Q1 FY21 STATUS REPORT

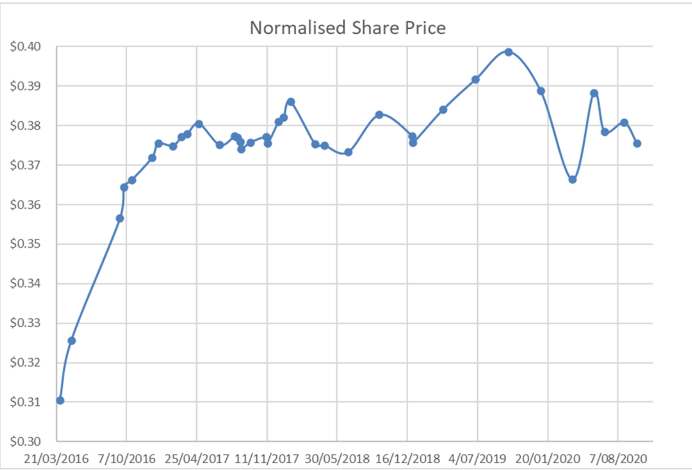
Investment Performance of Deployed Capital

Auduco Pty Ltd's current investment position and normalised share price are summarised in the table and figure below.

30/09/20 Snapshot		
Top 5 Equity Holdings	Ave Entry Price	Market Price
ANZ	$23.43	$17.22 (Q1 perf: -$1.42)
BOQ	$8.13	$5.73 (Q3 perf: -$0.47)
NAB	$19.01	$17.75 (Q4 perf: -$0.47)
WBC	$16.18	$16.84 (Q4 perf: -$1.11)
WPL	$23.28	$17.58 (Q4 perf: -$4.07)
	Current Market Value	

FY21 Dividends to-date	
FY21 Interest to-date[1]	
Cash Holdings	

Note 1: Does not include interest currently being accrued in term deposit accounts.



More of the same remains the situation. However, the backdrop is that while markets continue to advance, signs that not all is well continue to metastasise. We are experiencing this right now with the portfolio. Capital value is holding up ok, despite the holdings underperforming. But now, dividends are drastically reduced across the board. NAB $0.99 per share down to $0.30, ANZ $0.80 down to $0.25, BOQ currently at zero. Interest has dropped from ~2.7% to around 0.7%. The dividends are expected pick up again but right now it feels reward for following the Benjamin Graham / Warren Buffett playbook will still be a while coming. It is difficult to imagine Buffett thinking the current reality was ever possible. The worst thing to do right now is act rashly. We have made our key baseline acquisitions and simply need to hold and watch for the next targets.

The sheer scale stimulus, now coupled with enormous government support for main street (much of that misallocated to hands that do not require it), keeps the markets elevated.

The other backdrop to bear in mind in relation to all that stimulus and our holdings is that Australia's share market (XJO) is lagging pitifully relative to overseas. The local market performed poorly during the quarter. The uptick to the right of the chart below is from the subsequent quarter. The USA is, again, the stellar outperformer. Here is a visual (XJO relative to the S&P 500 since the new year):

It is a far more drastic difference when comparing to the NASDAQ: ~35% instead of ~13% when comparing underperformance relative to the S&P 500.

Both US indices have touched new alt-time highs. The NASDAQ is well above its pre-Covid highs. That is, 100%+ recovery. Yet Australia has only recovered 64% of its market losses.

Many commentators, bullish ones at that, are suggesting that we should start to see capital rotation into value. The basis of the argument is their long standing under performance....the winners, grossly overvalued tech stocks surely can only go so far before the penny drops. And with central banks having no choice but to maintain stimulus, it makes sense for assets with intrinsic value to start seeing some inflows.

System News

On the trading system we are working through the nuts and bolts of setting up for routine scanning, analysis and communication of alerts. It took the whole quarter to find and open an account with a broker with the appropriate platform APIs to enable data filtering, analysis and alerting in real time.

The key activity in the short term is to establish a feel for the frequency of alerts, repetitiveness and perceived versus actual reliability. This is a take time to observe the alerts and price action wash through process, and get used to how that works in with daily routines. There are critical psychological elements to this. For example: macro's and fundamentals do not matter to the system, but it can be difficult to wrap your head around long signals at obscenely over priced levels and then reconcile in hindsight that restraint lead to significant opportunity cost. At some stage we will need to establish the jump off point to take trades of appropriate position size.

Synopsis

The theme: the expectation of what is to come is more of the same….stimulus. With far more stimulus thrown at markets since March than the past 12 years combined, efficacy is not really a problem any more. We have shown previously that proportionally more money is required to both increase GDP and market capitalisation as stimulus continues. But there is now no more calling what the Fed injects as surgical. They have metaphorically fired a bazooka at it and the market has responded. The word "bazooka" might actually be underdoing it in this analogy.

Betting odds are now firmly in favour of Trump losing the election.

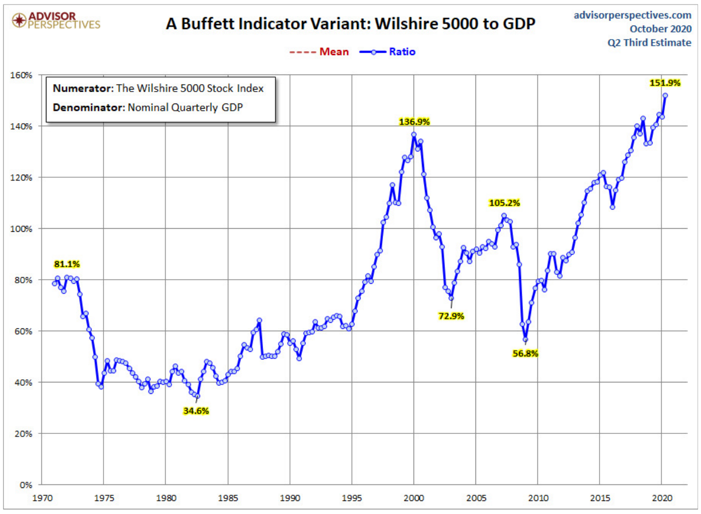
Many would believe that a Trump loss would be bearish for markets. But if Biden wins the election, the fiscal result will be more of the same[1]:

- Further stimulus. Austerity is no longer and option. We saw the **markets drop every time the Fed attempted to pare back stimulus and reduce its balance sheet** – the markets experienced minor panics (in the scheme of things) and the Fed placated it soon after.
- Rising US federal debt, surpassing levels reached in WWII.

The result will be negative real interest rates. There is also potential for some rapid material devaluation of the US Dollar.

In such environments the recommended theme is to invest in real assets. Gold, real estate, equities and commodities (especially critical materials for new technologies) all offer a hedge against inflation.

In the meantime, valuations continue at extremes. Here is the Buffett indicator, at all-time highs:



We are also seeing that not all major indices are at ~ all time highs like the Nasdaq and S&P500. The Dow Jones Industrial Index (DJIA / $DOW) paints a different picture. It has been consolidating in an increasingly volatile megaphone pattern while declining Money Flow suggests long-term selling pressure.[2]

Also interesting is the S&P 500 is showing bearish divergence based on the Twiggs Money Flow indicator, as hopes of achieving a further stimulus deal in the USA prior to the election is fading. Trump tweeted a declaration (early Oct-2020) that all negotiating with Democrats was to stop, but spent the rest of that day indirectly backtracking.

Surprisingly, the Australian XJO is trying to break out through key resistance at the time of writing. Until next time.

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[1] Some things will be different. Government will lean toward:

- Higher corporate tax rates in an attempt to slow public debt growth and avoid the tipping point where debt servicing costs exceed tax revenues.
- Higher personal tax rates for high income-earners.

[2] From Colin Twiggs / The Patient Investor Newsletter; https://thepatientinvestor.com/