Portfolio performance

The Swell Global Portfolio declined by 4.0% in the first half of FY23 (1H23). Technology was at the epicentre of the market sell off last year as soaring inflation and rising interest rates led to declines in long duration assets.

Consumers globally are under pressure as rising inflation has impacted cost of living. Inflation expectations however remain well anchored which suggests consumers expect inflation to continue to come down in the future.

And as pandemic restrictions lifted, consumers shifted their spending away from goods to services like travel and eating out, making forecasting consumer demand patterns very challenging. Consumer sentiment and business confidence have also been volatile, placing further strains on stretched supply chains.

Central banks globally are wrestling with inflation as they know failing to do so can be incredibly damaging for an economy. If left unchecked, high inflation can erode purchasing power, widen income inequality, harm the banking system and reduce international competitiveness. The good news is, inflation is moderating, and we expect this to continue in 2023.

The US economy continues to defy experts fears by maintaining jobs growth, culminating in a staggering 517,000 new jobs in January 2023, smashing estimates of 187,000. The last time unemployment reached 3.4% in the US, Marvin Gaye topped the charts with his smash hit “I heard it through the grapevine” in May 1969.

Market conditions

Three primary factors influenced markets in 2022:

- war in Ukraine
- rising inflation
- China’s zero COVID policy

War in Ukraine and the impact on soft commodities and oil

After the war began, Ursula von der Leyen, president of the European Commission, announced "massive" EU sanctions. The sanctions targeted technology transfers, Russian banks and Russian assets, and although they contributed to the collapse of the Russian Ruble, they also inflicted economic damage on the EU economy.

The war also made it challenging for Ukraine to export its commodities. It accounts for 10% of the world wheat market, 15% of the corn market and 13% of the barley market. The lack of Ukrainian produce had the effect of driving up soft commodity prices, adding to the inflation story.

Inflation approaches levels not seen since the 1980s

Grappling with higher inflation, central banks shifted from accommodative to restrictive monetary policy, fearing the effects of high inflation and rising interest rates.

The US Fed continues to take a data driven approach and will be responsive to changes in economic growth. However it is clear the FOMC is prioritising price stability over maximum employment and they are right to do this, it’s the lesser of the two evils.

China reopens after COVID-19

China, the world's second largest economy, has experienced rapid economic growth over the last few decades and is a major hub for global manufacturing. China’s low-cost labour force, favourable government policies, and supportive infrastructure, made it attractive for multinational companies to set up operations there. China is also a key supplier of goods and components to the global market, and its manufacturing sector is a significant contributor to its economy and to the global economy as a whole.

As the world reopened, China remained closed. And this decision severely impacted global supply chains at a time of already high inflation. Supply shortages continue, however we expect these bottlenecks to resolve as China reengages with the world.

A year of review

Despite the challenges faced by the global economy, we remain confident in our portfolio companies. Each company has been selected based on key characteristics:

- a durable business model
- a sustainable competitive advantage
- the ability to produce a high return on invested capital

Our process ensures we consider the long term prospects of each company, and absent a change in the valuation, as prices fall we will purchase more shares to lower our entry price. We have done this for a number of our portfolio holdings over the last 12 months.

Portfolio investments

Our top three investments in 1H23 were Deere & Co, Shopify and Booking.com. We discuss each below.

Deere & Co

Deere & Co continued to perform strongly in 2022 as demand for farm machinery, buoyed by high commodity prices, accelerated the upgrade cycle. Deere's investments in precision agriculture are helping farmers become more efficient, improving both their bottom line and yield. We continue to take a cautious approach with Deere, and have reduced our position weighting as the share price appreciates.

Shopify

Shopify, the global commerce platform, performed strongly as more merchants, large and small, discovered the benefits of Shopify. It has built a class leading online platform which boasts an expanding group of dedicated software developers and today powers 10% of all US ecommerce. This drives the flywheel as more merchants are attracted to the developer apps.

As Shopify evolves it is attracting the attention of larger merchants and this is evidenced by the growing cohort of Shopify Plus merchants on the platform. Shopify is still in the very early innings of its evolution and counts a growing number of enterprise merchants as customers.

We are excited by the recent launch of "Shopify Components", which opens the platform to more enterprise merchants by offering flexibility to choose from many components including Shop Pay, their class leading checkout.

Booking.com

Booking.com is well positioned to benefit from strong online travel bookings driven by several tailwinds including a demand recovery for travel in the short term. Additionally, increasing consumer digital awareness and adoption post the pandemic is propelling the overall online travel booking penetration.

We believe Booking's "connected trip" strategy, brand equity and ecosystem and solid business fundamentals will allow it to continue to grow in excess of industry trends and capture increasing market share. It can leverage its scale and brand ecosystem to accelerate the network effects of partnering with more travel service providers and providing additional services to provide the best consumer experience.

2023 Outlook

It would be foolish to think there aren't surprises waiting in 2023, however our businesses have the wherewithal to respond to any environment. We expect interest rates to peak in 2023 and inflation to continue to moderate. Inflation remains a wild card and will need to be monitored.

While share prices swing between fear and greed, our valuations do not. We remain optimistic of a recovery in our portfolio companies as investment markets normalise. January has emerged as a very strong month with the Swell Global Portfolio increasing 16.7%, 13.7% ahead of the market.

We never know what the market will do on a day by day, quarter by quarter or year by year basis. However, we do know that over time, high quality companies with a sustainable competitive advantage and experienced management will continue to increase their intrinsic value.

We look forward to providing a further update in June.