Apostle Dundas Global Equity Fund

Quarterly Letter - Q4 2022

Dear Investor,

We are sending this letter to provide you with an update for the fourth quarter for the Apostle Dundas Global Equity Fund. Further updates are available through our monthly factsheets, quarterly reports or better still speak with our Sales Directors at Apostle Funds Management.

Markets

Global equity markets jumped in Q4 2022. MSCI's All Country World Index rose 9.8%, the EAFE + Canada index gained 16.2%. While these advances were welcome, they were not big enough to offset the damage done earlier in the year. MSCI's ACWI and EAFE + Canada indices were down sharply in 2022, -18.4% and -14.3% respectively, all in USD terms.

Three big stories grabbed the headlines and shook investors.
First, Russia's invasion of Ukraine. Almost a year on since the news broke, we may be guilty of becoming familiar with it. That would be a mistake.
Second, inflation rose swiftly and sharply across the world, partly thanks to the spike in energy prices following the Ukraine invasion, partly from supply chain pressures which arose in Covid-related lockdowns, and partly from tightening labour markets in developed economies.

Third, bond yields rose in response to renewed inflation but not by enough to maintain investors' real returns. Ten year yields in the USA and Europe remain below prevailing inflation rates. Central banks were slow to increase policy rates at the start of the year, probably because of anxiety about making a bad situation worse in the real economy.

The combined weight of these concerns drove down equity valuations. The MSCI ACWI's Forward Price / Earnings ratio was 18.2x at the end of 2021 and 14.6x at the end of 2022. The equivalent figures for the MSCI EAFE + Canada index were 15.2x and 12.1x. 2022 was a year when Mr Market's anxieties determined the returns all of us earned.

In contrast to declining valuation, dividend growth remained healthy in 2022. MSCI ACWI's dividends rose 9%, EAFE + Canada dividends rose 9%, boosted by earnings and distributions from oil and gas companies. We estimate that the portfolio's 2022 underlying dividends rose by 19% in local currency, with up to half of that figure representing recovery from supressed or omitted dividends during Covid lockdown. Average reported dividend growth was 10% in the fourth quarter, with the element of recovery all but passed.

Performance

Gross total return was 4.61% versus the index' 3.96% gain.
The rally was broadly based; nine out of eleven GICS sectors rose. Consumer Discretionary was the worst performer in the index but good stock selection alongside an underweight position delivered the biggest contribution to the Fund's relative return.

Zero exposure to oil & gas stocks detracted as it had done throughout the year, but the effect on relative performance was negligible.

Stock selections in Health Care and I.T. had a positive impact, however the Fund's overweight to I.T. hurt performance. Financials, Consumer Staples and Industrials were the biggest detractors from a selection perspective. Also disappointing was stock selection in Materials and Communication Services.

Selection within and allocation to North America were positive factors. The overweight to Europe was positive, offset by stock selection. Both stock selection and allocation within Asia were negative despite the portfolio's holdings in Hong Kong's AIA Group and India's HDFC Bank performing well.

Outlook

Short-term market movements based on greed and fear can be vicious, but they are just white noise. Equities' excellent record of beating inflation rests on long-run real dividend growth. Long-run equity return potential is signalled by dividend declarations, the milestones marked as companies make progress in sales, profits, cash flows, reinvestment, and dividends. Corporate profits drive those returns via dividend growth which we monitor in two ways.

(1) Dividend declarations in the quarter had an average increase in local currency of 10%, the average for the year was 17%. Stripped of post-Covid recovery, the underlying growth rate is closer to our long-term experience. Measured in USD, reported dividend growth in 2022 averaged 15% versus 9% for the MSCI ACWI. 2022 has seen a wide gap between market valuations on one hand and, on the other, earnings and dividends. Fundamental growth met Mr Market at his most anxious. The Fund's valuation on a forward price to earnings basis finished the year at 20.3x versus the opening 27.2x, a drop of 26%.

(2) Our dividend growth indicator implies 11.2% future growth versus 7.9% for the MSCI ACWI ex Australia index. Maintaining that premium is essential for the Fund's long-term success.

What are 2023's biggest risks? A widespread recession which would reduce profitability and slow dividend growth. Of the present suite of concerns that could tip us into recession, the most serious would be a further big rise in interest rates leading to people not being to afford their mortgage payments. Consumer demand would decline, banks would suffer impairments.

Companies make profits by supplying the goods and services that customers – consumers, other companies, governments – need and want. Great companies reinvest most of those profits to support future growth via capacity expansion and productivity. Profitability and reinvestment are the foundations for future dividend growth, and over the long-term outperformance. We have seen no reduction in the portfolio's reinvestment rates.

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