

Insync’s short-term performance continued to be negatively impacted by the derating of growth businesses resulting from an increase in the real (inflation adjusted) long bond yield. However, we remain unchanged in both our approach and the type of businesses we invest in - for very good reasons. As we will demonstrate, this adjustment in both the absolute and relative price earnings multiple for growth businesses is largely complete. Companies benefiting from the secular forces of Megatrends tend to deliver **earnings growth during periods of subdued economic activity**.

Markets, will in turn, readjust their pricing of those impacted stocks accordingly. In our minds, this swing backwards in the first half represented the same but opposing force of the unjustifiable prices that many tech/disruption stocks enjoyed until then. Neither position is worthy of serious, risk aware and longer-term investment. It’s why we invest in companies that can *sustainably* deliver strong above average *Earnings Growth*. Their stock prices invariably follow their earnings growth (a short lived event-based calamity can only temporarily place them off track).

Insync is an investor in quality businesses, which have been recently sold down indiscriminately, along with stocks that were perhaps deserving of their negative re-ratings. This ‘lumping all together’ of stocks occurs when markets first swing heavily. Sense will prevail. Right now the lack of it presents a rare buying opportunity.

	1 Month	3 Months	6 Months	1 Year	2 Years	3 Years	5 Years	10 Years	Since Incep#
Insync Global Quality Equity Portfolio ^	-3.19%	-11.99%	-27.21%	-19.35%	0.74%	5.12%	9.67%	12.98%	11.36%
Insync Global Capital Aware Fund*	-2.69%	-11.53%	-27.39%	-20.16%	-1.37%	5.10%	9.44%	10.42%	9.60%
MSCI ACWI (ex AUS) NTR (AUD)~	-4.40%	-7.84%	-15.76%	-8.08%	8.35%	7.00%	9.42%	13.29%	10.32%
Global Quality Active Out-Performance	1.21%	-4.15%	-11.45%	-11.26%	-7.60%	-1.88%	0.25%	-0.31%	1.04%
Global Capital Aware Active Out-Performance	1.71%	-3.69%	-11.63%	-12.08%	-9.72%	-1.91%	0.02%	-2.87%	-0.71%

Source: Insync Funds Management - Past Performance is not a reliable indicator of future performance. *Represents net of fees and costs performance, assumes all distributions reinvested. ^Returns prior to July 2018 represent the underlying Insync Global portfolio (including cash) inclusive of a 0.98% p.a. MER. ~ MSCI All Country World ex-Australia Net Total Return Index in Australian Dollars. # Inception date 9/10/2009

A Different Message For The Year’s Mid-Point

Each month we show how we invest practically by focusing on a Megatrend, then one or two stock examples in support. Given we are halfway through the year and with so much negativity about after the last 5 months of stock price volatility, we thought a closer look at these negatives is warranted.

We will assume you are already well versed with ‘the sky is falling in’ commentary and opinion from elsewhere. All good decisions however come from looking at both sides.

A very important reminder: Embedded genetically into us all are biases that helped us a species thrive but can also work against us with things such as investing. No one in this industry is exempt either; no matter their experience or achievements. Investors ignore these biases at their own peril.

Negativity Bias: We notice the *bad* far more than the good. It’s why commentators lead with bad news. It gets our attention.

Cognitive Bias: We’re more aware of, and seek out, information *supporting* our view or assessment, even if we can’t point to why we have that view. As an extension, we often then block or discount information to the contrary.

Time bias: The immediate and near term has a greater weighting in how we respond than further out; even if it is counterproductive to achieving what we are seeking.

Straight Line Bias: We assume most lines and trends will continue as they are now, unabated. For example, today’s inflation rate combined with negative headlines is interpreted as inflation will keep increasing.

Fear Bias: We tend to emphasise and process negative information *ahead* of positive information. So much so that positive news is often received with cynicism or suspicion. Fear beats positivity every time.

Inflation, recession, high interest rates.....

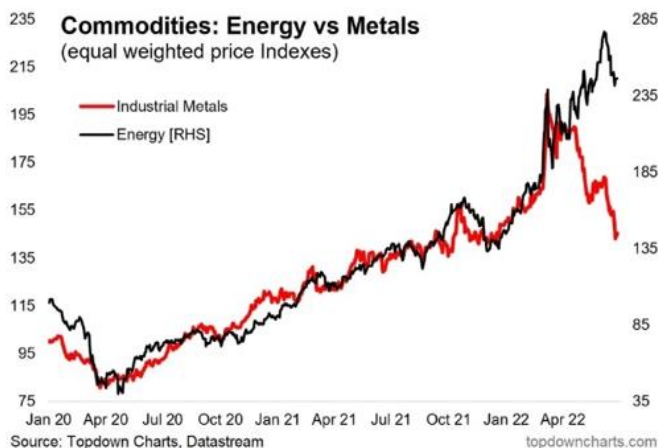
Commentators have espoused many things in the last 5 months, the general message swinging between ongoing crippling inflation, high interest rates, and recession. We have noticed **5 common assertions** they often use, and for our investors benefit we felt it worthwhile examining each one carefully. What we discovered may surprise you, and so remember those 5 genetic biases.

The inference is that investing in growth assets will be a risky decision and thus growth managers will face hard times. As a Quality Style manager, we are not convinced of these inferences as what we found suggests otherwise. The details behind our reasoning can be found in our recent **White Paper** on this subject on our website.

Common Assertion 1: Carbon prices will continue to rise.

- **Supplies globally can easily meet demand** (the potential temporary exception of gas to Europe accepted). OPEC sees oil and gas price pressures as ‘transient’, and not worth the expense or risk of lifting output creating oversupply.
- **Net Carbon Demand** continues to drop as **Oil Intensity** in our economies also falls (has been for the last 15 years).
- **The Russian war will end**, with bad news outcomes mostly factored into its price already.
- **Longer term**, carbon demand growth overall will be offset by green energy, emerging energy storage solutions and shrinking populations in developed nations.
- **Scant evidence supports a sustained price rise** above the present US \$100-\$120/ barrel trading range, especially as the US reopens shale extraction.

Given this, prices are not likely to either significantly increase or decrease. As carbon energy is the PRIMARY driver of key inflationary factors, should it trade around where it is now, it will fail to drive inflation further.



The red line in the graph shows the general basket of major commodities. They too are falling and earlier than carbon energy has. Indeed, this might not only point to a fall in inflation but to the prospects of a recession. We will address that further on.

Common Assertion 2: Global shipping supply chains are crippled and expensive.

The problem with this is that shipping capacity and efficiency is rapidly improving and prices are falling. These facts and more below.

- **Next 2 years the equivalent of an additional 25% of all TEUs** (6 Mn+ 20ft containers) shipping capacity in the world today will enter the water.
- **Those ships are bigger** and more efficient. They consume less fuel per TEU, with a very large proportion of new ships over a whopping 14,000 TEUs in size. (the largest carries 21,000 containers)
- **Bottle necks are evaporating** as a vaccine driven Covid BAU takes hold.
- **Container costs have averaged under \$2k/TEU** for over a decade - Covid increased this temporarily to \$10k/TEU at its peak last October.
- **It's now already falling** DESPITE high fuel costs.

Covid is an event based disruption- not permanent. Life resumes, blockages unblock. This is already occurring.



Common assertion 3: Reshoring back to the West means higher prices

A UBS survey of American CEOs had 90%+ intending to move production away from China. Already 6 massive multibillion dollar chip manufacturing plants are already underway in Texas and Arizona. It comes down to what's being re-shored. Goods being re-shored are mainly higher value/complex goods (e.g. technology intensive). Let's look at some further current facts:

- **Multiple US tariff wars, Covid, Taiwan, Hong Kong, and now Russia** – CEOs are adjusting their risk/reward calculations en masse. (There’s been exponential increases in both the number of corporations both acting and planning moves).
- **Re-shored goods by in large face lower transportation costs** and delays, and less logistical complexity.
- **Higher technology inputs utilising higher skilled labour** means wage price differentials are less than previously assumed in financial models.
- **White goods are already being made in the US** at prices as if they were made in China (Ironically in one example Haier from China is the plant owner)
- **Automation of new plants** is reducing manufacturing-based wage pressures.
- **No one is yet certain how much will return** to major consumption centres (beyond strategic goods such as chip manufacturing and rare-earth mining) but indications are clear that it’s a significant amount.

There are emerging spin-off benefits not previously factored in that offset nearshoring or reshoring costs; for example massive construction activity for rehousing all this manufacturing, along with the support industries providing the new equipment for them. US facility construction soared 116% in the last year, dwarfing the 10% gain on all other construction combined.

This move may will assist western economies increase resilience to geo-political events of the future too (meaning more stable prices and supply),

Common assertion 4: The US economy is faltering, and now from the Russian war, the EU is too.

There are several arguments entwined in this, and so we shall try to be brief, knowing we have a fuller answer contained in our White Paper found on our website.



That **red circle** in the graph shows a **critical historical disparity**. The market has overshot the negative and is out of kilter with the 300 odd critical US businesses purchasing managers that this reliable benchmark survey covers. Investors are already expecting the US economy to contract, yet importantly *not to the extent* that it did during the pandemic, the GFC or the 2000 recession.

Despite all the news headlines, US hourly wage growth is exceeding the inflation of goods and services (ex food and energy). Real wages are growing at (a moderate) 1.7% pace, maintaining a healthy demand for labour and not too much of a concern for the Federal Reserve. Given the low labour participation rate, there is little chance that we see wages driving inflation. This is what would concern the Federal Reserve, as unit labour cost growth is the real source of endemic inflation.

Low participation = underutilised employment market. Positive real wage growth, robust consumer balance sheets and solid corporate balance sheets (as measured by interest cover/debt payback) are **running contrary to a deep protracted recession.**

Until the Russian war ends the EU is in for a bumpy ride-short term no doubt, but there will be positive surprises as is already evident.

Common assertion 5: Ever increasing interest rates.

Bond markets basically set the future of interest rates and particularly in the US. So, let’s take a closer look at what they are telling us. Their expectations after allowing for inflation, energy and commodities prices, geopolitics etc. says the next 5 years will top at 2.55% and the 5yr-10yr expectation at 2.14%.

Let’s say that again... 2.55% and 2.14%.

From this we can gauge the expectations for 10 years which currently stands at 2.35%.

Clearly interest rate rise expectations, are **actually rapidly declining**. This has implications for how much more the Federal Reserve is likely to tighten. Whilst there is sound basis to argue that the Fed Fund Rate is too low, it is unlikely to be lifted more than 3.5% due to the combined effect of **slowing GDP growth** and **peaking shorter term inflationary** expectations. Long term inflation averages a little over 3%, yet in the last 10 or so years, we got used to a once in a lifetime decade of ultra-low rates. Life, markets, consumers and companies adjust. This level of inflation is not bad for growth assets.

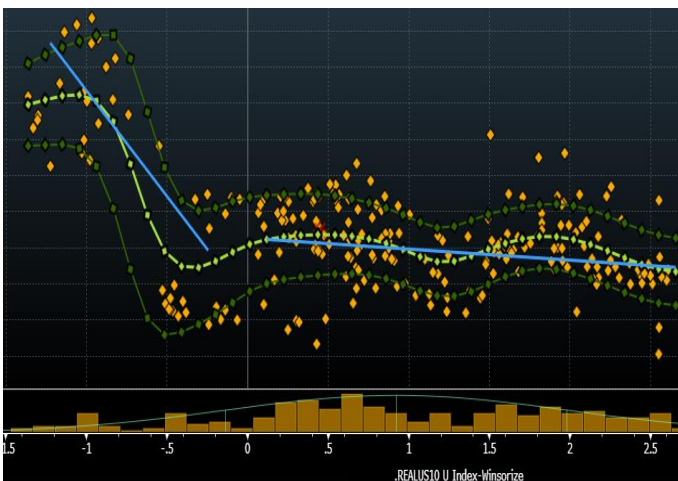
There is further supporting analysis for our look on future interest rates in our White Paper. It's possible there is another 100-120 bps is about all there is to go for short term rates.

Isn't debt servicing going to be a real problem now for consumers, however?

Given corporate balance sheets are in far better shape than in previous times such as the GFC, all eyes are on consumers. The **orange line** in the graph below tracks debt servicing cost as a percentage of household disposable income for the US consumer. Sitting currently at circa 10%, this is *significantly* below the 12% threshold that typically portends a consumer crisis. **Historically, the economy and thus the S&P500 (blue line) only undergo significant declines when this condition is met.**



Interest rates impact Price Earnings Ratios: Let's not forget that most beloved equity price indicator. Often, it's overused in determining fair prices in growth assets. Impacted heavily by interest rates, the downward quantum shift in Equity PE ratios, in response to a higher real 10-year bond yield, is now complete as can be observed below.



Last of all: Beware of the Base Effect.

Keep this in mind when interpreting inflation moves. This describes the danger of a percentage point headline result distorting the reality of a situation. In this case, the inflation number has risen steeply from its unsustainably low past. When an arithmetic value has sat at a low figure, even a small rise distorts the inferred interpretation. Additionally, once a high rate has resulted, after say six months (like where we are today), then to keep sustaining a high inflation rate percentage number, further increases now requires a larger driving impact than the previous time. We can see from the 5 counterpoints that there is little support for this to continue at such high rates.

In conclusion:

- No real basis for increasing inflation at high rates (3% p.a. is a longer term normal).
- Interest rates may rise a bit more but nothing overly dramatic.
- World logistics are normalising fast.
- Reshoring doesn't always mean higher prices.
- Carbon prices are likely to trade in a range of where they are today for another year or so, meaning little inflationary impact.
- Unemployment and household capacity is ok
- As is real wages versus other key factors

In short, perhaps a small technical recession but little chance of large inflation lifts, or big interest rate rises. Nothing in the future is guaranteed but we do ask you think about these facts, the biases waiting to deceive you and come to a balanced decision. **We leave you with one last thought for the rest of 2022 below. What follows the worst first-half years on record? Take a look.**

Year	2nd Half % Change
1970	26.51
1962	15.25
1940	6.01
1939	15.01
1932	55.53
Average	23.66
Median	15.25
% Positive	100.0%

S&P 500 second-half performance after a first-half fall of 15% or more DOW JONES MARKET DATA

The S&P 500 did rise in each of those instances, with an average rise of 23.66% and a median rise of 15.25%.

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Risk Measures – Global Quality Equity Portfolio^

	1 Year	3 Years	5 Years
Standard Deviation	17.50%	16.20%	14.64%
Tracking Error	9.06%	8.95%	7.71%
Information Ratio	-1.24	-0.21	0.11
Sharpe Ratio	-1.11	0.30	0.65
Batting Average	33.33%	50.00%	55.00%

Risk Measures – Global Capital Aware Fund*

	1 Year	3 Years	5 Years
Standard Deviation	17.25%	15.46%	13.83%
Tracking Error	9.10%	9.81%	8.40%
Information Ratio	-1.32	-0.19	0.00
Sharpe Ratio	-1.17	0.31	0.63
Batting Average	33.33%	50.00%	48.33%

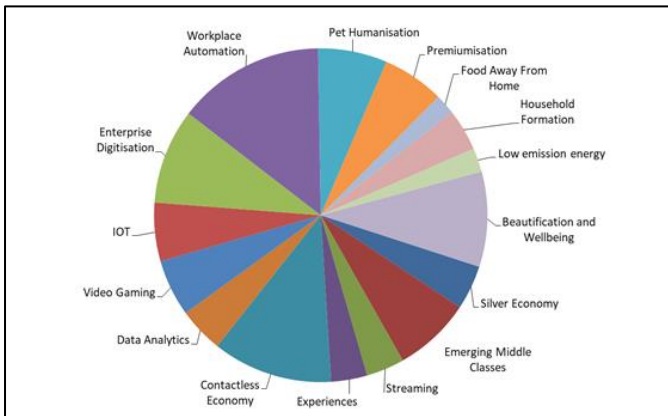
Capture Ratios – Global Quality Equity Portfolio^

	3 Years	Since Incep#
# Index Positive Months	21	95
# Index Negative Months	15	58
Up Market Capture	1.20	0.98
Down Market Capture	1.45	0.84
Capture Ratio	0.83	1.18

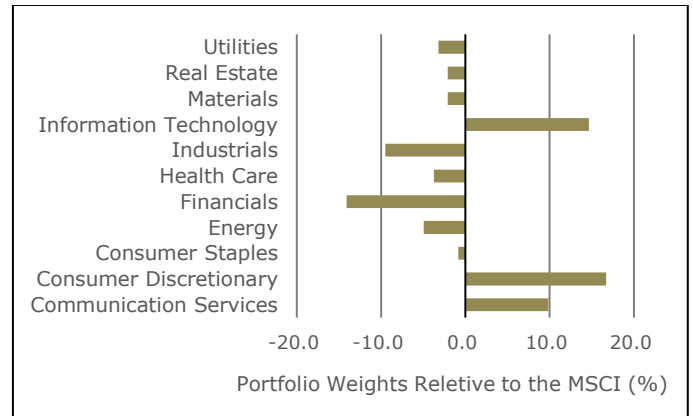
Capture Ratios– Global Capital Aware Fund*

	3 Years	Since Incep#
# Index Positive Months	21	95
# Index Negative Months	15	58
Up Market Capture	1.10	0.85
Down Market Capture	1.31	0.77
Capture Ratio	0.85	1.11

Megatrend Exposures



Portfolio Sector Weights vs MSCI



Top 10 Active Holdings

Stock	%
Qualcomm	3.7%
Visa	3.5%
Nintendo	3.5%
Rightmove	3.4%
LVMH	3.3%
Domino's Pizza	3.2%
KLA Corp.	3.1%
JD Sports Fashion	3.1%
Accenture	3.0%
Alphabet INC-CL C	2.9%

Key Portfolio Analytics

	Portfolio	Index
Forward PE	18.62	13.98
ROIC	55.93	15.17
Market Cap (USD Bln avg)	387.44	41.25
Market Cap (USD Bln median)	114.47	16.11
Std deviation (ex ante)	18.67	15.50
Interest Cover	186.11	66.98
Total Debt to Ebitda	1.37	3.08

Key Fund Information

	Insync Global Quality Fund^	Insync Global Capital Aware Fund*
Portfolio Managers	Monik Kotecha and John Lobb	
Inception Date	1 July 2018	7 October 2009
Management Fee	0.98%p.a. of the NAV	1.3%p.a. of the NAV
Performance Fee	Nil	Nil
Buy/Sell Spread	0.20% / 0.20%	0.20% / 0.20%
Distribution Frequency	Annually	Annually
APIR Code	ETL5510AU	SLT0041AU
Trustee	Equity Trustees Limited	

Disclaimer

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