ROSEVALLEY FUNDS

Portfolio Report November 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.

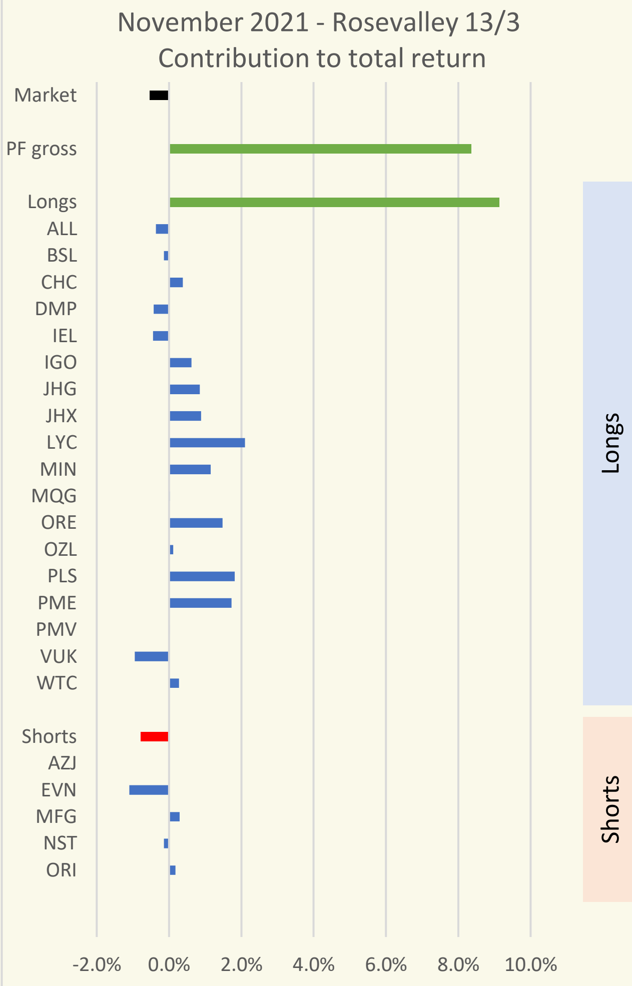
First-time readers of this report, please refer to the blue box at the end for added context and history

Market commentary

In November markets around the world took a step back, with the equity markets we track down from -0.5% in Australia to a more volatile -7.4% in Hong Kong. Rosevalley, however, delivered a stellar performance, with the various portfolios up 7.5-9%.

Total return	
	November 2021
MSCI World	-1.4%
S&P 500	-0.7%
DJIA	-3.7%
FTSE100	-2.2%
DAX	-3.8%
Hang Seng	-7.4%
ASX-200	-0.5%
Rosevalley 13/3	8.4%
Rosevalley 10/0	7.5%

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



Source: Factset, Rosevalley

Covid and inflation continued to drive markets.

For most of the month, markets were up (see chart to the right for the performance of the Australian ASX200 index). The "re-opening theme" dominated trading – this is the premise that, as the pandemic wanes, economic activity will pick up, and therefore stocks are becoming worth more. As always, we are slightly bemused by such explanations of market movements: surely the probability that the pandemic will wane did not change materially over the month?

At the end of November the omicron variant was identified and labelled a variant of concern. Stock markets reacted quickly and brutally: all of a sudden, re-opening was out, and the spectre of new lockdowns was in.

The Australian market was in positive territory for most of the month, but dipped sharply in the last three trading days.

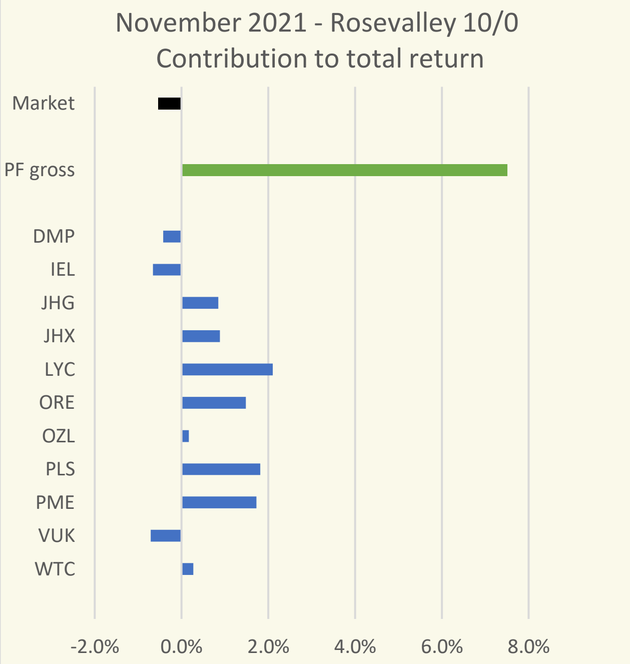
Source: Factset

Performance as of November 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	8.4%	-2.1%	13.5%	36.1%	20.9%		
	Net	8.0%	-2.5%	10.8%	30.2%	17.3%		
Rosevalley 15/5	Gross	9.0%	-1.8%	16.0%	42.0%		21.1%	
	Net[1]							
Rosevalley 10/0	Gross	7.5%	-0.2%	18.3%	30.2%			22.6%
	Net	7.3%	3.3%	19.0%	24.1%			10.9%
ASX-200		-0.5%	-2.5%	3.3%	15.5%	8.9%	8.4%	8.5%

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.

Through all this, the inflation debate continued in the background – with continued high numbers being published in several OECD countries, is inflation permanent or transitory?

In November, the Fed (the US central bank) continued its position that inflation is transitory, and therefore there is no need for a specific response on their part. At the time of writing (mid-December), the tone had changed. The Fed now acknowledges that inflation is more persistent than they thought, and therefore there is a need for them to do something (i.e. raise interest rates). The markets reacted positively to this news – this was perhaps curious, since for most of the past 20 years the market has behaved in the pattern of "low rates = good for equities, high rates = bad for equities" (we have of course long disagreed with this, so it was a bit vindicating to see the market behave as we think it should).



Source: Factset, Rosevalley

Portfolio performance

All three Rosevalley portfolios showed considerable outperformance, returning 7.5-9% vs. the ASX200 down 0.5%. The outperformance was driven by the long side of the portfolios, with materials/mining-related stocks the main contributors. The long in bank Virgin Money (VUK) and the short in gold miner Evolution Mining (EVN) detracted from performance.

Longer term performance

Now that the particularly bad month of November 2020 has fallen out of the 1-year numbers, the performance once again looks very strong on every time frame in the table above. We mentioned two months ago that this would happen, and while we obviously take pride in showing 1-year numbers in the 30-40% range, vs. the market at 15.5%, we would continue to argue that the only really important number is the performance since inception – on this measure all portfolios are more than 10% p.a. ahead of their market, thus doing a little better than what's on the tin.

Execution

This month the usual sources of gross-net difference were favourable relative to the modelled expectation: the gross-net gap was -35 bps (vs. an expected -61 bps).

Rosevalley 13/3 Execution		
	Model	Realized
Gross performance	8.36%	8.36%
deviation from model portfolio		0.00%
difference between trade price and end-of-previous-month price	-0.07%	-0.16%
trading costs	-0.41%	-0.07%
borrow costs	-0.12%	-0.11%
Reported net performance	7.75%	8.01%

December Portfolio Manager model overrides

As in the previous month, the portfolios for December have one long stock substitution for the 13/3 and 15/5 portfolios – again this is Afterpay (ASX:APT), which is under takeover offer from the US listed company Square (NYSE:SQ). The substitutes are Premier Investment (ASX:PMV), a specialty retailer, in Rosevalley 13/3 and Seek (ASX:SEK), an online jobs portal, in Rosevalley 15/5.

	13/3	15/5
Longs taken out	APT	APT
Replaced by	PMV	SEK
Comments	APT is under takeover offer – consequently the price signal does not reflect the behavioural signals that the model would ordinarily pick up.	

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 December-December 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.

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

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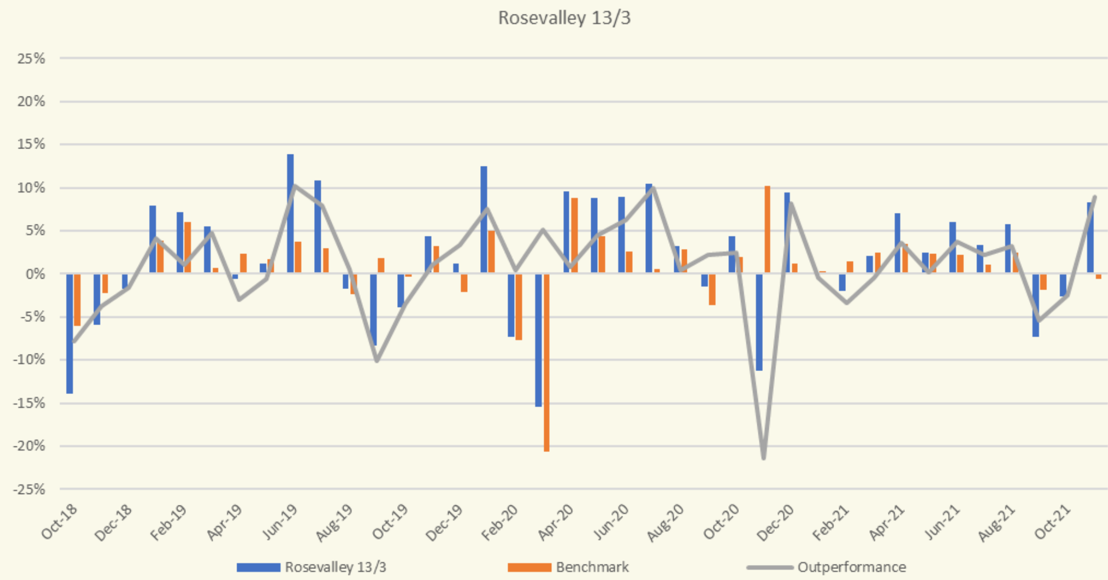

Source: Factset, Rosevalley

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.