Wilson Asset Management

WAM Leaders FY2023 Interim Results Q & A Webinar

Bridget Thelander: Hello and welcome. Thank you all for joining us today for the WAM Leaders (ASX: WLE) Interim Results Webinar. My name is Bridget Thelander and today I am joined by Lead Portfolio Manager Matthew Haupt, Portfolio Manager John Ayoub and Equity Analyst Anna Milne. To start, I will first give you an update on the WAM Leaders Interim Result and then I will pass to the investment team to discuss the investment portfolio before opening up for Q & A. To begin, the WAM Leaders Investment Portfolio performed strongly during the half year to 31 December 2022 increasing 8.8%. In the 2022 calendar year, the investment portfolio outperformed the S&P/ASX 200 accumulation index, by 9.9% while being on average 97% invested in equities. The WAM Leaders Board of Directors declared a fully franked interim dividend of 4.5 cents per share and this represents a 12.5% increase on the FY2022 fully franked interim dividend and an annualised dividend yield of 5.8% on yesterday's closing sharing price of $1.55. The profits reserve was 41.1 cents per share as at 31 December representing 4.1 years of dividend coverage. I will now hand over to Matt, John and Anna who will provide a market update, discuss key portfolio themes and take us through some company examples. Thanks Matt.

Matthew Haupt: Thanks Bridget, and welcome everyone to the WAM Leaders investment call. I am going to talk about the market through the macro lens and the economy lens before I hand over to John who will run through some of the portfolio positions and then to Anna who will run through some stock examples. What I thought I would do, is walk through some slides that are catching our attention at the moment and I thought it was a good place to start given the uncertain environment we are in. This was a great quote from the Godfather of investing, Benjamin Graham and this sums up our views at the moment. It is not about avoiding risk, but navigating through this period and positioning the portfolio according to the circumstances which are in front of us. We have an investment process that can navigate these periods, so it is not uncertain for us, it is just part of the process. I will now walk through some of the market valuation slides that I have put together and then we will talk about the economy. It is very noisy at the moment and we are in a bear market. What I am trying to show here is how we are progressing through the bear market and as you can see, if you are following the slides, it shows you that this is not uncommon. We are progressing quite normally through this period. Normally bear markets last for a fairly lengthy period of time, but it depends on the drawdown as well. You have had some really large drawdowns in previous bear markets and they have been a very short duration. We feel like this will be a long duration event, but we are progressing quite nicely and we are starting to see some light at the end of the tunnel through some of the leading indicators. We have still got a lot of work to do and we still have to navigate a fair distance before we come out of that. On slide 10, financial conditions are a variant, falling hard of equity valuations. Financial conditions were extremely tight last year and that was a function of rising interest rates, a strong US dollar as well as credit squeeze increasing. When financial conditions tighten, equity valuations fall. We have had a reprieve in financial conditions now, it is starting to be a little bit easier, but we feel like financial conditions will tighten again later this year. We feel like we are in a narrative now where we were in a soft landing potential scenario and that is flipping. Now we are on a probably on a higher weight longer trajectory for the immediate future. Why has this happened? Like we touched on financial conditions and interest rates, as you can see here on page 11, the interest rate environment last year in particular was incredibly tight, very poor made policy changes and it was really the emergency policy settings unwinding and that has continued today as you can see here very, very strongly. We are coming towards the end of this policy tightening cycle and when we look at policy, Central Banks were very key in putting liquidity into the system. Central Banks inject bank reserves into the system and bank reserves are a symbol of the lifeblood of how the financial system operates. They were in emergency settings for a period and again you can see that is in contraction now and that is just a reserve emergency settings coming out of the markets. Again, nothing to be too alarmed about at this point in time, but you can see now that policy has definitely shifted and we are starting to feel that through equity markets and also the economy. On page 12 here, we have got a slide showing how in the last 3 years there has been a shortfall on long equity, apart from a few mishaps like the GFC. You can see that gap between bonds and equities has narrowed and again we think that is a little bit of a what you are seeing at the moment, a bit of an asset allocation shift. That has been a headwind for equities and we see that as an ongoing issue for equities, but again nothing to get too alarmed about at this point in time because we think that could reverse later this year. This is something that has been a bit of a headwind for equities as well. When we obviously look at the global macroeconomic environment, then we try and nail down some of the impacts on the Australian economy and we thought we would put together some slides around what we are watching in the Australian economy at the moment. When we are trying to assess how the economy is performing, we try to look through cycles and where we are in various cycles. We are definitely in a slowing down period of extraordinary resurgent uplift from COVID lockdown. We are definitely slowing. Again, this is nothing to be alarmed about, this just gives us an indication of where we should position with the portfolio and again, we are watching this closely. We do not think it will be enough for a harder ending at this point in time, but definitely a slowing economy. Again, that shapes on how we position the portfolio. Here, we are trying to explain how bad confidence is within Australia. Consumer confidence is at all-time lows. Business confidence is doing a lot better, but one of the reasons why consumer confidence is so low is really a function of this next slide on page 17. The cost of living for Australians has been incredibly steep in recent periods and it is really a function of inflation flying through the economy and taking away a lot of that discretionary spending power away from consumers. That is likely to continue albeit inflation in Australia should moderate. The RBA were out recently saying they think maybe it will peak in December, but it is probably going to take longer to come out of the system. It is definitely abating which brings us to why has inflation hit the Australian economy so hard? It is really through a lot of the discretionary items like food and transport which is linked to moving goods but also households and housing. On housing, we went through this incredibly stimulative period with low interest rates. We had APRA allowing a lot of lending to go on. We have had financial or fiscal responses allowing people to access Super, and that put a lot of pressure on Australia's demand part of the economy. It is abating as I mentioned, but there is more of a headwind to come and that is from the fixed interest role within fixed interest mortgage lending. It has been a very big part of flow going forward and this year there is a huge amount of rollover starting that will add to the sentiment hit to consumer. You can see not only the variable part of the book has increased in rates, but this fixed part over the next few years show there is going to be another headwind for consumers. We are a bit cautious of the consumer. Now one of the saving graces for Australia over the last 10 – 15 years has been China. China was locked down for about 2.5 years, they weren't really driving the economy that hard, they had times of trying to get the economy going but what we saw in January was the total social financing hit an all-time record. That probably puts China in good stead for this year. They are trying to get credit going through the system again and get some activity going. We think the policy environment for China will be quite good going forward this year. We think although the macro environment is still conducive for a good performance from Chinese basement stocks on the ASX. In summary, we are going through a slowdown period. We think financial conditions are probably going to get tighter over the next month or two from a tactical point of view. We went from a scenario last year in October/November where there was a huge liquidity and then in January we saw lower rates and an easing environment. The narrative is probably shifting again now and we are going to have a tighter environment over the next month or two. We are quite cautious short term, but we are working our way through this point of the cycle. We think later this year potentially you will get easing cycles and interest rate cuts if they go too hard in the short term and that will create an environment where equities and the PE ratio could improve. We still think there is an earnings impact to be felt over the next 3 to 6 months, but eventually a fallen interest rate will cushion equities on the valuations. At that point, I will now hand over to John who will run through some of the portfolio positions.

John Ayoub: Thank you, Matthew. As you can tell from Matt's comments, what we do know, is that it is going to be uncertain. The uncertainty is creating volatility like we have seen in the markets over the past few months. The ASX has had a really good start this financial year up +13 to +14% but that is not to say we are about to go through a slightly tougher period and from where we stand we are looking at the market and the valuations being a fairly robust period where a lot of stocks, in particular in January, were at a really strong period. What we have seen in February was probably a pullback of that enthusiasm. As earnings start to come through and show the real headwinds in the economy, as Matt was pointing out, the results period certainly highlighted that revenue is still there. The top line growth is present for a lot of the representatives of the ASX200, but we are starting to see bottom line pressure, particularly as costs start to grow and as consumers start to struggle. Other themes that we really like is valuation support. As you can see from our top 20 holdings I we have got a diverse spread of stocks and for the first time in a long time you could probably characterise the portfolio more as a stock picking portfolio as opposed to directionally macro driven portfolio. That is something because of the uncertainty that we have seen in valuations, uncertainty we have seen around the consumer and the markets more broadly. We feel like right now is the opportunity to pick the best in various stocks that will help us navigate through the next period of the market, the various gyrations that we will see. If you pick a few of those names out, if we can try and get that valuation support, if we knit quality with defensive characteristics, stocks like Brambles (ASX: BXB) and APA Group (ASX: APA), Dexus (ASX: DXS) Transurban (ASX: TCL). These are the stocks that we think will continue to outperform over the next little period. We will take stocks which we think have gotten too cheap and though they are high off the risks associated with Star Entertainment Group (ASX: SGR) and LendLease (ASX: LLC) for example, we will take those proportionate risks within the portfolio because we think there is that valuation support at current trading levels to provide that catalyst or that quality performance and re-rate over the next 6 to 12 months. Other things that we will call out is that valuations still remain fairly full, but I think what we will see is that the other side of the PE will start to pair back, particularly over the next 6 months. That is where we see the opportunity to buy some high quality companies where we will see some temporary headwinds based on this rate environment, and this will provide us with opportunities over the next 6 months, in particular buying high quality companies which we have not bought for a very long time and valuations we have not seen for a very long time. As those opportunities arise, we will capitalise on those and ensure that obviously the next leap of our portfolio going forward. A couple of comments also I want to talk about and some things that we are starting to see the legal pressure on profits. You just need to follow Twitter for a couple of hours and you can start seeing all the noise from various pockets of Unions, of Politics calling for the large Australian corporate to hit back. Throughout the reporting season and speaking to the various management teams, we have all seen the theory of what politics may do to earnings. What this could do to wage growth. What it could do to the bottom line. Could there be Super taxes? It is something that we are watching closely. We have already seen governments get their hands on the energy transition, you have seen them get their hands on the games space and even on superannuation. Nothing is off limits and it is something that we are carefully evaluating when we construct the portfolio. What risk do we see around that political pressure which we have not seen for a long time? It provides another level of solid risk which we had before and we do not have to worry about in Australia too much but it is becoming certainly more and more present. What we would say is the portfolio is more balanced than it has been previously. There are stocks like Dexus, Treasury Wine Estates (ASX: TWE). These are the names that tend to drive the portfolio. We think that it can’t get any better, and it’s certainly going to get much worse. We have had a fall from COVID, we have had consumer balance sheets continue to shrink, disposable income is becoming thinner and thinner. From that standpoint we will continue to stick to defensive quality names in the portfolio and perhaps Anna can share a couple of examples of those.

Anna Milne: Thanks John. I thought I would run through one name that I have mentioned a number of times before. At risk of being a broken record, CSL Limited (ASX: CSL) is a holding our portfolio has held for a long time. We built our position around the middle of last year, as you can see in that slide. It really is a fundamental story CSL. Although the macroeconomics are not very favourable, it is highly defensive, and it is not related at all to what is happening in the economic environment. It is a fundamental story about a very well run business, there is a lot of growth levers which are all really coming to fruition over the next couple of years. Matt, John and I met with the outgoing CEO Paul just a couple of weeks ago, following the most recent results, and not only did we like all the insights into the financial and operational expertise of the company, but also the ethos and the performance mindset that they have and what is really driven their success over the last decade and the story we continue to like. It will remain a position in our portfolio for quite a while to come, I expect. I am fortunate enough to be travelling to Europe next month to talk to that next level down in the business at their operations in Switzerland and Germany, and I will report back after that but CSL is absolutely a key holding in our portfolio. I also wanted to touch on a couple of names that are slightly further down in our portfolio, and would not get a lot of attention previously and they are names that we actually built more recently. At the start of this calendar year Medibank (ASX: MPL) for example. I am sure many of you who are aware they had a cyberattack in October last year, according to the share price chart, and it was a big hit as you would expect. There was a lot of media sentiment that policy holders would be running in every direction and it would not recover its reputation. We let the air clear for a while, we didn’t touch it. Then we decided the fundamentals of the business were still extremely strong. Claims have come back a lot slower than expected from hospitals in terms of elective surgeries and again it is a defensive sector into slowdown given the tax implications for Australians. We built this position based on the sentiment and it delivered a really strong result. That is a name that we have been quite happy with, Medibank Private. The last name I wanted to talk about was Brambles. Now Brambles was probably another positioning story. It didn’t really participate at all in the rally at the start of this year despite what it looked to us like the fundamentals improving. The lumber price was falling and even though there is a consumer slowdown, they are mostly exposed to staples. Even if there is some weakness it might actually be positive is the outcome of the result and that if there is a destocking, there will be less pallet constraints and they will be able to get their pool operating more efficiently. We took a position in this late last year, we increased our position late last year and then had a good result. Brambles is a third name that I thought I would mention, and with that I would like to hand back to Bridget.

Bridget Thelander: Thanks Anna. We will open up for questions now and thank you to those who have been sending through all of these webinar questions. We will answer as many as we can and if we run out of time we will contact you after the call. We will begin with some of the questions that have been sent in from our shareholders. Matt, this first question is from Alex. He has asked what were your biggest takeaways from reporting season in terms of where the earning cycle is at?

Matthew Haupt: Thanks Alex. Great question. I will touch on John's point around government intervention. It was a common thing for our area and every CIO we spoke to. There is some wariness around potential intervention, we are very cautious and that is the biggest takeaway as far as where are we in the Union cycle. Everyone is uncertain, everyone is trying to get some clarity around the outlook and there is so much uncertainty at the moment, you can see that in the leading indicators. The key takeout was uncertainty, potential intervention and also the fight to reign in costs because inflation has gone through the top line and now inflation is coming through the operating cost line. In a moderating sales environment margins are going to come under pressure. In our minds the labour market has to soften. There was a few bright spots, I mean QBE Insurance Group (ASX: QBE) was an absolute standout result, they were benefiting from this period. Orora (ASX: ORA) was another great one, the Australia US packaging and beverage company. There were bright spots but overall the trend was a very cautious approach, very uncertain around government. It makes it very hard to get on with business when you have got such a negative environment. They were the big takeaways from reporting season.

Bridget Thelander: Thank you Matt and we will stay with you. Alex has also asked, given the dividend cuts in the mining sector and growing headwinds facing the banks, have you seen signs of a rotation in terms of earnings leadership from reporting season?

Matthew Haupt: Yeah a good question there. There has been a rotation in resources. Again, costs are becoming very high, and we have had a strengthening in the US dollar of late as the interest rate environment has tightened up in the US, which was predominantly the driver of some of the rotation out of the resources. It is not going to the banks. In the large cap stocks, out of the top 20 stocks, CSL (ASX: CSL) or the staples, there has been a bit of money into staples, but so far there has not been a clear trend. It feels like people are just holding onto their cash. Normally you would get a clear trend, but there has not been this time so we are still watching that one.

Bridget Thelander: And while we are on the topic of reporting season, Harvey Norman reported its result and we have had a few questions come in around that. What are your thoughts on the health of consumers in Australia particularly following the Harvey Norman result?

John Ayoub: Following on from earlier in our presentation, there is significant pressure on the consumer in Australia. The cost of living pressures and then the variable rate mortgages that were fixed rate mortgages coming through now. The consumer outlook is pretty bad and then February was terrible so again this is just the natural play out of that stress on the consumer after the irrational spending for a period even though we could all see what was coming. There was almost a ‘we are just going to keep spending until it all gets too much’ scenario and we are starting to see that now. Is it a sign of recession? I would say recession is a too strong a word. Recession in moderation from what we are seeing. Data today, it looks like a beat on the headline number but seasonally adjusted, it was actually weaker. It is coming through the broad retail sales numbers now and there is a weakening of the consumer. There are two sides of the consumer coin right now. Over the last 2 to 3 years we have seen a pull forward demand for at home products; the white goods, TV’s, you name it. Harvey Norman and JB Hi-Fi have benefited material over the past 5 years and from the pull forward demand the low rates and stimulus. What we expect now is that demand for furniture, for homewares, for white goods will slow down, material slow down, particularly over the next 12 to 24 months. The pockets of the consumer where we think may hold up are those that are spending on travel, entertainment and those exposed to the younger demographic who do not have a mortgage or seeing wage growth and spend more.

Bridget Thelander: Thanks John. And John, perhaps you can answer this next one. George says, where are you seeing the biggest opportunities right now and why? You did touch on this.

John Ayoub: George, thanks for the question. The stocks that we hold in a meaningful way within the portfolio that we think are standouts are Santos (ASX: STO), LendLease (ASX: LLC) and Dexus (ASX: DXS). These are the ones that stand out from a valuation standpoint. Santos is incredibly cheap considering its peers in Woodside and we think over the next 6 months we should see a bunch of positive news. I will not put a target price out there because it will come back to bite me, but we think that is there is potential upside. Stocks like Dexus, where is a discount on a certain 30% of its net tangible assets, we could argue that the NTA is wrong and we probably would say that the NTA is wrong. However it is best in breed and I think there is a middle ground which should be reached in the not too distant future because these are tier one office assets and they are mispriced. LendLease is one of those ones where I think over time if the equity markets are not going to value appropriately, I think the company will take measures into their own hands and start divesting things to make the market realise that the sum of the path is much greater than the current share price. They are the three companies in the portfolio that I will call out. Maybe we take the step below and look at names, the smaller names that we are looking at. Stocks like Dominos (ASX: DPZ) and James Hardie (JHX), A2 Milk (ASX: A2M) are names which are great businesses and you get to see get these things at depressed valuations following 1 or 2 growth earnings periods. These are names that you can field for a long term benefit for shareholders, they are the names that we are looking at closely. They are not true leaders of the portfolio today but they may be in the future.

Bridget Thelander: Fantastic, thanks John. And that leads in well, Anna I think you can answer this one. You touched on CSL, Brambles and Medibank Private, but Ingrid says, you mentioned some of the companies you are liking for the year ahead, can you please touch on the core holdings that contributed to outperformance in the 2022 calendar year?

Anna Milne: Absolutely, thanks Ingrid. It was a very volatile period and it is difficult to make any broad brush comments about stocks in particular that delivered that outperformance. There were times where we had to aggressively change our positioning based on changes in data, changes in expectations or changes in our own views. If I focus on the latter part of the year, the last few months, we took the macro point of view that we had reached peak rates. Rates were expected to fall and with that in mind we positioned heavily into Real Estate and Infrastructure. John mentioned a few of the names such as Dexus and LendLease but we also own Goodman Group (ASX: GMG), APA Group (ASX: APA) a gas pipeline company and Transurban (ASX: TCL) were names that delivered outperformance for us over that one quarter of the calendar year.

Bridget Thelander: Fantastic, thanks Anna. Matt this one is from Jarod. He says, you seem somewhat more buoyant on the economic environment ahead. What are your plans to continue driving solid returns in 2023?

Matthew Haupt: Yeah thanks Jarod. Buoyant would be an exaggeration of the economic view. The great thing is that the stock market is not the economy, which is hard to get your head around sometimes, but there is obviously a linkage through earnings, but there are also the financial conditions and interest rates which affect PE's. We are more buoyant because we can see that there is an end here. Before we relate, we are going through such an uncertain period. You had the fastest interest rate hike cycle in history. You had dislocation in markets in October and November with the global US dollar shortage and credit spreads flying out and we were in a position where our A list looked terrible. We are in a slowing economy and we would not be buoyant but we can see a path out of this. Before we were on a collision course, it did look terrible and now we can see a path out of this. In that respect, we are a bit more buoyant than where we were, but we are definitely constructive on equities in the latter part of this year. We think we are progressing nicely. We are going through the cycle without too many issues so far, there is a slowdown as we mentioned, but so far no dislocations yet. Again, the policy from here will dictate what path we go. The policy becomes too reactive late in the cycle and it can cause a lot of damage. We think the inflation moderation which we are seeing now, although in the short term, there is a bit of hawkishness creeping back in the Central Banks that will unwind as the economic data unwinds. We think the underlying data is weak which will be shown up later in March, April or May. That was a long way of answering but the environment for stocks will get there later this year.

Bridget Thelander: Great and I will stay with you Matt. This one is from Neil. He says in the FY2023 interim result the portfolio held over 25.2% in the material sector. Why were you so heavily exposed to this sector?

Matthew Haupt: We try and expose ourselves to areas with tailwinds and for us the China reopening became a significant source of opportunity for us. China never gives a direct signal of their policies but they will give clues along the way and every week we were getting clues around reopening, dropping zero COVID and stabilising the property sector. While that happened we built our position in materials and that is why we have such a large position, predominantly on China reopening. That played through and we have aligned it as the stock prices have reacted to the reopen.

Bridget Thelander: Thanks Matt. And John this one is from Philip. He says, has the increase in CSL's share price made you think that you should sell some shares?

John Ayoub: Thanks Philip. I will lift the hood on how we do things in team leaders. We wake up every day and ask ourselves the question, if we did not own a stock today, what weighting it would it be in the portfolio at the current share price? History does not dictate what we do. It is what we think in terms of what the future of that share price is going to do and we pride ourselves on active management. If the share price is getting closer to our target price, absolutely, we will trim our holding. Equally if it falls back to somewhere where we think is attractive, we will increase that holding. In short, above $300 dollars we did trim some of our CSL, but back into $290 we will increase it again. That is one thing we do pride ourselves on, we revise that decision making process and we try to come with a neutral view and an open mind every day.

Bridget Thelander: Thanks John. Anna, Marcus has asked what are your thoughts on Telstra (ASX: TLS)?

Anna Milne: Thanks Marcus. Telstra had a rock solid result and the main question from here is, are they going to increase mobile pricing by CPI come the middle of the year? In the last 12 months they have done the hard work moving everyone onto contracts where they can escalate it by CPI, but they are now worried that if they increase it by this March it is going to hurt affordability. As we discussed earlier, it is definitely a wait and see environment, but it appears Optus and TPG are still earning well below the returns that they expected. The other question that we are often asked on Telstra is, do you think the dividend safe? I think it is fair to say that it is safer than houses at the moment. The market has a 17 cents dividend to FY23, 18 cents dividend by FY24 and then 19 cents dividend by FY25. Your Telstra dividend is safe.

Bridget Solander: Fantastic thanks Anna. This next question is for John. Marianne has asked about Qantas (ASX: QAN). She says the recent half year profits from Qantas are impressive. Do you think the airline can maintain this despite several safety incidents and a struggling brand image?

John Ayoub: All valid concerns Marianne. I think they are in damage control from a company standpoint. They realise they went too far from a cost standpoint; they went a bit too far on the consumer. Firstly, around their earnings, it is a question around demand and we think you will get peak demand later this year as capacity starts to come on from international players. I think we should start to see that price and the issue around price abate a bit and you will not be spending $20,000 dollars to get your business class seat to New York, if you are lucky enough to fly business class and you will not have to pay $5,000 dollars for your economy seat anymore. I think we will get a normalisation around the price of airline tickets back after this year as that capacity comes on. Naturally that means Qantas' earnings probably comes back somewhat. They need to put more capex into the business and they have discussed putting additional fleet and newer planes into the system. Arguably you can say that you are probably towards big earnings for Qantas this year and then what does the business look like next year? They have rapidly wound down in their debt position and from the capital standpoint, they are in a really strong sound financial position. In Australia, if you look at the documents coming out from Virgin, I think competition problems are going to be a little bit more benign than it was in previous cycles. Domestically, I think Qantas will continue to earn strong profits and internationally will pare back a bit but we still think I it is okay for the time being.

Bridget Thelander: Thanks John. Anna this next one is for you. Heidi has asked if you can please talk to a few of the positions that you have added on the back of good reports this earning season?

Anna Milne: Thanks Heidi sure. These are the names from our top 20, but I like them because they have been ones that we have been adding to or may intend to add to depending on price movements. The first one is Endeavour Group (ASX: EDV). We think the market is underestimating just how defensive their portfolio is and as a team we met with the new CFO Kate and we think she is an excellent hirer and will do an outstanding job. We like Endeavour Group at the moment and another name that Matt mentioned earlier was Orora. They dispelled concerns with their US business at the result as everyone was really worried about the declining eCommerce environment. In Australia it is a fantastic business with big capex plans but big returns from that capex. We like Orora, that is a small name in our fund at the moment. The last name I call out is National Storage Rate (ASX: NSR) and I think the storage story is quite an interesting one. Their top line is growing extremely strongly from a price perspective and again there has been some concerns around occupancy and how defensive storage is but they talk to the 5D's which drive occupancy being Debt, Divorce, Downsizing, Dislocation and Disaster and that all sounds quite defensive to me.

Bridget Thelander: Thanks Anna. Matt we have had a couple of questions on this from Krishna and Mowha. They have commented on the profits reserve and franking balance. Is there enough to maintain the current dividend?

Matthew Haupt: Yeah, thanks for the question. We are in a very strong position on the current run rate, it is almost 5 years of coverage. An incredibly strong position with respect to the potential to pay dividends. It is a Board decision what they do with that dividend coverage, but incredibly strong position. Barring unforeseen circumstances it is hard to see it not being paid for a long period of time, so that is about all we can probably say on the dividend front given that it is a Board decision, but they are in a great position to make those decisions.

Bridget Thelander: Thanks Matt and the next one is for John. Ivan says, reflecting on the past year, what could you have done better? Has this taught you anything for the year ahead?

John Ayoub: How much time have we got? There is probably three things that stand out that as a team we probably could have done better. The first one I'll call out is James Hardie (ASX: JHX) and Reliance Group (ASX: RWC). Our process and what we pride ourselves on is top down bottom up when we try to identify those stocks that had that tailwind and we went too early in James Hardie and Reliance towards the back end of last year. We built a sizeable position a little too early and they both downgraded twice. We did one the first time and we doubled down the second time and got hit again. I think from a valuation stand point, when you are going into the cycle, the stock cycle that we are seeing, valuations are irrelevant and the headwinds and the rapid decline that we saw in housing demand in the US we missed. That was probably the first standout that we got wrong. The second one was Ramsay Healthcare (ASX: RHC). We got a little bit too close and fell in love with that investment when the takeover was happening and we were looking at the $80 dollar takeover price in opposed to the reality of what the market was telling us. $88 dollar share price I should say. We missed the fact that their markets were closing, it was becoming increasingly difficult to get access to the funding to complete this transaction and the underlying business was deteriorating also at a rapid great of knots. Those two probably were the standouts and I think I have got another question on this in a minute on Star Entertainment Group (ASX: SGR).

Bridget Thelander: That is the next question that has come through and we have been asked this a few times. Can you explain why you hold Star and provide your updated thoughts on the stock after the recent fall in share price and the capital raise?

John Ayoub: First of all, we had a really good experience in Crown (ASX: CWN) for the first half of last year where the demand for these elite critical tourism hubs we thought were undervalued stories and we had a very good experience with the shareholders in the Crown takeover and made significant returns there. We quickly pivoted from Crown into Star and again probably went a little bit too early and we sold all that at $3.00 dollars. I think if you recall around the AGM we were watching some concerns around the sector and towards the back half of last year we started to sell some thinking that we got some insight from the Crown's update. We tried to sell it a little bit not quick enough and not fast enough and nowhere near enough. You saw the first downgrade, but what really caught us off guard in Star was the Treasurer, New South Wales Treasurer Matt Kean's land grab. If I can kind of speak out of school for a second, that was probably the worst policy I have ever seen any politician come out with when you have a four year agreement by a contract and you kind of go in there and change that agreement, it makes it very difficult for investors to get any confidence in investing in New South Wales going forward and given the significant investments that is required for the Green Energy Transition, it makes it very difficult to trust a government where they are willing to change a contract based on by changing legislation to do a quick little land grab on tax and trying to get a hundred million dollars ultimately cost the government a lot of money. Putting that to one side, we were caught off guard. The company got caught off guard. Everyone was caught off guard with the announcement around the extra tax and that saw the share price spiral from $2.50 down to $1.90. That is when we actually built a significant position at $1.90 and then as it panned out, the asset was written down to $1.6 billion dollars and the deterioration in trading and the slowdown of costs saw that downgrade in early February. We doubled down in capital raising at $1.20 and we made 25% out of that capital raising. What does the share price imply? You have got two wonderful assets up in Queensland which are owned and unencumbered and you have a 70 year leasehold asset here in Sydney that, in the absence of reform from the government, and we're quite optimistic that the government will actually see the light and do a huge turnaround those tax changes, that they have kind of commented on you will see significant cost out program here in Sydney. If anyone wants to talk more about it I'm more than happy to take it offline and provide more context but it is one that we got wrong. It hurt, but you know we've had some wins recently from the government capital raising and we are not quite in front of the old cost base, but we are not far away.

Bridget Thelander: Thanks John. This next question is from Gary and I think John this might be one for you too. He says with mining stocks now coming under pressure and experiencing price pull backs, how are you handling these changing circumstances?

Matthew Haupt: I'll take this one. The stronger US dollar from potential higher Fed rates is one area we are a bit cautious about. The fundamentals look okay but the economic or the macros framework is getting a bit tighter and we have taken a little bit off the table but we are looking to add to them over the next period. You have got industrial production in commodities like copper and you have got the ED metals. It is hard to characterise them all at once. Industrial metals, copper, you cannot really get any exposure anymore. We had Oz Minerals but unfortunately, that's gone and CFI just doesn't quite pass the quality test for us. We do own a little bit of lithium through Allkem (ASX: AKE) and Pilbara Minerals (ASX: PLS) and a bit through West Farmers but short term emphatically reducing it a bit and then long term we will probably add to those names. Iluka Resources (ASX: ILU) is probably a bit of a call out as well. Iluka is a call out but again, the way we operate is very tactical. If we love the fundamentals but the backdrop changes we will move to take account of the backdrop and then we will add back into them.

Bridget Thelander: Thanks Matt. We'll stay with you again. This one is from Rob. He says, Mike Wilson from Morgan Stanley seems convinced that the US equity market will suffer a major correction this year and most recently has suggested it will occur in the northern spring. If this does occur, Rob is keen to hear your thoughts on:

1) The likelihood and extent of contagion affecting the ASX and:

2) hether Australian investors wishing to substantially increase their holdings in local equities might be advised to wait a while?

Matthew Haupt: I mean the consensus in the US from the US strategists is very bearish and it is almost like the economy and the backdrop is coming up bear and they are doubling down on their bets. I listened to him the other night and it is quite depressing when you listen to him. I sympathise with that view and we all sympathise with that view because it is a possibility. We are all going into this unknown period after that rapid rate hike. To go back to the end of 2019, 2020 the world was heading into a recession, global growth was slowing, the

Fed had stepped in trying to put liquidity into the system and then you had COVID hit and massive monetary policy distorted everything. You have had opening up of economies at different stages, and we are coming out of this in an incredibly tough period to forecast. What we have got to do though is look at consumer confidence and leading indicators which are at all-time lows. The lows are comparable to the GFC and to the dot.com bubble, so there is a lot baked into expectations of how bad things will get. To see a massive spiral here, thee will have to be an event where liquidity dries up, the banking system shuts down, like a massive credit cycle and we don't see that happening at this point in time. There is a possibility though if the Feds stay high and keep hiking throughout this year, 100% we could go into that scenario. With everything in front of us at the moment we don't see that doomsday scenario playing out. If that did play out, would it cause contagion. Australia is an open economy, it does follow a lot and if the US fell by 20% we will have to borrow as well. Not to the same quantum because we have may see China propping us up a bit, but we would have contagion. The way we look at it in the portfolio in WAM Leaders is we are positioned relatively defensive with quality throughout the portfolio. We're not opening the portfolio up for risk at this point in time and by risk I'm meaning at the cyclical front end of the cycle. The way we manage the money is, we work out where we are in the cycle, how supportive the backdrop is and then we will pull the levers. The lever is pulled back at the moment, we are a bit cautious but that can change in a heartbeat. It could change if you had a sudden dramatic fall of inflation and policy to fall away but we don't see that doomsday scenario playing out. We have not entertained that yet, but if that did play out we know exactly what to do. That is the advantage of our investment process, we can pull those levers pretty quickly.

Bridget Thelander: Thanks Matt, let's hope that doesn't happen. The next question is from Ian and perhaps you can take this one Anna. He says thank you for the excellent result. Could you outline why you prefer Transurban to an investment in Atlas Arteria?

Anna Milne: Thanks Ian. Firstly just highlighting they're both in our top 20 holdings, so we like both companies and I would say TCL is extremely well run and it has a greater CPI link and as we know once tolls go up they don't come down. That can only really be beneficial for the TCL. The main reservation will be the CEO stepping down at the last result. Like any CEO change, it does provide a bit of uncertainty, but we do like both names.

Matthew Haupt: And at this stage I think the disruption to the French economy last year through the diesel shortages and strikes really affected traffic volume, ANX probably has more of a tailwind through traffic volume going into this year than the Transurban, but TCL is actually a higher weight in our portfolio. It is almost double the weight than ANX and we actually do think TCL is a higher quality.

Anna Milne: ANX also has the organic side of it. They recently purchased Chicago Skyway.

Bridget Thelander: Thank you and this next question from Andrew. Geoff is not on the call but perhaps John you might be able to take this one. He says, can you explain the logic of stockpiling so many years of dividend reserves unless they're being built up for another like takeover to distribute across a wider shareholder base?

John Ayoub: Thank Andrew. These are Board decisions and Geoff is the Chairman and the Board decides what a sustainable level of dividend payments is and I think what we articulated as a group from day one was we wanted to grow a steadily rising stream of fully franked dividends. We have been able to do that since Leaders inception nearly 7 years ago and we continue to grow that dividend. At the end of the day, that is what the Board is trying to do is create that sustainable level of dividends. Hopefully we will be able to continue to drive that growth.

Bridget Thelander: Thanks John and we might stay with you. We have a question from Scott. He says, which lithium miner would you buy into?

John Ayoub: The cheapest one on the ASX is Wesfarmers. If you go down the quality spectrum, Independence has probably got the best assets and Babylon and mineral resources are pure players. Those two have the best hard rock assets in the country, closely followed by Pilba and APE at the next level down. I think at the end of the day it is more about picking down to live commodity and Pilba demonstrated that it is operationally sound. There are some headwinds and for us, I think you will probably see a pullback in lithium pricing over the next 6 months.

Bridget Solander: Thanks John. Matt this question is for you. Joseph says, the world is very volatile right now as you have just discussed. Will your team think about capital management initiatives such as and other rights issue so that the team has power to invest?

Matthew Haupt: Again that is simple a decision… those sort of discussions happen at the Board level. We try and manage the money to the best of our ability and we just focus on doing that every day. Capital management is really up to the Board. When they meet and if they want to grow, we would love to have more money to manage because there are lots of opportunities out there at the moment. John and Anna have touched on some amazing and companies at depressed valuations so 100% but that is completely up to the Board.

Bridget Thelander: Thanks Matt. We'll stay with you and we have a question from Noel. He says, why is Macquarie Bank not in your top 20 holdings?

Matthew Haupt: Noel good question. It was for a period for about a month. It goes back to the process, the fundamental story is still intact. We like Macquarie. We have since reduced it, so it fell out of the top 20 and the reason why we reduced it was the stock had a great run. Again, the interest rate environment was changing and the strong US dollar was enough for us to change weighting of the stock, but we're looking for a re-entry into the stock because fundamentally we like the story. It goes back to our investment process where we are always trying to make money, if we can move the capital around somewhere where we think we can make more money then we will do that and that was purely the case at Macquarie. It is such example of how to run a company, incentivise the right people, let them take risks and you have seen the rewards over multi decades.

Bridget Thelander: Thanks Matt. And I think John this next question is for you it's also from John. What is your view of gas and oil stocks going forward in particular Santos and Woodside?

John Ayoub: Earlier when asked what we got wrong, Woodside is probably one of those answers where the demand for Woodside from international investors is something that we did not foresee. Where we look at the valuation disparity between the two today, Woodside is at a 40% premium to what Santos is trading at and the growth profile, the yield and the quality of asset compared to that global set has seen Woodside become one of the global mini major which is very much loved. Unfortunately for us here, our preference is Santos as it's yielding more, it's undertaking a buyback and it has missed that re-rate. What we see today is that Woodside is a great company run really well. We see insignificant capex coming for that organisation and we probably have limits around the upside, dividend and any potential capital management buybacks. While we look at Santos and we think that it was ready to complete the sale of PNG LNG, they have some finality around the Alaska investment and you can start to see through press and that there is a resolution there coming. We see significant capital management in the way of buyback, continue growth of dividends and operation I think they have had a few hiccups over the last few years but we still believe in Kevin Gallagher the CEO and I think they will get back on the right track, so that valuation disparity between the two will be remedied.

Matthew Haupt: Looking at the commodity it was showing you that there was weak demand for oil and that is due to the softening of the economy. China from our estimations could be an extra five hundred to probably 1.5 million gallons today as you get mobility going back into China. We have had Russia cut an extra five hundred thousand barrels a day and the supply side is matching that and we do think China's mobility will be a key theme throughout this year. The strong US dollar is not great positioning wise, but the positioning of oil… the people who move money around the CTA accounts which are Commodity Trade Advisors they are all net sure oil and we are not that worried because they have already positioned for a negative oil price. Therefore w are quite constructive on energy. We think the oil price is okay this year due to the supply side and Santos is just an absolute stand out on valuation. It astounds us and it has been astounding us for 2 years unfortunately on the valuation. That has to change, it just has to change.

Bridget Thelander: Thank you and perhaps now turning to the banks. Matt, Ashok has asked what is your view on the banks for the next 12 months?

Matthew Haupt: Yeah Ashok good question. The CBA really scared everyone out of banks and it is really competition and it has been so intense. Some banks are offering $4,000,

$10,000 dollar cashbacks for mortgages and that constructive environment has been competed away unfortunately if you are a bank shareholder. Once that competition falls away, which we do not think it will, we are probably the largest underweight we have been in Australian banks for a period because we are seeing credit growth slowing, MIN contraction where we thought MIN would be extended for another 6 to 9 months. We see the bad debt cycle starting to tick up and then you have got government pressure again. ASIC is talking about deposits and competition and we think in the May budget is going to happen there with government intervention in the banks again. I mean we have already seen a bank tax previously, but we just feel like there are headwinds stacking up for the banks. We love the Management teams, most of them are all high quality. It is hard to make a constructive case for the Australian banks unless valuations pull back to make them more attractive, but at these levels we are happy to stay out of the way in a large manner unless something changes.

Bridget Thelander: Thanks Matt. And John over to you. Graham has asked are you considering buying the Lottery Corporation (ASX: TLC)?

John Ayoub: We do own that below the top 20 holdings that you get to see. When the split occurred between Tab Corp and TLC, we categorised it as the best company in the ASX and the worst company in the ASX splitting and TCL being the best company in the ASX because it is just such a high quality reoccurring annuity style business. Tab Corp has been very easy to stuff up over the years. If you saw the most recent result they have been able to navigate and provide some clarity around what the jackpots need and should look like, what the earnings growth should look like and whether they have potential upside and repricing and the likes. We think it is a good solid core holding. It is definitely a name that we would love to increase in the right environment.

Bridget Thelander: Thanks John. And Matt this one might be for you. John has asked how does the WAM Leaders team weigh up quality against value for an investment?

Matthew Haupt: Yeah that is… there's obviously some strict definitions in the textbooks, but I mean the way we look at it is, when we look at quality when talking about the sector they operate in, the characteristics of that sector and it's management team. Management team is a massive one for us. Throughout the year we go and see all the management teams, we sit down with them and we are looking for strong leaders with clearly articulated players as well. In short, there is a whole raft of things we look for in quality. In the textbooks you get the value market; the growth market and we don't like to pigeon hole ourselves into those buckets. We try and assess quality in those things that I mentioned. We have got so many factors we look at to assess the quality of a company. The one thing I will mention is when it comes to quality versus value versus asset backing, the way we control risk is by the size and the position and quite often a quality stock has a lower level of embedded return in it but what we can do to get to maximise that return is that a larger position in the portfolio. Typically we will have those the risk controlled by deciding the position in the portfolio to provide more context on how we do it day-to-day.

Bridget Thelander: Thanks John. And I think this is the last question that we have time for, it is from Asher. He says is there any chance to increase the portfolio exposure to the tech sector going forward?

John Ayoub: Slim pickings.

Matthew Haupt: I know. We love a quality tech sector, unfortunately we don't have a huge tech sector which is quality. What we are looking for is the backdrop, do not rule it out but once we get the backdrop which is conducive to the tech performance, 100% we will up the weight there. We have had the peer re-rate in the market and that's going to unwind over the next month or two and then that may be our opportunity to go back in there in a more meaningful manner. We must have the right framework and the right environment for us to push that lever and we do not have that at this point in time.

Bridget Thelander: Thanks Matt. That is all we have time for. Thank you everyone for sending through your questions and to Matt, John and Anna for joining us today. A recording of the call will be available on our website shortly. Matt, do you have any closing remarks?

Matthew Haupt: Again, we are all working extremely hard through this cycle, we have been through this before, we are trying to pull the right levers at this point of time, the cycle is progressing as we had thought and we are quite comfortable how we are positioned. I would also like to thank everyone for their continued support and look forward to catching up next time.

Bridget Thelander: Thanks Matt and as always please get in touch with us by phone or email at any time with any questions or feedback that you have. Thank you.

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