of the portfolio, this is achieved through holdings in the sectors such as Telcos and Consumer Staples.

The Fund continues to offer a higher forecast gross yield than the overall market and, as always, our focus will continue to be on investing in quality companies with strong balance sheets, which are offering attractive valuations and have the ability to deliver high levels of franked dividend income to investors.

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