ROSEVALLEY FUNDS

Portfolio Report CY 2020

The Rosevalley Behavioural Finance Funds

The Rosevalley Behavioural Finance Funds are high-conviction funds that take the theoretical and empirical evidence developed over the past 30 years in Behavioural Finance, and systematically build portfolios from these learnings. The portfolios are constructed on a benchmark-unaware basis, but performance is compared to the ASX-200 accumulation index.

The year in review

2020 was the strangest year for stock markets in living memory. We saw both the steepest decline and the fastest recovery. In Australia, for the ASX-200, of all daily movements larger than 5% in the ASX-200 since the index was created, half were in the month of March 2020. By the end of the year, many markets around the world finished in positive territory, but this masked very different returns at the sector level: tech stocks performed extremely well, while most other sectors were flat to down.

Various Accumulation Indices

	Jan-Mar	Apr-Dec	CY2020
MSCI World	-20.5%	40.5%	11.7%
S&P 500	-19.6%	47.3%	18.4%
DJIA	-23.2%	39.6%	7.2%
FTSE100	-23.8%	16.1%	-11.5%
DAX	-25.0%	38.1%	3.5%
Hang Seng	-16.3%	15.4%	-3.4%
ASX200	-23.1%	31.9%	1.4%
Rosevalley 13/3	**-11.8%**	**47.9%**	**30.4%**
Source: Factset, Rosevalley			

The year started out well. Many stock markets reached all-time highs in February. But then the COVID-19 pandemic sent many economies in lockdown, and stock markets fell precipitously. However, the downturn was short-lived and what followed was a swift and strong recovery, at least when measured by overall index levels.

One can probably point to three drivers. First, both government and central banks around the world took massive, decisive steps to support their economies. These measures included, lower interest rates, large stimulus programmes, direct payments – all adding up to being the largest support packages in history. Second, the market recovery wasn't quite what it seemed: some sectors (tech, resources) performed very strongly, while others (travel, education) struggled. Finally, it should be noted that "the stock market is not the economy". In this case, the economic downturn was mostly felt by smaller businesses, while the stock market is (by its very nature) skewed to larger businesses.

Against the backdrop of the pandemic was the drama of the US presidential election. Curiously, all the twists and turns tended to be mostly ignored by the markets. Even when then-president Trump refused to concede when it was obvious that he had lost, even when (in January) his supporters stormed and briefly occupied the Capitol building, markets for the most part ignored it all.

Rosevalley Funds again in top-10 of all fund managers in Australia as measured by Mercer.

As usual, Mercer tabulated and ranked fund managers' performance for the year. We don't have access to the full list, but the AFR published the top-10 funds in the Mercer survey (see page 5).

- *The best performer returned 43.6%, and the second best 33.7%. Had the Rosevalley funds been part of the survey, Rosevalley 13/3 and 10/0 would have taken 3rd and 4th place respectively*.*
- *Rosevalley 15/5 would have been in 11th* place, if you include Rosevalley 13/3 and 10/0 in the ranking.*
- ***Rosevalley now has had its funds in the top-10 list for every June and December ranking that Mercer published since inception – one of only 2 fund managers to have done so. Over the combined CY19/20 timeframe Rosevalley 13/3 beat the other fund by 600 bps.***

*Note: Rosevalley's return are not audited. *Rosevalley 13/3 returns are achieved net returns; Rosevalley 15/5 and 10/0 net returns are proforma on the assumption of the same gross-net gap as Rosevalley 13/3.*

Performance as of December 2020								
Portfolio		1 month	3 months	6 months	1 year	Since inception annualized (1 Oct 2018)	Since inception annualized (14 Aug 2018)	Since inception annualized (1 Aug 2018)
Rosevalley 13/3	Gross	9.4%	1.4%	13.9%	30.4%	18.6%		
	Net	9.5%	2.1%	14.3%	26.5%	15.9%		
Rosevalley 15/5	Gross	9.2%	-0.9%	10.6%	26.5%		16.7%	
	Net[1]							
Rosevalley 10/0	Gross	8.4%	19.7%	26.0%	28.8%			22.7%
	Net[2]	7.5%	16.7%	19.7%	13.8%			8.7%
ASX-200		1.2%	13.7%	13.2%	1.4%	6.3%	5.9%	5.9%

Source: Rosevalley, Factset. Note returns are not audited. [1]Rosevalley 15/5 was not actively traded during the month, so no net numbers are available. [2]Rosevalley 10/0 is traded on a demonstration basis – as a result of its small size commissions are a large proportion of assets, which explains the large gap between gross and net returns.

Portfolio performance

The Rosevalley portfolios ended the year with very strong performance. On a gross basis, all portfolios showed significant absolute performance, as well as outperformance relative to the index and against peers. Even on a net basis, while performance was negatively impacted by the small size of the portfolios, performance was far in excess of the broader market:

- The flagship portfolio (Rosevalley 13/3) returned 30.4% gross and 26.5% net.
- Rosevalley 15/5 returned 26.5% gross. It wasn't actively traded, but we estimate that, if the size had been similar to the 13/3, the net performance would have been 22.6%.
- Rosevalley 10/0 returned 28.8% gross and 13.8% net. This portfolio is the smallest of the three – we estimate net return would have been around 24.9% if the size had been larger.

For a discussion on a stock-specific level, we refer to the Rosevalley 13/3 portfolio (see chart on page 3).

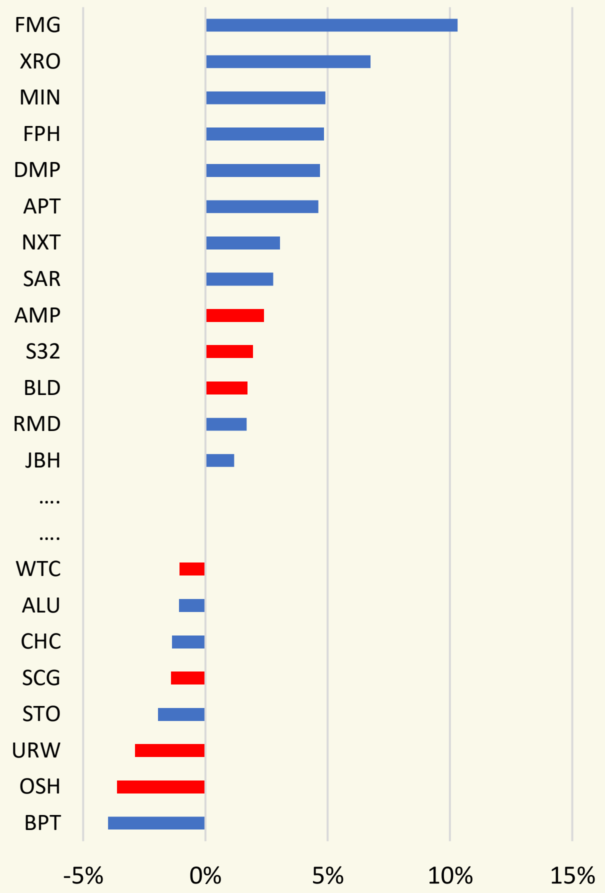
- Over the course of the year, 53 stocks made it into the portfolio, with an average of 24 positions each month.
- Of these, 27 had a positive contribution, while 26 detracted from portfolio performance.
- However, the positive contributors contributed on average +2.0%, while the detractors contributed -0.9%.
- There were 8 stocks that contributed more than 2.5%, while there were 3 stocks that detracted more than -2.5%.
- The largest contributors[1] were:
  - Fortescue (FMG) is a leading iron ore miner. It has performed well during 2020, mostly on the back of

[1] To clarify: these are contribution numbers, not stock returns, i.e. they are the stock return multiplied by the weight in the portfolio for the duration they were held.

Stock	Contri-bution	Position	Time held (months.)
Fortescue (FMG)	10.3%	Long	12
Xero (XRO)	6.8%	Long	12
Mineral Resources (MIN)	4.9%	Long	6
Fisher & Paykel Healthcare (FPH)	4.8%	Long	11
Domino's Pizza (DMP)	4.7%	Long	9
AfterPay (APT)	4.6%	Long	5
Source: Rosevalley			

high iron ore prices over the year. The portfolio was long throughout the year.
  - Xero (XRO) is a provider of accounting software for small- and medium-sized businesses. Its rapid international growth has translated in significant share price appreciation over the year.
  - Mineral Resources (MIN) is mainly a lithium miner, although they have iron ore as well. The global drive to decarbonization is driving demand for lithium (needed in batteries).
  - Fisher & Paykel Healthcare (FPH) is a producer of medical equipment. The COVID-19 pandemic increased demand for their products.
  - Domino's Pizza (DMP) was another beneficiary of the pandemic, as people stayed at home more, and ordered more take-out meals.
  - AfterPay (APT) is one of the world's leading Buy Now Pay Later companies and is experiencing extremely rapid growth.
- The worst detractors were:
  - Beach Energy (BPT), Oil Search (OSH), Santos (STO), three oil companies that recovered about half of the fall they suffered during Feb/Mar, as the oil price only came back very gradually over the year. Unfortunately, we were long BPT and STO early in the year, during the downturn, and short OSH later in the year, during the recovery.
  - Unibail-Rodamco-Westfield (URW), a real estate company. Our short worked reasonably well for most of the year, but the good news on the vaccine in November sent the stock price soaring, creating a loss for us on the position for the year.

CY2020 - Contribution by stock, Rosevalley 13/3; top and bottom contributors



Note: shorts in red; Source: Rosevalley

Execution

To illustrate the difference between gross and net performance, we show a waterfall chart (page 4), using the Rosevalley 13/3 portfolio as an example. The sources of difference between gross and net are:

- Weight difference: due to small position size, sometimes the achieved weight differs marginally from the model weight

Rosevalley is looking for a Sponsor

As most readers are probably aware, the Rosevalley Behavioural Finance Funds are currently run in "Proof of Concept" mode. Of the three portfolios discussed in these monthly newsletters, two (the 15/5 and 10/0) are run with actual money in two different broker accounts, while the third one (the 13/3) is run as a "paper portfolio" with the same broker. The idea is to establish a paper trail that shows the validity of the strategy and can be independently verified.

The monthly newsletters reflect the purpose of the exercise. The comments on gross vs net, execution, trading costs, etc. reflect the goal of establishing credibility both with regard to the strategy itself and the practical implementation of it. The publication of the full portfolio result of the previous month (which no fund manager would normally do) further serve to create the possibility of independent verification.

We are currently looking for a sponsor to enable us to continue to build out our track record. We are keen to meet with potential clients interested to sponsor these strategies and /or invest alongside us.

- Entry/exit price: the difference between achieved trade price and the end-of-the-month that the model uses as the basis for its gross performance calculation
- Trading: brokerage commissions
- Stock borrow cost: the borrow fee and interest costs on the short positions
- Other: this captures the difference between accrued and paid dividends and the residual difference as a result of geometric compounding over time for the above-mentioned differences

All of the steps in the waterfall are in line with the modelled assumptions in the backtest.

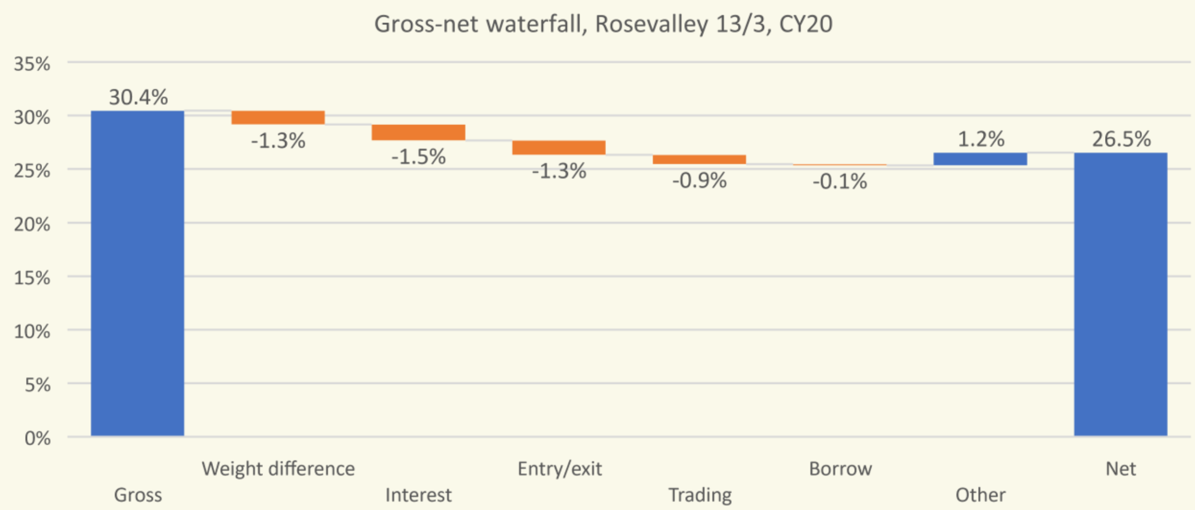
Looking ahead

We are looking forward to a more "normal" year in 2021 (whatever that means!). However, we are under no illusion that the global pandemic is close to being over and we anticipate ongoing social and economic hardships to continue in the year ahead. The roll-out of vaccinations has begun in many countries around the world, but delays are already starting to be reported and in some cases on a mass scale. A number of the medical companies trying to find a vaccine, have stopped researching. It appears it would be quite a good outcome if by the end of 2021 most countries have reached their goals for their vaccination programmes (depending on the country and the vaccine, between 65-85% of their population).

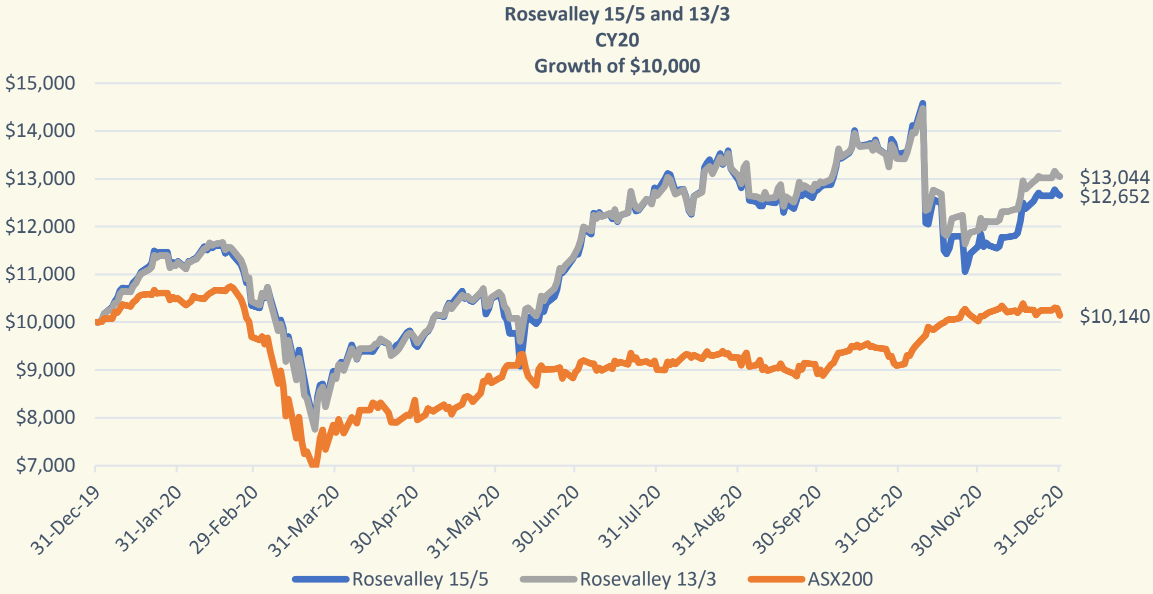
This means that a return to normal economic conditions won't happen until early 2022. This presents a problem for governments and central banks: how much further can economic support programmes go before the debt becomes too much to carry? How wise is it to continue to prop up companies that perhaps cannot survive in the long run anyway? How much further can central bank balance sheets be expanded? At what point does inflation become a real issue?

We don't have answers to these questions, but we do venture a guess as to what most governments' and central banks' answers will be: a lot further, a lot longer, and a lot bigger. In turn that probably means that share markets around the world will do fine in 2021.

And finally, quoting from our FY20 review: Among all the uncertainty in the world, we believe one thing remains unchanged: people's behaviour. Since the Rosevalley portfolios are built to take advantage of how people behave, we are confident that the portfolios will continue to perform well in the coming years.



Source: Rosevalley



Source: Factset, Rosevalley

https://www.afr.com/markets/equity-markets/2020-s-top-fundie-bullish-on-market-s-quiet-achievers-20210119-p56v5k

Rosevalley Funds: The Behavioural Finance Approach

Over the past 30 years Behavioural Finance has emerged as a serious alternative to the Efficient Market Hypothesis. Whereas the Efficient Market Hypothesis starts with the assumption that people (investors) are rational and profit-maximizing, Behavioural Finance builds upon empirical observations of how people actually behave, and goes on to explain securities prices from this principle. Along the development of Behavioural Finance, it has been able to explain many peculiarities that had remained puzzles under the Efficient Market Hypothesis.

Rosevalley Funds portfolios are built around the theoretical and empirical underpinnings of Behavioural Finance, and at heart take advantage of the way human beings behave in the real world.

info@rosevalleyfunds.com
+61-457-807-914
www.rosevalleyfunds.com