BEULAH CAPITAL

Beulah Conservative Portfolio

Quarterly Fact Sheet | March 2022

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Investment Approach

The portfolio aims to achieve a rate of return that matches inflation (CPI) plus 3% over a rolling 5 year period.

INVESTMENT STRATEGY

The portfolio targets a 70% investment in income assets (cash and fixed income) and 30% investment in growth assets (shares, property and international) either directly or through specialist wholesale fund managers. The allocation to individual asset classes is managed on a dynamic basis and may vary within nominated ranges.

Universe

The portfolio is invested across a mix of shares, property and fixed income securities. The targeted use of specialist managers also allows access to investment expertise and a diverse range of securities not readily available in an individual portfolio of this size.

RISK PROFILE
Low to medium: The estimated frequency of an annual negative return being less than 1 in 8 years.

MINIMUM INITIAL INVESTMENT
$100,000 on a standalone basis

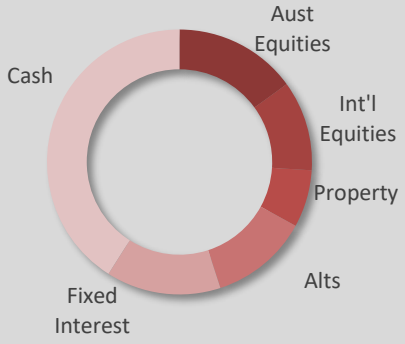
MINIMUM SUGGESTED TIME FRAME
4 Years

Performance

Beulah Conservative Portfolio							1-Jul-10
	3 Month	6 Month	1 Year	3 Year	5 Year	10 Year	Incept.
Model Portfolio Return	-1.91%	0.12%	5.04%	5.19%	4.07%	5.26%	5.30%
M* Moderate Target Allocation	-4.05%	-2.99%	0.83%	3.40%	4.26%	5.61%	
Relative Return	*2.14%*	*3.11%*	*4.21%*	*1.79%*	*-0.19%*	*-0.35%*	
Investment Objective (CPI +3%)							5.12%

Performance Notes:
1: Peer returns are based on Morningstar Category peer averages that most closely reflect Beulah asset allocations.
2: Model portfolio return includes dividends and income, but does not assume reinvestment.
3: Returns greater than 12 months are annualised.
4: Returns are calculated after Managed Fund and other transaction costs, but before portfolio and MDA fees.
5: Returns are rounded to two decimal places.
6: Returns and holdings may vary between investors given the nature and timing of beneficial ownership under an MDA structure.
7: This document is for marketing purposes only.
8: Past performance is not an indication of future performance.

Asset Allocation



Asset Class	Actual %	Range %
Australian Equities	15	0-30
International Equities	11	0-25
Property Securities	7	0-10
Alternatives	12	0-20
Fixed Interest	14	20-50
Cash (inc. Tactical)	41	10-60

Contribution to Performance

Asset Class	Contribution to performance %
Australian Equities	-0.71
International Equities	-1.01
Property Securities	-0.26
Alternatives	0.23
Fixed Interest	-0.17
Cash	0.01

Market & Economic Review

The March quarter of 2022 will go down as one to forget as financial markets began the year on a dismal note. January opened proceedings with a sharp correction in equity markets as the valuation of growth stocks, in particular, were impacted by fast rising bond yields. Bond markets sold off in response to inflation data that continued to surprise, with investors concerned that this could lead to a steeper trajectory of interest rate rises by central banks. Ultimately, such moves could harm economic activity and company earnings.

At the same time, rising tensions between Russia and Ukraine added to the wall of worry. And Russia defied the expectations of many political analysts, invading Ukraine on February 24th. This sparked a spate of sanctions by the US, Europe and elsewhere, with many multi-national companies pulling out of Russia of their own accord. In addition, February posted no new S&P 500 closing highs, something not seen since October 2020, as momentum ground to a halt. This came despite a strong quarterly earnings season in the US.

Meanwhile, domestic shares posted far stronger performances than their global peers. The S&P/ASX 200 generated returns approaching 7% during the quarter, while the MSCI All Country World index (ex Australia) finished in the red. Emerging markets were hit especially hard. Domestic investors benefited from the local market's stronger yield focus and higher-than-average exposure to the financials, resources and energy sectors. Indeed, over the March quarter, excluding dividends, the S&P/ASX 200 Index outperformed the US S&P 500 by the biggest margin since the December quarter of 2018. The US S&P 500 experienced just its twelfth quarter post-WW2 that saw the index fall 10%+ from a closing high and rally back 10%+ from its intra-quarter low. This is partly explained by short covering and by a partial switch out of bonds into equities.

Market & Economic Review (cont.)

As the quarter continued, bond markets were hit with further losses across most sub-asset classes, from sovereign bonds to most credit categories, with longer duration assets taking the brunt of the hit. Ultimately, traditional fixed interest printed deeply in the red. But, the worst was saved for local bond markets, where domestic investors saw negative returns spanning a three year period.

In mid-March, the US Federal Reserve (the Fed) raised official interest rates by 0.25% and upgraded its inflation forecasts, while moderating growth predictions for 2022 and beyond. The FOMC meeting revealed that the median voting member now expects seven hikes this year. Furthermore, markets are assessing whether some of these hikes will come in the form of 0.5% increments. An additional four rate rises are predicted for next year, signalling that rates could eventually exceed the Fed's perceived neutral rate for the US economy of 2.4%.

This led some investors to forecast a US recession later this year, with yield curves very flat from 2yr to 10yr maturities. Meanwhile, Russia's invasion of Ukraine has made a recession in Europe look especially likely, due to supply and price impacts. Not to diminish the human impact of these events, the war immediately exacerbated the surge in inflation, prolonged supply chain disruptions and placed a handbrake on global growth. Oil and gas prices escalated as a risk premium was built into the energy price complex. Food prices also jumped.

On the domestic economic front, the labour market continued to strengthen and there was further anecdotal evidence of labour shortages in some sectors. With the Reserve Bank about to commence raising the Official Cash Rate, fixed rate mortgage rates continued to climb, and the largest increases happening across the longest duration mortgages. The median home buyer using a fixed rate mortgage is now paying $680 more in monthly repayments than they would have had they purchased a year earlier (rising house prices is also a factor). Despite these pressures, markets are pricing the cash rate to reach 2.5% by year-end and 3.5% by May 2023.

Portfolio Review

In what proved to be an eventful quarter, there was mixed performance across the Portfolios. Conservative and Balanced outperformed their relevant Morningstar Target Allocations, while Growth and Growth Plus underperformed.

Solid outcomes in the Alternative asset class (primarily Perpetual Pure Equity Alpha) were outweighed by losses across most risk asset categories, including Equities and Property. Our tilt towards domestic shares over global helped to mitigate losses as higher-growth global shares were battered by rising bond yields. Our fixed income/credit exposures also incurred small losses during the quarter, but largely avoided the bloodbath that occurred in traditional fixed interest markets. Further losses were largely insulated by overweight positions in Cash, which is mostly of the tactical nature, as we patiently await opportunities for deployment.

In light of the uncertainty around the trajectory of interest rate rises in the US during the quarter and the oil price spike in response to the Russia-Ukraine conflict, we sought to insulate the Portfolio by reducing our overweight exposure to Franklin Global Growth Fund (FRT0009AU) and exiting our remaining holding in iShares Global Healthcare ETF (IXJ), in favour of cash. On the stock front, with the Tech sector a notably poor performer in 2022 due to the potential for interest rate rises to weigh on valuations, we exited our position in Block Inc. (formerly Afterpay). The company had been a strong performer for the Portfolio over the medium term, but suffered in the market rotation towards Value. Given Afterpay is now part of the Block group post acquisition, we felt the company would continue to be diluted in the larger group and exited our position. The effect of these moves is to further reduce bias to growth-style equities in the Portfolio.

In Fixed Interest, with market volatility rising, we elected to exit our exposure to Mutual Income Fund (PRM0015AU) in favour of further bolstering our tactical cash holding. As credit spreads moved wider during the quarter, even high quality floating rate notes were not immune from the potential for losses and, hence, we sought to reduce this impact within the Portfolios. Overall, the Portfolios are holding larger-than-usual cash balances and we expect this to provide some capital protection as growth assets deal with worsening risk-off sentiment during the current June quarter.

Outlook

With Russia's invasion of Ukraine pushing inflation higher through higher food and energy prices and by exacerbating global supply disruptions, the outlook appears decidedly clouded. Perhaps a bright spot is that Covid-19 is becoming endemic, with more contagious variants proving to be less virulent. Hospitals and ICUs are no longer being overwhelmed and many countries, including Australia, are relaxing many of their pandemic laws. China, however, is continuing to pursue a 'zero Covid' approach and at time of writing had locked down tens of millions of people, including the largest city and financial centre, Shanghai. As a result, its services sector has once again collapsed and economic policy settings relaxed.

In March, we downgraded our outlook for the global economy and, in particular, the US. We moved from an above-consensus position of cautious optimism to one of greater concern, with our growth-range prediction just below a market consensus that had also been reduced. To this end, analysts are already slashing earnings estimates for 2022 on the basis that rising uncertainty will hit consumer spending as input costs peak. This is despite a strong first quarter US earnings season, with the notable exception of Netflix, where rising competition has seen an exodus from the stock.

While we are broadly in agreement with this position, our base case for the US economy does not currently foresee a recession in the current calendar year. The labour market is strong, with low unemployment and rising workforce participation. Employment is now down by 1.6 million, or 1%, from its pre-pandemic level in February 2020. The industrial side of the economy is also strong with rising capital expenditure excluding lumpy items, such as those related to transport and defence orders. As the year unfolds, we will continue to monitor develops and assess risks, such as for the possibility of stagflation (i.e., stagnating growth with high inflation).

In Europe, Germany has seen its growth forecasts slashed for 2022, with an outright recession a real possibility if there is a complete cessation of Russian energy supply. Such a contraction would continue into 2023. Even without such a dramatic turn of events, Euro Area activity has already slowed as is evident across the high frequency data releases since the end of March.

On the domestic front, the market is wrestling with the hawkish pivot in the language emanating from the RBA. As recently as October, Australia's central bank was guiding for no hikes to the official cash rate prior to 2024. But, at the beginning of May, the RBA raised rates by 0.25%. Indeed, the market is fully pricing a 2.5% cash rate by year-end and 3.5% by May 2023. We think that the pace and extent of such moves are unlikely and that the RBA will consider many factors beyond inflation in deciding on interest rate policy. Mortgage stress is likely to feature highly in its decision making, with Melbourne and Sydney particularly at risk, and falling real wages will also be a factor.

Across financial markets, our equity market valuations imply asymmetric risks that are weighted to the downside. Equity risk premiums are around the long term average across most developed market regions, but despite credit spreads widening in recent times, equities look expensive relative to investment grade corporate bonds. This is not to say that both sectors can't decline. While inflation likely peaked in the March quarter, future inflation surprises could continue to play have havoc with bond markets, especially for longer durations, as these securities are more sensitive to interest rate changes.

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