

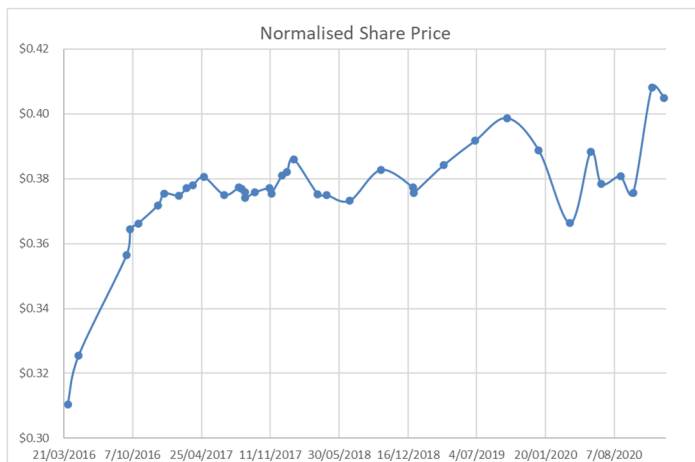
Investment Performance of Deployed Capital

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

31/12/20 Snapshot		
Top 5 Equity Holdings	Ave Entry Price	Market Price
ANZ	\$23.43	\$22.70 (Q1 perf: \$5.48)
BOQ	\$8.13	\$7.74 (Q3 perf: \$2.01)
NAB	\$19.01	\$22.60 (Q4 perf: \$3.59)
WBC	\$16.18	\$19.37 (Q4 perf: \$3.19)
WPL	\$23.28	\$22.74 (Q4 perf: \$5.16)
Current Market Value		

FY21 Dividends to-date	
FY21 Interest to-date¹	
Cash Holdings	

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



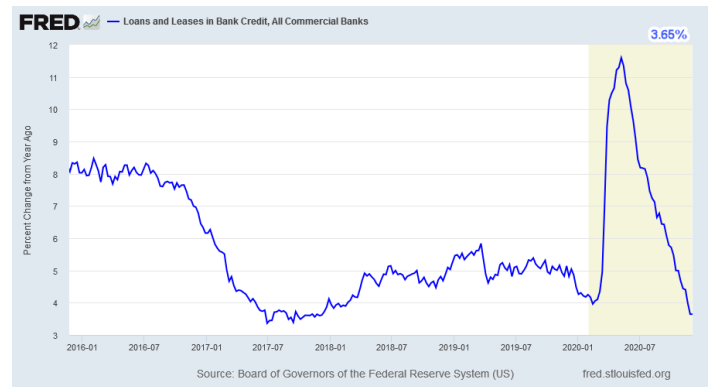
The Australia's share market (XJO) has spent this quarter playing catchup with international indices (see chart below). Many blue-chip stocks, including our larger holdings, have broken out of long basing patterns to drive this catch up. This has also resulted in our normalised share price (chart above) reaching its highest point.

Synopsis

There is not much to say on the macro front in this update so, this will be brief to enable us to discuss system testing later. The situation with the metrics remains the same with valuations becoming more extreme. The everything bubble of epic proportions continues to become more epic. Lots of speculation out there, which is fine, but professional advisers continue to highlight the importance of gearing toward more defensive investments.

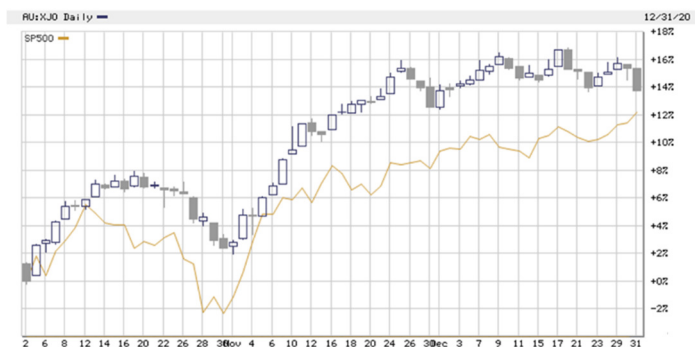
Stimulus remains the theme. Central bank and governmental fiscal stimulus have continued to win the popular unofficial argument that "fundamentals do not matter so long as interest rates remain low." From our point of view, we are entering the 4th year of this kind of complacency gone too far, i.e. crazy times. Multiple parabolic moves in indices, synonymous of market tops, yet with no sustained bear market to flush companies with poor fundamentals...strange times.

When will it end? Most often, it will be down to credit impulse. When bank credit growth falls below zero, that's when stocks are likely to tumble into a bear market. It remains above 3%, defiantly in our view, as we have often thought it on a trajectory to zero (usually accompanied by our observations of Europe and China).



Until then it will be as we flagged in the last update: more of the same as Biden takes office – stimulus and rising US debt. We called the Biden win (the betting agencies (not polls) that swayed us usually get it right) and are relieved that he got over the line. We observed the positive appetite for the Biden victory with markets surging from the beginning of 3-Nov. It only pulled back for the brief period that it looked like Trump was in the running, falsely claimed victory and started demanding that the counting stop.

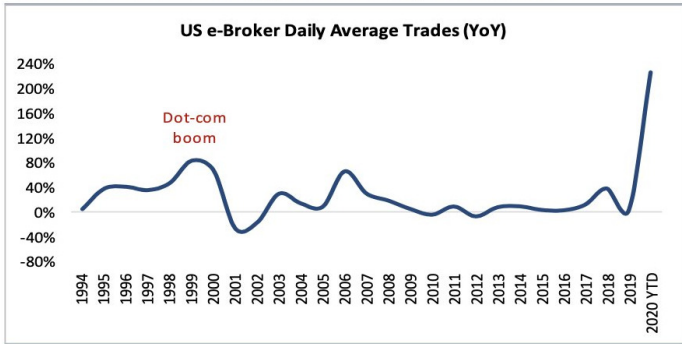
We saw a sharp drop in the US dollar this quarter, corresponding with devaluation expectations, but note it has not fallen below its 5-year range. These devaluation (hyperinflation) expectations have existed for decades. When it will finally fall off a ledge is something most forecasters will continue to get wrong while it remains the global reserve currency. Whether it corresponds to a market crash is another coin toss. Under the right combination of factors, rapid currency devaluation can lead to massive gains in local asset prices.



Dividends are now being paid across the board again but remain at much lower payout ratios. Interest rates on term deposits are now pitiful. We will now dovetail to a brief macro synopsis and

The standout observation of the year was rise of the retail trader and their rush to markets:

Chart 37: Retail trading growth has exploded in 2020



An article by Real Investment Advice explains how this has occurred through a **combination of RobinHood trading accounts, stimulus cheques and gamblers turning to stock trading due to sports gambling being shut down during Covid.**¹ We recommend reading it. It also demonstrates how Robinhood use the guise of zero brokerage for retail traders but sells that data to hedge funds to enable them to **front run** stocks. That would be illegal for almost everyone else.

System News

During the quarter we have been configuring the trading system to different markets and observing the frequency of alert generation. This has all been part of the working through of the nuts and bolts of setting up for routine scanning, analysis and communication of alerts.

System Test

During the back end of the quarter, we performed some trades using system rules for entries as an exercise in re-acclimatising to executing rules. This was performed on local stocks. Most stocks selected were sub-ASX 200 level. The basis for the decision to go this way was:

- Lesser capital requirements and more easily accessible;
- Asymmetric risk-reward ratios (sectors targeted were commodities and healthcare - one an established performer, the other gaining traction); and
- Being Australian stocks, whilst they can outperform, they often do not, hence a successful test bodes well for other markets.

The results of the trading are summarised in the table below.

The win rate (or in-front by end of period rate) was pretty low at 44% (the system has been tested to achieve 55-65% over the long term). This is would normally not be unexpected when trading less-liquid equities. That being said, the biggest loser was an ASX 200 stock. Since the test period cut-off, the 44% has proven to be an artificial measure as the majority of remaining open positions are in profit at time of writing.

As we were working these trades, it did not feel that the outcome would be as good as it proved to be. This is part of the psychological aspects that need to be worked through. The test outcomes demonstrate the need to continue to work the process

regardless of personal sentiment. The more we trade the easier this will become.

Q2 FY21 Additive Directional Trading System (ADTS) Test						
ASX Stock Symbol	Entry Date	Entry Price (\$)	Closing Date	Closing Price (\$)	Days Held	% Return on Trade
TNT	7/10/2020	0.255	23/10/2020	0.39	16	53%
AMI	20/10/2020	0.530	26/10/2020	0.535	6	1%
ARR	9/11/2020	0.105	9/12/2020	0.1	30	-5%
PDN	10/11/2020	0.125	11/12/2020	0.215	31	72%
A2M	13/11/2020	14.670	2/12/2020	13.4	19	-9%
OBM	17/11/2020	0.330	24/11/2020	0.289	7	-12%
A3D	18/11/2020	0.080	Still Open	0.073	43	-9%
ASM	18/11/2020	3.770	10/12/2020	4.3	22	14%
EXL	24/11/2020	0.180	Still Open	0.175	37	-3%
FEX	25/11/2020	0.155	Still Open	0.23	36	48%
HVN	26/11/2020	4.800	Still Open	4.69	35	-2%
PXM	11/12/2020	0.165	Still Open	0.17	20	3%
MX1	16/12/2020	0.385	Still Open	0.355	15	-8%
NCZ	18/12/2020	0.255	Still Open	0.24	13	-6%
TLS	22/12/2020	3.000	Still Open	2.98	9	-1%
OBM	30/12/2020	0.305	Still Open	0.305	1	0%
Percentage Return on Capital Invested:						8.34%

Woulda, Coulda, Shoulda

Two of the positions could have led to significantly more profit over the testing period:

- EXL – Was held to the end of the period to a -3% drawdown but was as high as 67% in profit. Instead of taking profits, which was considered, we surmised that it could run further based on news flow and overall market momentum. It is currently ~20% in profit at time of writing.
- ASM – Opposite dynamic to EXL. Decided to take profits when up 14%. Decision was based on peers underperforming and hence, locking in profits when ASM started to pull back at that point. It recommenced its advance 2 days later (the trend held) and was up 64% prior to 31-Dec.

These are examples of the discretionary aspect of the system. Over the long term, as the number of trades taken reaches a statistically significant sample, the effect of such discretion will be inconsequential.

These two alternative actions would have seen the test achieve a 15.03% profit instead of the realised 8.34%. Nonetheless, the realised profit was a great result.

The alternative actions were discussed because they still reflect a system that works, and well. They highlight extent of realisable profit that was achievable over the short term and they were captured as such due to the system having identified the opportunity. Said another way, three out of 16 trades achieved greater than 45% profit in under 36 days, and that could have been as high as five trades. It is looking extremely positive.

Until next time.

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¹ Technically Speaking: Charting 2020 – A Year Of Speculative Mania, <https://realinvestmentadvice.com/technically-speaking-charting-2020-a-year-of-speculative-mania/>