Understanding the Market

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InterPrac Model Portfolios Update

Five years ago, we commenced the **InterPrac Model Portfolios**. We targeted a total return of 10-11% per annum over rolling 5-year periods, offering low cost, exclusive, actively managed equity portfolios.

The Income Portfolio had a goal to see us deliver 5% income every year, and average 5% capital growth per year over a 5-year rolling period.

The Growth Portfolio was looking to achieve a higher capital growth average of 8% per annum or 46% growth every 5 years, plus 2-3% income per annum.

Whilst these returns may not seem that exciting, we are looking to provide consistency and a lower risk growth target, compared to the index, by buying at price lows and selling at price peaks.

In 2015, after 2 years of tracking our performance we added the Portfolios to the HUB24 platform.

Setting up the Portfolios in the HUB24 platform as Separately Managed Accounts, means clients of InterPrac advisers get access to the Portfolio where we make the changes.

Our Portfolio trading plan is simple. We look to take advantage of the volatility, setting Fair Values of all ASX 200 stocks and a short list outside the ASX 200, publishing these on a weekly basis, so advisers can track them. We buy when companies we like trade below 85% of Fair Value, and sell when the share price moves above 120% of Fair Value.

In essence, each constant $1 Fair Value during our holding period, is bought at $0.85, and sold at $1.20, for a 42% growth return.

We employ this strategy because history shows that individual stocks go through popularity cycles, and the market goes from bullish to bearish very quickly. Buying when others are nervous and selling when others are greedy has stood the test of time.

From an ASX 200 index point of view, we also know that over the 10 years prior to the commencement date the Portfolios were listed on HUB in 2015, the ASX 200 return was 7.91%. **Not 7.91% per annum**, but 7.91% of actual capital growth over the entire 10-year period, from 1 January 2006 to 31 December 2015.

On 1 January 2006, the ASX 200 was 4,929 points and by 31 December 2015, it had only risen to 5,295 points. It is now about 10% higher again.

In that 10-year period, and prior to commencing the Portfolios, I was of the view the opportunity was to use the index volatility as our friend.

In the 2005 to 2015 period the index traded as high as 6,500 points and as low as 3,700 points. In our opinion, having a passive approach simply buying the index or the biggest caps and holding was a floored strategy.

Today, some 5 years since the Portfolios went live, I am pleased to say we have outperformed the index significantly, and more importantly, achieved the first 5-year performance targets we set as our benchmark.

In May 2012, the ASX 200 index was 4,096. On Friday, the ASX 200 closed at 5,722, around 40% higher than in 2012 when we commenced the InterPrac portfolios. I accept that the environment to reach our target return in this 5-year period has been friendly, particularly for income stocks, which have had the added tailwind of falling interest rates to prosper.

The average ASX 200 income yield over that time has been 4.3% or in total return, around 21% of income in 5 years. An ASX 200 index investor over that 5-year period has generated a total return of 62%.

In the same period, our Income Portfolio has achieved 145% total return, whilst the Growth Portfolio has achieved 82% return, both well ahead of our forecasts.

The major reason for the major outperformance in the Income Portfolio has been a result of the volatility in the top 20 stocks of the ASX. We have been able to buy more than 15 of the Top 20 companies at 85% of Fair Value and sell them over 120% of Fair Value over the last 5 years, and in many cases been able to buy them back again when the index fell back.

We have made some mistakes, and we will learn from some of these. I believe the next 5 years will see us continue to provide your clients outperformance and a Portfolio of growth on capital invested.

Arguably, the most exciting fact in regards to the first 5 years performance of our Portfolios is the income generated from the Income Portfolio for the initial portfolio holders.

At present, our Income Portfolio yield is just below 6%, which for those clients who invested at the outset $100,000 of capital and let the income compound, the $100,000 capital is now $245,100 generating over $14,700 of mainly franked income.

	Income Portfolio	Growth Portfolio	ASX 200
12 Month total Return to 30 June 2017	26.53%	12.93%	13.1%
5-Year total Return to 30 June 2017	145.10%	82.34%	62.8%

I do not expect that the past performance of the Income Portfolio will continue in an environment where interest rates are likely to rise rather than fall, as they have over the last 5 years. I do expect the Portfolio to outperform the ASX 200 index, and I do expect 5 years of 5% growth per annum plus 5% of income per annum.

In regards to the Growth Portfolio, I do believe this portfolio will move to a situation where the capital growth outperform the Income Portfolio over time. At present, the Growth Portfolio is trading at almost a 15% discount to Fair Value, and that gives me confidence the next period of reporting will see it close the gap on its sister portfolio.

No matter what happens, as long as the minds of investors continue to move from a bullish state to a bearish state, our trading strategy of buying the bottom and selling the top of fair valuation will hold us in good stead.

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