ESCALA PARTNERS

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MARCH QUARTER FUND REVIEW

A jolt that reverberates

Equity investors don't typically have to worry about the first rate hike. It is usually the end of the rate hike cycle that matters most. The concern is how late this rate hike cycle has started. Now there is urgency being expressed by central bank officialis in the US, to catch up.

It is this dramatic shift to urgency that is most concerning. Investors don't like to be jolted but that is what they got in the March quarter. Bond yields and rate hike expectations surged as did the cost of borrowing for households and corporates. This dramatic re-calibration will reverberate through economic growth and corporate earnings.

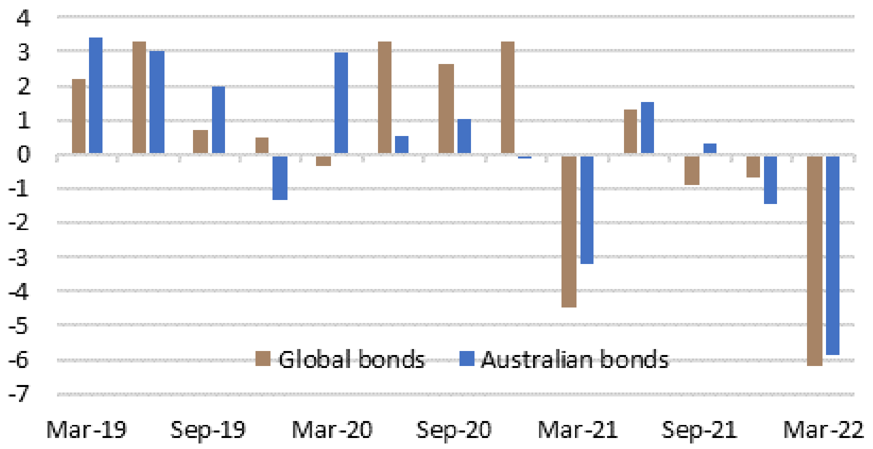
1. A difficult time for bonds

The March quarter was the worst quarter on record for Australian bond investors and the second worst on record for global bond investors. Benchmark returns for Australian bonds came in at -5.9% for the quarter surpassing the worst of the returns seen in at least 32 years. At -6.2%, global bonds gave their worst return since the -7.1% print in the December quarter of 2016.

Bond markets responded to the dramatic pivot in interest rate expectations by the US Federal Reserve over the quarter. As early as September 2021, the US Federal Reserve was expecting no interest rate hikes in 2022. By their March meeting, that expectation had lifted to 7 rate hikes. This was the fastest pivot in policy expectations by the Fed in modern memory.

Investors have been fleeing bonds en masse as the central banks unwind their pandemic-era stimulus, with Treasuries set for the biggest quarterly loss in more than 40 years. Estimated allocation to bonds globally now stands at only 18%, the lowest level since 2008.

Chart 1: Benchmark bond returns (quarterly % change)

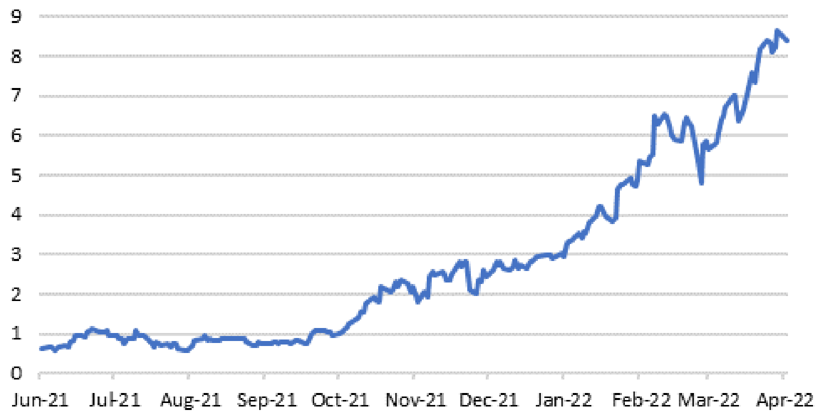


Source: Bloomberg

2. US Fed pivots

Even with a nearly 5% gain in March, the S&P 500 is closing out its worst quarter since March 2020, a stretch that marked the onset of the pandemic in the U.S. Worries about slowing economic growth were compounded by soaring commodity prices, following Russia's invasion of Ukraine on February 24th, and the subsequent implications for monetary policy.

Chart 2: Number of US rate hikes priced in by the bond market



Source: Bloomberg

3. China's zero covid policy

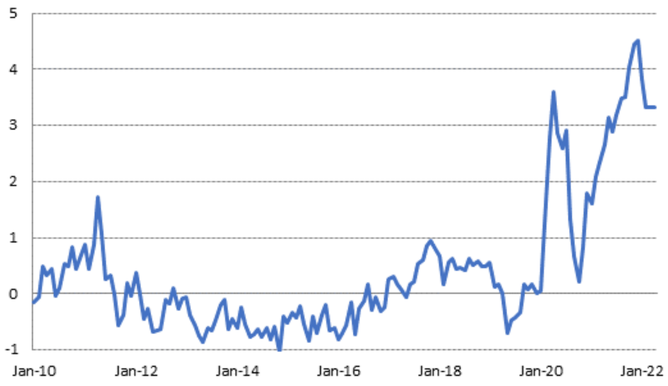
China's continued hard line against Covid outbreaks pose challenges in the March quarter.

Home to six of the 10 largest container ports, China is still the global economy's most important manufacturing hub and an export powerhouse. While most countries have decided to learn to live with Covid, Beijing has maintained a "Covid Zero" policy where even small outbreaks can shut down large population centers and slow economic activity. This is what heppend in Q1 2022.

In Shenzhen, companies including Apple Inc. supplier Hon Hai Precision Industry, better known as Foxconn, had to temporarily shut for a week in March. In Changchun, an industrial hub that accounted for about 11% of China's total annual car output in 2020, automakers such as Toyota Motor Corp. were forced to close. The policy has a dampening effect on China's domestic growth but also disrupts global trade - 80% of which moves on ships – and puts upward pressure on inflation.

Ocean freight rates that are still several times higher than 2019 levels. According to research by the International Monetary Fund, "when freight rates double, inflation picks up by about 0.7 percentage point.

Chart 3: Global supply-chain pressure index



Source: Bloomberg

Australian Shares	3m	1 Yr p.a.	3 Yr p.a.	5 Yr p.a.	10 Yr p.a.
Legg Mason Martin Currie Equity Income	5.10%	13.00%	8.04%	5.75%	9.40%
Legg Mason Martin Currie Equity Income - Ethical	2.49%	13.11%	8.07%		
Bennelong Concentrated Australian Equity Fund	-14.41%	4.87%	14.38%	12.45%	14.80%
Selector Australian Equities	-15.43%	7.97%	10.66%		
Pendal Australian Share SMA	2.58%	13.28%	11.86%	9.99%	
Alphinity Sustainable Share	-1.79%	14.12%	12.87%	12.36%	11.86%
WaveStone Australian Share	1.52%	17.21%	11.40%	10.54%	11.01%
Pendal Focus Australian Share Fund*	1.72%	11.96%	12.29%	10.78%	11.55%
Selector High Conviction Equity A	-14.73%	7.84%	8.75%	13.56%	15.79%
S&P/ASX 200 Accumulation Index	*2.24%*	*14.97%*	*10.59%*	*9.22%*	*10.15%*
Ophir Opportunities Fund	-9.56%	16.77%	20.45%	20.12%	
QVG Opportunities Fund	-8.65%	17.08%	16.40%		
Spheria Australian Smaller Companies	-3.87%	13.18%	13.47%	12.98%	10.14%
Spheria Australian Microcap	-0.48%	36.53%	23.94%	15.91%	
Fairview Equity Partners Emerging Co	-5.97%	12.49%	16.34%	15.39%	10.70%
Flinders Emerging Companies Fund	-5.86%	5.83%	12.75%	12.75%	
S&P/ASX Small Ordinaries Accumulation Index	*-4.21%*	*9.68%*	*9.64%*	*9.90%*	*6.02%*

* Performance as at February 2022

Key points:

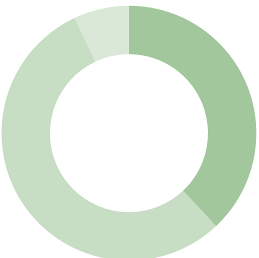
- The Australian equities market rebounded from an early selloff to finish as one of the few global benchmarks to record a positive return in the March quarter, with a total return of 2.2% for the three months. This marked the sixth consecutive quarter of positive performance for the ASX 200 Accumulation Index.
- Equity returns were significantly influenced by two external macroeconomic factors in the first three months of the year. The first of these was a sharp rise in bond yields, as investors anticipated an aggressive monetary policy tightening cycle by central banks in order to combat prevailing high levels of inflation. The second was the conflict in Ukraine, which exacerbated the supply-demand imbalance affecting a range of commodities and led to large gains in commodity prices.
- These two factors led to an unusually wide dispersion in sector returns for the quarter. The sharp rise in interest rates had a detrimental impact on higher-growth companies, particularly those trading on elevated price to earnings ratios within the IT, health care and consumer discretionary sectors. Each of these three sectors experienced declines of 10-14% for the quarter. Meanwhile, the rise in commodity prices led to a solid quarter of gains for resources stocks.
- Fund performance was thus primarily driven by these events. Among large cap managers, those with a focus on higher earnings growth companies and who had typically generated solid outperformance in 2021 saw these gains lost as they were on the wrong side of both factors, with a large exposure to growth companies and an underweight position in cyclical resources. This was most evident in the underperformance of Bennelong and Selector.
- Our other large cap strategies generated returns more broadly in line with the benchmark, reflect a more balanced exposure across the various sectors of the equity market. This group included Pendal and WaveStone.
- Small caps struggled for performance in the March quarter, hurt by the index's higher growth and higher beta nature compared to large caps. Similarly to the

large caps index, small resources (+14%) materially outperformed small industrials (-9%) and so this was a key differentiating factor among fund performance.

- Funds that lagged the benchmark Small Ordinaries were those that typically have little resources exposure, including QVG and Ophir, though the former was helped by a takeover bid in one of its larger positions.
- Underperformance was more limited across other small cap funds, while Spheria's performance was solid, helped by the manager's high valuation discipline and focus on free cash flows.

International Shares	3m	1 Yr p.a.	3 Yr p.a.	5 Yr p.a.	10 Yr p.a.
MFS Concentrated Global Equity Trust (Wholesale)	-10.63%	7.40%	11.47%	12.52%	15.79%
MFS Global Equity Trust	-9.93%	6.58%	10.14%	11.37%	14.42%
WCM Quality Global Growth	-18.88%	0.71%	15.06%	17.70%	17.46%
Franklin Concen Glb Eq ex-Aus Model (SMA)*	-16.15%	-1.63%	18.95%	20.55%	
WCM International Small Cap Gr	-21.99%	-6.29%			
Impax Sustainable Leaders Fund A	-16.90%	0.73%	10.96%		
Pengana WHEB Sustainable Impact	-16.79%	-2.20%	8.78%	7.33%	5.95%
Stewart Investors Worldwide Sus-Class A	-15.84%	2.40%	8.96%	10.36%	
Franklin Global Growth I	-16.21%	0.42%	15.13%	15.84%	16.03%
Artisan Global Discovery	-16.29%	1.69%			
Loftus Peak Global Disruption	-14.54%	1.78%	18.37%	19.53%	15.73%
Munro Climate Change Leaders	-13.79%				
MSCI AC World ex Aus ($A)	*-8.59%*	*8.68%*	*11.69%*	*12.07%*	*13.68%*
MFS Fully Hedged Global Equity Trust	-6.08%	7.47%	11.00%	10.43%	12.78%
ClearBridge RARE Infrastructure Value - Unhedged	0.18%	18.21%	8.57%	9.02%	11.32%
ClearBridge RARE Infrastructure Value Fund - Hedged	3.92%	18.81%	9.60%	8.18%	10.02%
ClearBridge RARE Infrastructure Income – Hedged	5.70%	22.51%	13.64%		
ClearBridge RARE Infrastructure Income - Unhedged	3.06%				
MSCI AC World ex Aus	*-5.59%*	*7.15%*	*13.78%*	*11.71%*	*10.08%*
CC Redwheel Global Emerging Markets Fund	-13.27%	-15.67%	5.35%		
Fidelity Asia	-14.87%	-11.46%	7.93%	12.24%	13.86%
MSCI Asia-Pac Ex Japan ($A)	*-6.71%*	*-13.03%*	*5.35%*	*7.09%*	*6.54%*
Quay Global Real Estate Fund (Unhedged)	-7.52%	19.63%	7.71%	10.86%	
FTSE EPRA Nareit Developed Index ($A)	*-6.83%*	*17.02%*	*4.44%*	*7.83%*	*11.36%*

* Performance as at February 2022

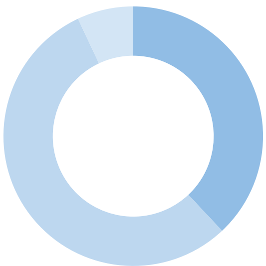


Key points:

- Global equities were down 5.5% in the March quarter 2022 after recording a rise of 7.5% in the December quarter.
- For the fifth consecutive quarter, emerging markets underperformed developed markets with the former falling by 7.3%. Once again, China came under some heavy selling pressure finishing the quarter down 8.6%. South Korean equities fell by 7.4%. At the other extreme, Brazil rose by 14.5% helped by higher commodity prices. European equity markets were 7-9% lower, weighed down by the war in Ukraine, while the Japanese Nikkei index finished 3.4% lower.
- The US S&P500 fell 4.9% overall but the dispersion was wide with tech and consumer discretionary sectors down around 9% while energy was up 38%. The tech-heavy NASDAQ finished 9% lower.
- The Australian dollar rose by 3% over the quarter against the US dollar. This means the hedged versions of our international equity funds did better than the unhedged versions.
- The best performing funds over the quarter were the infrastructure funds (ClearBridge RARE), the less growth-oriented funds such as MFS and the global real estate fund Quay.
- WCM Quality Global Growth lost 15.3% over the quarter with the majority of being lost in the month of January. Among the top underperforming companies over the quarter was Sherwin-Williams, First Republic Bank and Old Dominion Freight Line.

- Franklin Global Growth lost 16.2% over the quarter. Among the top underperforming holdings over the quarter were SVB Financial Group, Intuitive Surgical, and Partners Group Holdings.
- Emerging markets funds were challenged over the quarter by the underperformance of Chinese equities which declined by 8.6%.
- The WCM International Small Cap fund struggled over the quarter given its 51% allocation to Europe which was particularly impacted by the war in Ukraine.

Fixed Income	3m	1 Yr p.a.	3 Yr p.a.	5 Yr p.a.	10 Yr p.a.
Legg Mason Western Asset Aus Bd A	-6.24%	-5.86%	-0.24%	1.94%	3.82%
Realm High Income - Wholesale	-0.71%	1.71%	3.83%	3.54%	
Realm Short Term Income Ordinary	-0.09%	1.12%	2.19%		
Perpetual Credit Income	-0.55%	0.66%	2.72%	3.08%	4.19%
Alexander Credit Income Fund	0.49%	3.39%	3.22%		
Bloomberg AusBond Bank Bill Index	*0.01%*	*0.04%*	*0.46%*	*1.02%*	*1.83%*
Bloomberg AusBond Composite Index	*-5.88%*	*-5.55%*	*-0.32%*	*1.86%*	*3.44%*
Bentham Global Income Fund	1.61%	2.89%	4.59%	4.33%	6.38%
PIMCO Global Bond Fund – Wholesale Class	-4.65%	-4.12%	1.45%	2.35%	4.53%
PIMCO ESG Global Bond Fund - Wholesale	-4.61%	-4.15%	1.39%	2.02%	
PIMCO Global Credit W	-5.65%	-4.30%	1.11%	2.05%	4.05%
Perpetual Ethical SRI Credit	-0.87%	0.28%	2.16%		
Robeco SDG Credit Income (AUD Hdg) A	-0.76%	-1.98%	3.19%	3.78%	
Barclays Global Aggregate $A (Hdg)	*-5.15%*	*-4.14%*			

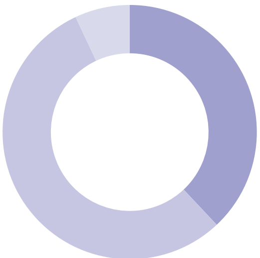


Key points:

- Government bond yields were higher over the quarter leaving the high duration funds such as Western Asset Management Australian Bind Fund and PIMCO Global Bond Fund underperforming.
- Credit spreads also widened over the quarter which left funds with a higher credit spread duration, such as the PIMCO Global Credit Fund, underperforming.
- The best performing funds over the quarter were those that invest in shorter duration bonds, such as the Realm Short-Term and High Income Funds and the Alexander Credit Income Fund.
- Within our credit funds, the best performing were those that remove or hedge out credit duration risk. This was the case with the Bentham Global Income Fund and the Perpetual Credit Income Fund.

Alternatives	3m	1 Yr p.a.	3 Yr p.a.	5 Yr p.a.	10 Yr p.a.
Partners Group Global Value Fund*	-0.74%	19.58%	14.62%	13.26%	
Munro Global Growth Fund	-12.17%	-2.86%	13.31%	13.72%	
Hamilton Lane Global Private Asst (AUD)*	-1.10%	18.50%			
Hamilton Lane Global Private Asst (Unhedged)*	-1.82%				
Aquasia Enhanced Credit Fund*	0.86%	4.24%	4.60%	5.10%	6.56%
Charter Hall Direct Office Fund	1.78%	15.98%	12.17%	13.33%	
Barwon Healthcare Property Fund	2.52%	20.70%	12.69%	10.56%	
Merricks Capital Agriculture Credit Fund	1.78%				
Merricks Capital Agriculture Credit Fund - Founders Class	1.88%				
Merricks Capital Partners	1.98%	8.13%	9.06%	10.55%	
Realm Strategic Income Enduring*	1.31%	5.74%			
Alium Alpha Ordinary*	-1.69%	12.79%	15.95%	19.45%	
Spire Oaktree Opps XI (AUD) Frst Cls*	-0.66%	11.60%			

* Performance as at February 2022



Key points:

- The first quarter proved to be volatile for global financial markets. A growth equity correction escalated through February with the Russian Invasion of Ukraine and concluded in March with a bond market sell off on the back of an increasingly hawkish Federal reserve. This combination of factors impacted hedge fund performance over the quarter.
- Equity long short manager Munro Global Growth finished the quarter -12% against the backdrop of highly volatile equity markets. The bulk of the losses occurred in the first two weeks of the year in the long book following the sell-off in equity markets. The fund quickly followed its stop loss disciplines and reduced exposure to equity markets, ultimately lowering volatility through the February / March period only to see those hedging gains given back as markets rallied to close the quarter.
- Following a record year for private equity (PE) activity in 2021, Q1 2022 was slightly more subdued in terms of private equity activity. Rising inflation, geopolitical tensions and public market volatility all caused PE dealmakers to pause for several weeks which has meant total deal count and value will likely be lower over the first half of the year. Public listings of PE sponsored companies will slow from the record in 2021 and strategic sales will become a bigger focus for PE managers.
- Our PE managers finished the three month period ending Feb-22 lower with Partners Group Global Value Fund down 0.7% while Hamilton Lane Global Private Assets Fund was down 1.1% compared to global listed equity markets falling 5.9% over the same period. Multiple contraction was the main driver of the softer performance over the quarter however this was offset by strong financial returns for underlying portfolio companies in both funds, specifically across healthcare and technology direct equity positions.
- In the private debt space Merricks Partners Fund added 2% over the three months ending March 2022. Underlying loan portfolio income was up for the month due to new investments settled in February and two existing loan extensions. The portfolio currently comprises senior secured loans diversified across fourteen sub-sectors and is additionally diversified by geographic spread and borrowers. The investment outlook for deploying private credit across asset-backed opportunities in Australia and New Zealand remains positive.

- In direct property markets Barwon Healthcare Property Fund added 2.5% over the quarter. The indicative yield on the portfolio is currently 5.5%. The healthcare property industry continues to benefit from strong demand for essential service properties in prime locations across the country with high occupancy rates and quality tenant profile. With government entities and ASX listed companies the largest tenants across the portfolio and 98% occupancy the Barwon Healthcare Property Fund is well positioned to benefit from this trend

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