

# CHIEF INVESTMENT OFFICER LETTER

QUARTERLY LETTER DECEMBER 2020

www.foragerfunds.com

## FORAGER FUNDS PERFORMANCE SUMMARY (as at 31 December 2020)

	1 month return	3 month return	6 month return	1 year return	3 year return (p.a.)	5 year return (p.a.)	10 year return (p.a.)	Since inception* (p.a.)
<b>Forager Australian Shares Fund</b>	3.56%	26.39%	58.82%	21.63%	0.42%	7.99%	12.04%	11.01%
<b>Forager International Shares Fund</b>	5.98%	20.24%	36.30%	38.26%	16.23%	15.95%	-	16.28%

Past performance is not indicative of future performance and the value of your investments can rise or fall. Performance in FASF is calculated using Net Asset Value (NAV), not the market price.

\*8 February 2013 for FISF and 30 October 2009 for FASF

Extraordinary. It is an overused word. It's also an odd word, to me at least. Why does something that is unusual or infrequent have an extra amount of ordinary?

Anyway, we can safely use it to describe 2020 without being accused of hyperbole. Travel plans, living arrangements, schooling, workplaces and shopping have all been thrown into turmoil by a virus that has spread around the world, caused governments to lock citizens in their homes and killed almost two million people. For those of us in financial markets, the March crash will sit alongside the 2008 Lehman-induced meltdown as a placemark in our careers.

At Forager, it was an especially extraordinary year. The Forager International Shares Fund returned positive 38.3% for the year. In absolute terms, that is an outlier. Relative to the MSCI AC World Net Index in \$A, which returned 5.8%, it is the sort of result you hope for once every couple of decades.

The Forager Australian Shares Fund's 21.6% return is less of an outlier — you could argue it was overdue given the underperformance of the prior two years — but it was extraordinary nonetheless. That 21.6% encompasses a fall of 54% between 1 January and 23 March, followed by a 166% rise between that nadir and 31 December.

You should expect us to perform well in volatile markets. But the magnitude of the performance is particularly pleasing. My thanks go out to the entire Forager team for their outstanding work in a difficult year and our loyal Forager clients, who allow us to do our jobs in dysfunctional markets.

## THE GAME THAT NEVER STOPS

One thing I like about marathon running is the well defined end-point. You train hard for a few months, eat well, dial it back for a week and then it's race day. Once the finish line is behind you, it's time for a cold beverage, a few weeks of rest and all the pies you can eat.

Running an investment portfolio in a year like 2020 is nothing like running a marathon. There is no finish line. Like a two year old child, it needs to be fed and monitored every single day. And the better your returns, the faster markets are moving, the more monitoring and feeding it needs.

If 2020 proved anything, it was that predicting the future is extremely difficult, if not futile. Look no further than my February blog [Corona no virus for global stocks](#), two weeks before a market meltdown. That also shows that prognostications are not a prerequisite for above average returns.

We didn't predict the market bottom in 2020. We didn't anticipate the fastest bear market recovery on record. We simply tried to construct the best portfolios we could with the opportunities that were in front of us. We recognised that the best opportunities on the 23rd of March were very different from those on the first of January, and made quite dramatic changes to both portfolios.

In fact, writing a blog that looked foolish in hindsight was probably a blessing in disguise. It served as a timely reminder that great investment returns come from finding great investment opportunities. While many of those who predicted a market meltdown were wasting their time trying to identify the bottom, we were out there looking for stocks to buy.

We will take the same approach in 2021. Start with the view that anything could happen, and we won't be surprised.

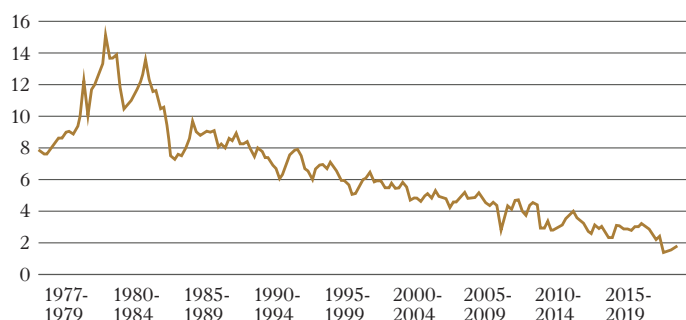
### A MONETARY EPOCH?

One thing that could happen, that most people think won't, is that we look back on 2020 as more than just a market crash. It may be seen as the end of an era.

Will inflation return? That was the question on the cover of the December 12 edition of *The Economist*. The answer will define the next decade, perhaps two, of returns on almost every asset class.

In September 1981, the 30-year US government bond was yielding 15% for an investor who held it to maturity. In the early 1990s, my parents were still paying interest rates of 18% on their mortgage. Today's yield on a 30-year US bond is less than 2% and a mortgage loan in Australia can cost you less than that.

### 30-YEAR US GOVERNMENT BOND YIELD



Source: Bloomberg

For the past three decades, interest rates have inexorably fallen alongside inflation expectations. Today, central bankers are far more concerned about inflation never coming back than it ever getting out of control again. Investors are using low long-term interest rates, based on a lack of inflation concerns, to justify sky-high prices for property, infrastructure assets and Tesla shares.

There are theories, from ageing populations to technological improvements and low cost labour substitution, that explain low inflation or even deflation as a permanent feature of the developed world. I don't have a strong view that those theories are wrong. But I know that when the whole market thinks something can't possibly happen, the consequences of that assumption being wrong are significant.

### WHY MIGHT INFLATION RETURN?

Some investors and economists — particularly of the pessimistic kind — have been predicting the return of inflation ever since the financial crisis of 2008/9. It hasn't happened, the argument goes, and therefore it won't.

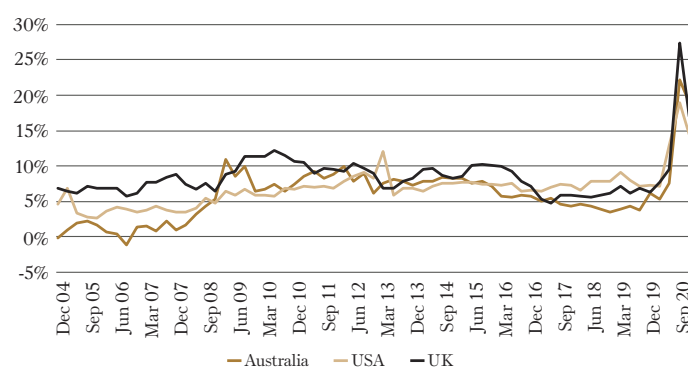
Throughout the past decade, monetary policy was extremely accommodative. But it didn't have much help. The private sector — including consumers and banks — spent most of the decade in balance sheet repair mode. Fiscal policy wasn't helping, as politicians caved to austerity demands every time their economies looked like recovering. Just like the recovery from the Great Depression of the early 1930s, the recovery has been mired in fits and starts.

This pandemic-induced crisis might be more akin to a war than a financial crisis, though. By the end of 2021, all three components will be surging in the same direction. Morgan Stanley estimates the four largest economies will expand central bank balance sheets by some 38% of GDP in 2020, almost four times the amount of purchases following the financial crisis.

And the same G4 economies will be running the largest fiscal deficits since the second world war at the same time. The US government deficit is expected to be 14.9% of GDP in 2020 and remain at 9% of GDP in 2021. Despite all of the bailouts in 2009, the US government deficit never exceeded 10% of GDP.

Perhaps most surprisingly, consumers around the world are in rude health. Unemployment has not risen as much as expected, and the large stimulus programs and a lack of things to spend their money on means consumers are flush with cash (see chart below). The lockdowns have hit a small percentage of the population hard but, as a whole, the savings rate in Australia soared to more than 20% of disposable income, a level unprecedented in RBA records.

### HOUSEHOLD SAVINGS RATES



Source: RBA, ABS, Office for National Statistics, U.S. Bureau of Economic Analysis

The aggregate picture is one of substantial pent up demand meeting more monetary and fiscal stimulus in late 2021 and into the following years. Perhaps we look back on this period as the monetary equivalent of the Second World War, one giant stimulus program that finally brought the economy to life.

Nonagenarian investor Charlie Munger once said "knowing what you don't know is more useful than being brilliant." Some of the brightest economics minds in the world have a patchy track record when it comes to macroeconomic forecasts. Perhaps demographics and technology do mean we never see inflation again. But the world is about to test the theory. And we won't be buying anything that assumes higher interest rates can't possibly happen.

Kind regards,



**Steven Johnson**  
Chief Investment Officer