



MORPHIC ETHICAL EQUITIES FUND

Monthly Report

September 2020



Fund Objective

The Morphic Ethical Equities Fund Limited (the Fund) seeks to provide investors a way to grow their wealth and feel confident they do so without investing in businesses that harm the environment, people, and society.

The Fund excludes direct investments in entities involved in environmental destruction, including coal and uranium mining, oil and gas, intensive animal farming and aquaculture, tobacco and alcohol, armaments, gambling and rainforest and old growth logging.

Investment returns*

	1 Month	3 Months	6 Months	1 Year	3 Years (p.a.)	ITD (p.a.)
Morphic Ethical Equities Fund ¹	0.32%	4.67%	10.05%	6.65%	7.13%	6.67%
Index ²	-0.15%	3.87%	10.08%	3.93%	10.40%	10.00%

* Past Performance is not an indication of future performance.

Ethical Investing in Focus

One side effect of the European push for a “green revolution” and [Net zero](#) targets by 2050 is the dawning realisation that to hit those numbers, there will need to be a way to stop businesses “importing” carbon from regions with no tax and bypassing the rules. Hence the need for a “carbon border tax” or what they are calling CBAM (Carbon Border Adjustment Mechanism) which is now rapidly moving forward.

Morphic [wrote about this idea in the AFR](#) some time ago, as it's a direct end conclusion of the fragmentation of consensus on climate change. This all matters to Australia. A lot. As our exports to Europe, will either get captured in the new Free Trade agreement with carbon, or we become part of their Emission trading scheme.

Portfolio review

The Fund rose 0.3% in September, outperforming global markets which fell 0.1% in AUD terms. Global equities fell 3.4% in USD terms, as markets lost some steam after the big gains over the prior 6 months. The fall in the AUD over the month softened losses in absolute terms.

For the second month, Japan was the leading region (+0.3%), with the USA, the strongest market Year to Date, the laggard (-3.9%). Europe (-3.4%) can't seem to catch a break, lagging in both rising and falling markets.

The Tech sector's stellar run came to an end (-6.1%) as the NASDAQ sold off heavily. Though somewhat remarkably it wasn't the worst sector over the month: Energy (-12%) was yet again the laggard. Industrials (+0.9%) performed best.

After underperforming last month, the Fund's conviction in NEC came good as the stock was the leading contributor this month. The new Japanese Prime Minister has promised two initiatives that are good for NEC. Firstly Japan is to prioritise the digitalisation of its government, an area that Japan has surprisingly lagged in. Secondly they are pushing for more 5G and lower mobile prices. Both these benefit NEC (and our other holding Fujitsu).

The Fund's holding in Ciena was the largest detractor over the month. Ciena dropped 30% over the month after reporting earnings, but guiding to a much weaker outlook. This was surprising because as recently as last quarter they had been very upbeat. Good portfolio management minimised the losses – the position had been trimmed into earnings and it was cut on the news. The Fund remains a holder in much reduced size – we need to see evidence this is a one off.

Outlook

We wrote last month about the frothiness in the tech sector and September saw some of this wash out. More importantly, it is now less than one month to the USA elections and markets are increasingly jittery about the outcome. Having been surprised by Brexit the election of Trump, it seems they are determined to not have this happen again:

Net Tangible Assets (NTA)

NTA value before tax ³	\$ 1.1879
NTA value after tax ³	\$ 1.1614

Investment Returns since inception⁴



Past Performance is not an indication of future performance.

Implied volatility is much higher for both the day and the month after, as investors fear Trump disputing the result.

Whilst we have no edge on who wins and how and when it is decided, the bigger debate is whether the impetus for more fiscal stimulus is there. If it's a “blue sweep”, then the answer would be yes. If not, the backdrop may look more like 2010-14: fiscal was a drag.

This matters as it says what sectors do best. The latter is tech and USA heavy, the former is more cyclical and banks and to some extent Asia. The Fund is not averse to owning cyclical exposure, a “Blue sweep” may be time to revisit those stocks.

Top 10 Active Positions

Stocks (Shorts)	Industry	Region	Position Weighting
Fujitsu	Information Technology	Asia Pacific	4.8%
NEC Corp	Information Technology	Asia Pacific	3.6%
Tencent	Information Technology	Asia Pacific	3.4%
Celinux	Telecom	Europe	3.1%
NetEase	Information Technology	Asia Pacific	2.8%
New Oriental Education	Consumer Discretionary	Asia Pacific	2.2%
CHACHA FOOD CO	Consumer Staples	Asia Pacific	2.1%
Assurant Inc	Financials	North America	2.1%
Keysight Technologies	Information Technology	North America	2.1%
Tencent Music	Communications	Asia Pacific	1.9%

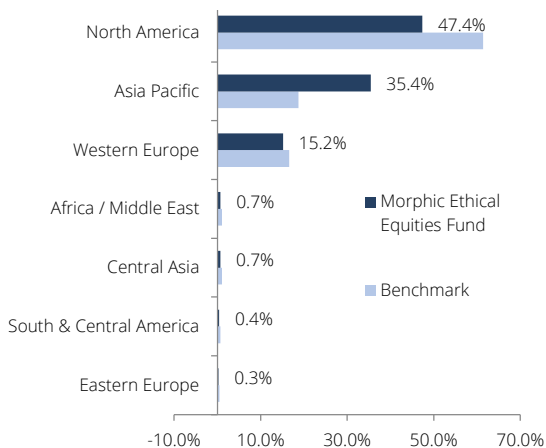
Top three alpha contributors¹⁰ (bps)

NEC Corp	47 bps
Fujitsu Limited	37 bps
New Oriental Education & Technology Group	18 bps

Top three alpha detractors¹⁰ (bps)

CHACHA FOOD CO	-26 bps
NetEase Inc	-27 bps
Ciena Corporation	-38 bps

Equity Exposure Summary By region

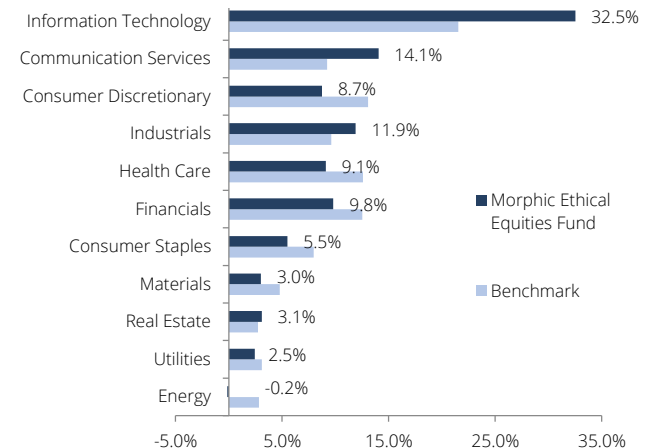


Risk Measures	
Net Exposure ⁵	100%
Gross Exposure ⁶	118%
VAR ⁷	2.80%
Best Month	5.51%
Worst Month	-6.49%
Average Gain in Up Months	2.21%
Average Loss in Down Months	-2.13%
Annual Volatility	9.39%
Index Volatility	10.96%

Hedge Positions	Risk Limit Utilisation (%) ⁹
None	

Key Facts	
ASX code / share price	MEC / 0.985
Listing Date	3 May 2017
Management Fee	1.25%
Performance Fee ¹¹	15%
Market Capitalisation	\$ 52m
Shares Outstanding	52,871,147
Dividend per share ¹²	\$ 0.02

Equity Exposure Summary By sector



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¹ Performance is net of investment management fees, before company admin costs and taxes; ² The Index is the MSCI All Countries World Daily Total Return Net Index (Bloomberg code NDUEACWF) in AUD; ³ The figures are estimated and unaudited; ⁴ Performance is net of investment management fees, before dividends, company admin costs and taxes. Fund listing on the ASX 3 May 2017. Past performance is not an indication of future performance; ⁵ Includes Equities and Commodities - longs and shorts are netted; ⁶ Includes Equities, Commodities and 10 year equivalent Credit and Bonds - longs and shorts are not netted; ⁷ Based on gross returns since Fund's inception; ⁸ As a percentage of the Fund's Value at Risk (VaR) Limit; ⁹ As a percentage of the Fund's Value at Risk (VaR) Limit; ¹⁰ Attribution; relative returns against the Index excluding the effect of hedges; ¹¹ The Performance Fee is payable annually in respect of the Fund's out-performance of the Index. Performance Fees are only payable when the Fund achieves positive absolute performance and is subject to a high water mark; ¹² Annual dividend per share.