ROSEVALLEY FUNDS

Portfolio Report July 2021

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.

First-time readers of this report, please refer to the blue box at the end for added context and history

Market commentary

Global markets returned marginally positive numbers in July, while the Rosevalley funds were quite a bit stronger, outperforming by ca. 250 bps.

Australia was the strongest market among those we cover. The market was supported by strong performance of commodity stocks, which are heavily represented on the exchange. Historically the Australian market has performed well when demand and prices for commodities are high. More broadly, markets around the world continued to move upwards against a backdrop of strong economic growth, as more and more countries are relaxing covid-related restrictions.

Total return	
	July 2021
MSCI World	1.7%
S&P 500	2.4%
DJIA	1.3%
FTSE100	0.1%
DAX	0.1%
Hang Seng	-9.6%
ASX-200	1.1%
Rosevalley 13/3	3.4%
Rosevalley 10/0	3.6%

Source: Factset, Rosevalley. Note: The Rosevalley figures are unaudited.

The new outbreak of covid in Australia that started in late June in a suburb in the east of Sydney spread widely during the month and led to lockdowns of various duration and intensity across the nation. At the time of writing (mid-August) the outbreak and related lockdowns show no sign of abating (see chart). The narrative coming from the political leadership has changed: it has gone

July 2021 - Rosevalley 13/3
Contribution to total return

Source: Factset, Rosevalley

Source: Johns Hopkins University
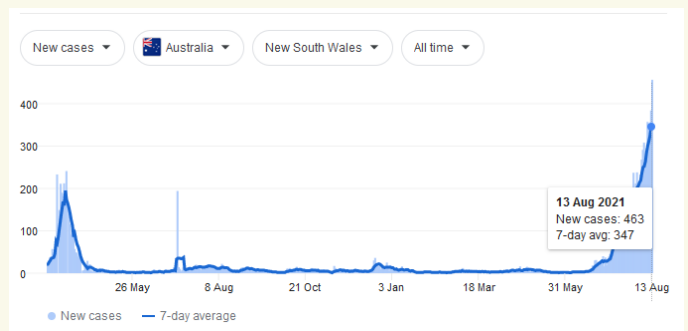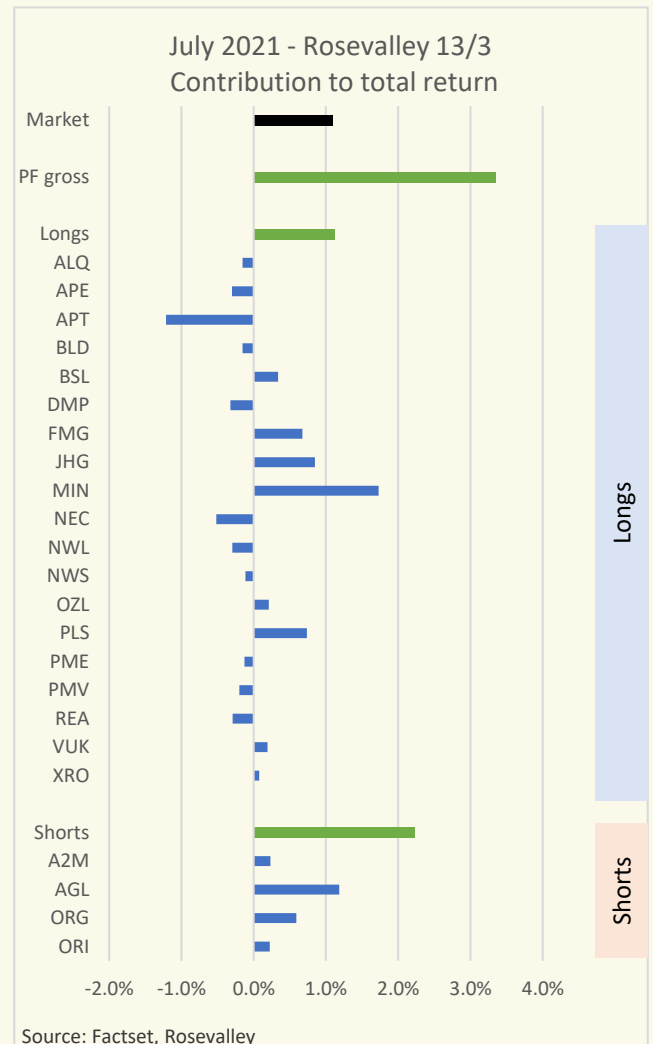
Performance as of July 2021								
Portfolio		1 month	3 months	6 months	1 year	Since inception annualized (1 Oct 2018)	Since inception annualized (14 Aug 2018)	Since inception annualized (1 Aug 2018)
Rosevalley 13/3	Gross	3.4%	12.3%	20.2%	23.8%	22.2%		
	Net	2.9%	11.6%	17.7%	21.7%	18.8%		
Rosevalley 15/5	Gross	3.5%	13.2%	24.6%	23.1%		21.7%	
	Net[1]							
Rosevalley 10/0	Gross	3.6%	9.6%	12.5%	32.3%			22.6%
	Net[2]	2.7%	7.0%	6.8%	19.4%			8.8%
ASX-200		1.1%	5.8%	13.8%	28.6%	10.0%	9.5%	9.5%

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.

from "it is not a race" and "we'll get cases close to zero and then return to normal" to "we need to get vaccination rates up to a level where we can open up even while the virus circulates". Estimates for when that point will be reached fall generally in the October-November range, at a point when a minimum of 70% of the eligible population are vaccinated.

The impact of the deteriorating covid situation on the stock market has been muted, or non-existent. Given what we wrote last month, this did come as a bit of surprise to us[1]. This should serve as another lesson as to how difficult it is to forecast short-term market movements and sentiment.

Markets seemingly continue not to be too worried about inflation – just as we observed in June. While there are many voices arguing that inflation is coming, and that by implication the currently high valuation of stock markets around the world are at risk, investors broadly seem to side with the Fed in their position that the current bout of inflation is transitory.

Portfolio performance

July 2021 - Rosevalley 10/0
Contribution to total return

Source: Factset, Rosevalley

All three Rosevalley portfolios were comfortably ahead of the market, returning ca. 3.5%, vs. the ASX200 at 1.1%. Both longs and shorts delivered positive performance during the month. The latter was especially pleasing, as all shorts contributed positively (i.e. their share prices went down) even in an otherwise broadly rising market. On the long side, Afterpay (APT) continues to introduce volatility into the portfolio, with a large contribution in June turning into the largest drag on performance in July. The model has progressively liked Afterpay less, and we would expect the stock not to return in September (although we can't say this for sure until the month has actually ended). The largest contributor was Mineral Resources, which was up
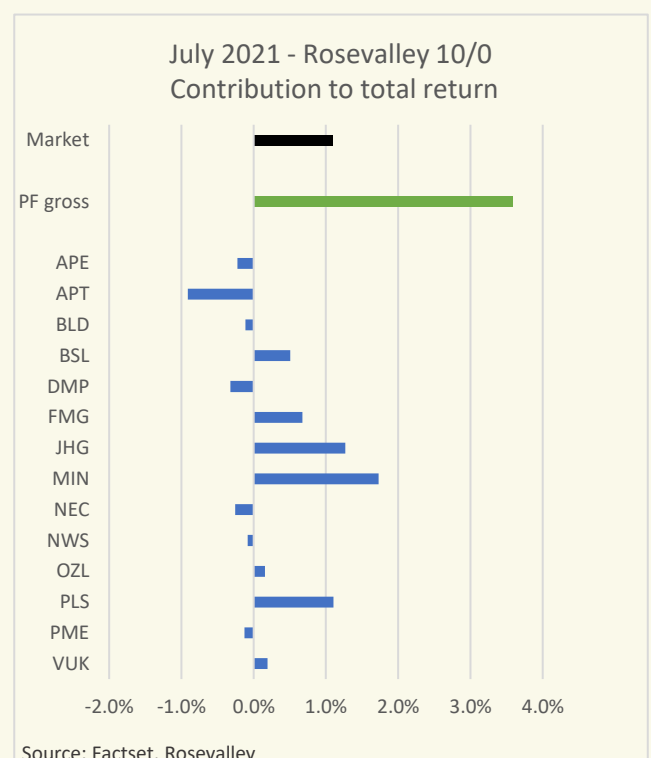
17% and was held at a 10% weight. On the short side Australian Gas (AGL) was the largest contributor, as the stock went down 12% over the month, and was held at a 10% weight.

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[1] We wrote: "While it seems so far the markets have shrugged these events off, we would expect that, if after another 2-3 weeks no firm date for the end of the lockdown is evident, stock markets will start to become a lot more volatile."

For the 12-month and since-inception timeframes, all Rosevalley portfolios continue to perform strongly, still close to an annualized ~10% ahead of market since inception.

This month the usual sources of gross-net difference worked against us – in particular the stock prices at which the trades were executed, such that the gross-net gap was 41 bps (vs. an expected 20 bps).

Rosevalley 13/3 Execution		
	Model	Realized
Gross performance	3.35%	3.35%
deviation from model portfolio		-0.12%
difference between trade price and end-of-previous-month price	0.02%	-0.20%
trading costs	-0.10%	-0.06%
borrow costs	-0.12%	-0.04%
accrued vs paid dividends		0.00%
Reported net performance	3.15%	2.94%

The portfolios for August have four and five long stock substitutions for the 13/3 and 15/5 portfolios respectively, driven by sector concentration concerns. The relatively large number of substitutions is because the tilt towards the Materials sector is currently larger than at any time since inception of the portfolio. Your managers are currently studying the implications of this, and whether there is room for improvement of the model as a result.

	13/3	15/5
Longs taken out	OZL, BLD, IGO, FBU	OZL, BLD, IGO, FBU, JHX
Replaced by	IEL, RWC, ALQ, CHC	RWC, ALQ, CHC, NEC, RMD
Comments	Sector concentration – in both portfolios the next stocks in the list that did not repeat the sector concentration were picked.	

Some context for readers who are less familiar with Rosevalley Funds:

Rosevalley is a boutique funds manager with a unique approach to portfolio construction. Rosevalley Funds are constructed using the principles of Behavioural Finance (BF). Behavioural Economics and Behavioural Finance were developed over the past 30 years or so through the work of economists like Tversky, Kahnemann, Thaler, Shefrin. The idea behind BF (and the Rosevalley portfolios) is to study human behaviour as it is, not as classical economic theory says it should be (i.e. BF does not believe humans are always rationally maximizing their utility).

Rosevalley's portfolio construction algorithms are based on these insights. The model yields a ranking of stocks in order of greatest to smallest upside. Portfolio construction then follows by going long the stocks at the top and short the stocks at the bottom. The flagship product is Rosevalley 13/3, which is a 130/30 fund. We also run a 150/50 (Rosevalley 15/5), and a long-only fund (Rosevalley 10/0). Inception for the three portfolios was during August-September 2018.
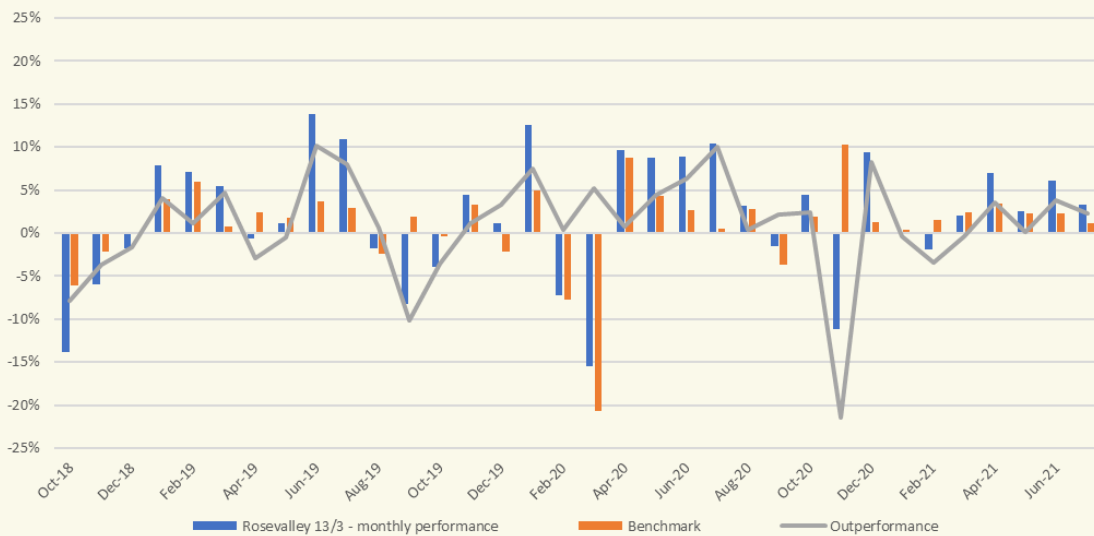
The portfolios are rebalanced monthly. The Rosevalley team has discretion to make some substitutions, albeit that the bar for those is set high.

The monthly report discusses current events, portfolio performance, trade execution, gross-net differences, next month's portfolio, and broader market and macro expectations.

Rosevalley 13/3
Since inception
Growth of $10,000

Source: Factset, Rosevalley. Note Rosevalley numbers are not audited

Rosevalley 13/3 — $17,643
ASX200 — $13,105

Rosevalley 13/3 - monthly performance

Legend: Rosevalley 13/3 - monthly performance | Benchmark | Outperformance

Source: Factset, Rosevalley

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.

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