Gleneagle Asset Management Gleneagle Investment Fund
(GT Momentum Portfolio)

March 2021 Review

The GT Momentum Fund declined by 4.1% in March as the lack of direction in the broader market and our specific portfolio failed to produce any meaningful opportunities. Much of this lackluster behaviour from financial markets is best reflected in highlighting the trading range not just over March but the past several months.

 The ASX 200 reached a level of 6765 on 18th December 2020 and on final day of March 2021 it traded at exactly the same level representing four months of zero trend and zero direction. Adding to the lack of opportunity, the index's range over the past month was just 200 points, bouncing around between 6860 and 6660 in a very whippy fashion as shown in the chart below.-

Other indices also took the month of March off from their usual trajectory and trends. Commodities, including precious and base metals, were also caught in this directionless performance.

The culprit for this pause in markets was triggered by an acceleration in the rise of long term bond yields as fears of inflationary pressures building in the global economy began to surface. We have discussed in the past six months that bond yields would head higher over the foreseeable future as the global economy slowly re-opens and the combination of Government and central bank stimulus will help drive a strong rebound in activity. The rise in bond yields on the back of this specific thematic (improving economic growth) is a good thing as increased activity leads to higher revenues that more than offset the rise in interest costs. However, markets do get spooked if bond yield increases rapidly rise in a short period of time, usually on concerns that central banks have lost control of the economy and/or inflation and will need to raise interest rates aggressively to cool the economy. Such circumstances lead to the typical boom-to-bust cycle.

As it turns out, the market concerns were unwarranted at this point as subsequent inflationary data showed inflation still relatively tame (especially wages) and central banks are in no way yet under pressure to back off from their stimulus measures as they work to their goals of full employment and re-inflating the economy.

We used this period to continue to accumulate holdings in those companies and markets which fit in with our favoured thematics of the green energy revolution, infrastructure stimulus and earnings tailwinds from mortgage demand and yield curve improvement (namely the banks).

So while the month of March saw very little performance from the indices, the story was very different at the stock specific level. Stocks like Fortescue Metals (FMG) and RIO declined between 10 and 20% over the month and we took advantage of this drop to build positions in FMG and RIO. As was experienced in the 2003-2007 commodity boom, resource stocks would experience huge price surges for several weeks and even months before retreating, consolidating and then embarking on the next re-rating higher. Buying during these price retreats proved to be a lucrative strategy and one which we are adopting once again during this cycle.

In addition to adding RIO and FMG, we also added Bluescope Steel that will benefit from ever improving steel prices as infrastructure demand only increases over the coming year on the platform of further of Government stimulus. US President Joe Biden’s $2 trillion infrastructure bill reflects the sheer weight of money being thrown at this policy.

On the specific commodity front we also established positions in copper as it is a major, if not the greatest beneficiary, of both the green energy revolution and broader infrastructure demand. We had been waiting for an appropriate point to enter the upward trend in copper prices and the March retreat provided the latest point to do so. Accompanying the direct investment in copper we also added world-class copper producer OZ Minerals to the portfolio for price and production leverage.

Finally we added positions in NAB and Westpac as rising bond yields, relaxed lending laws, booming mortgage demand and robust investment markets translate to an ongoing tailwind for earnings. The share prices of the banks over March were very unexciting as they traded sideways for the entire month, but we believe that this will ultimately resolve itself to the upside with another uplift in valuations for the sector.

Some investors may have noted that, while our outlook and key thematics for 2021 are unchanged, this month there has been a shift to a focus on larger-cap businesses. For the past three to four months the small and mid-cap companies had outperformed but we have distinctly noticed that many of those have run out of steam and are either in the midst of a steep correction or on the verge of one. Even those companies benefiting from the tailwinds of our favoured thematics have run their course for now and either buyer exhaustion or capital raisings has brought an end to that bullish momentum. Many in March halved in price.

Why is this worth noting?

Because mid and small-cap companies were the primary focus of the fund in recent months and they produce the biggest percentage swings in any given cycle. We have been fortunate enough to exit many of those near their high points and lock in big gains. Moving forward the large-cap companies will not produce the same sort of percentage gains for us that we have enjoyed over the past six months and so expectations need to be tempered somewhat. Weekly and monthly gains of 10, 20 and even 50% in small cap companies can be considered “normal”, but there is little chance the same returns will be generated from the big end of town. The plus side though is that the downside will also be limited and having reduced the majority of our exposure to smaller companies we will avoid much of the volatility they are currently experiencing.

Until next month,

Gregory Tolpigin Portfolio Manager
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