BlueAlpha BCI Global Equity Fund – Quarter 4 2018

BLUE ALPHA
INVESTMENT MANAGEMENT

Performance Period	Fund Return	Sector Average	Benchmark
1 Year	6.3%	1.0%	7.9%
3 Years (annualised)	4.2%	0.9%	2.3%
4 Years (annualised)	11.1%	7.5%	9.8%
Since Inception (annualised)	13.2%	8.0%	11.5%

Performance is reported for the A Class net of fees in ZAR
Sector Average: Global Equity General
Benchmark: 80% MSCI World Index, 20% USD Libor Rolling 1yr

Asset & Sector Allocation	
Cash	4%
Total Net Equity	96%
Consumer Goods	7%
Consumer Services	28%
Financials	9%
Health Care	13%
Industrials	11%
Technology	27%
Other	1%

Top 5 Global Holdings
Tencent
AbbVie
Broadcom
MasterCard
Apple Inc

Equity Holdings by Geography	
USA	83.1%
Europe	11.2%
Asia	5.7%

Portfolio Manager: Richard Pitt / Walter Jacobs
Commentary for the Quarter ended 31 December 2018

Looking back, 2018 seems like a perfect example of A Tale of Two Cities. To quote CNBC, it was both the best of times (Jan'18) – "The stock market is off to its best start in 31 years and that bodes well for the rest of 2018" – and it was the worst of times (Dec'18) - "US stocks post worst year in a decade as the S&P 500 falls more than 6% in 2018". Given the sharp declines in global equities during the 4th quarter, which accelerated into December, it was only a matter of time before historic data would be scrutinised to find some hair-raising statistic. It turns out, that the final month of 2018 is the second worst December performance over the last 100-odd years after 1931. Anything in proximity to the great depression is exactly the kind of headline to make investors panic. Is there any value in this statistic? We very much doubt it. The Vanguard Total World Stock ETF declined by more than 20% from a peak to trough basis in 2018. It has had two similar declines over the last 10 years – in 2011 and 2015/16. At the same time, it has delivered a gain of approximately 100% over that period.

Strategically we remain constructive on equities – but long-term returns will with certainty be marked by periods of decline. Intelligent investing requires the fortitude to stay invested and if possible, add to investments after price declines. Also - try and ignore headlines – they hardly ever help.

Performance

The fund returned -14.9% in USD (-13.7%in ZAR) vs. the MSCI World Index's -13.4% (-12.1% in ZAR). However, for the 12 months ended December 2018, the fund has slightly outperformed the market, returning -8.4% in USD (6.3% in ZAR) vs. the MSCI World's -8.7% (5.9% in ZAR). Despite the difficult quarter, we are happy to report the fund ranks 1st against the Asisa Global Equity General peer group for 3-year performance, and 5th over 1-year. While this is surely cold comfort for investors who have lost some money over the last 12 months – against a backdrop where almost everything except cash lost money in 2018 this is not an altogether awful outcome. Since inception a little over 4 years ago, the fund has delivered a gain of 26% in US$ and 73% in ZAR and has strongly outperformed its equity benchmarks.

Global Macro

The selloff in global equities was driven by global growth concerns with potential challenges to growth materialising, even in the US, with global earnings revisions collapsing across all regions from 1.41 in January 2018 to 0.48 in December. Several large and high-profile companies missed revenue expectations which further knocked sentiment. China vehicle sales have fallen -13.9% over the year, suggesting consumer weakness. Sentiment was further affected by headlines around both the continuing trade tensions between the US and China, continued Brexit uncertainty and the partial US government shutdown which at the time of writing is now running at a record 25 days.

As expected, the Federal Reserve implemented its 4th rate hike for the year, with a further 25 basis point increase. The Fed has since stressed their patience, in that they will take direction from the markets regarding decisions on further hikes. This flexible stance is due to perceived downside risks to financial conditions. It seems less frequent hikes are likely over the next year. Unsurprisingly, sentiment polls turned very bearish in the last quarter (a bullish signal), inflation remains low and the labour market is robust, supporting good consumer spending. Collectively this bodes well for equities.

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Commentary for the Quarter ended 31 December 2018 Continued

Portfolio

At a sector level, the fund had no exposure to Energy, Financials or Materials, which contributed to returns. Consumer Discretionary, Info Tech, and Communication Services were the largest detractors. With global markets broadly negative over the quarter, all sectors produced negative returns.

Top contributors to performance were AutoZone (+8.1% in USD QTD) and Broadcom (+4% in USD QTD). The largest detractors from performance were FedEx (-32.8%), Apple (-29.9%) and Aptiv (-26.4%). Apple is clearly a victim, to some extent, of its own success. The iPhone is a major profit contributor and the smartphone market is clearly maturing and phone improvements are more incremental than fundamental. This means a large part of their business growth is more cyclical than secular in nature. Nonetheless, the Apple brand, ecosystem value, growth of services and the launch of 5G phones driving another upcycle are all positives. The company generates very high returns and is highly cash generative. It is shareholder-focused, paying dividends and buying back shares. Furthermore, the company trades at a considerable discount to the market average before even accounting for the substantial net cash on the balance sheet.

We thank investors for their support and confidence placed in us and will keep investing in high cash returning businesses with opportunities for growth - in line with our strategy of looking for quality compounders.

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