Markets have changed. We need to respond accordingly.

Refining the Market Matters investment process

Dear Members and Investors,

We are writing to outline an important refinement to the way we manage the Market Matters Portfolios. A core part of our philosophy is the belief that our process can always improve. With that in mind, we have undertaken a detailed review of the past year's performance and identified several lessons that will shape how we manage portfolios going forward.

Performance provides the context

FY26 was a positive year overall. Each of our three primary strategies delivered solid absolute returns and outperformed its respective benchmark over the full financial year. The longer-term record also remains strong.

Strategy	FY26 return	Benchmark	Relative return	Since inception p.a.
Active Growth	8.35%	6.11%	**+2.24%**	12.30%
Active Income	17.68%	8.17%	**+8.51%**	9.67%
International Equities	17.58%	14.78%	**+2.80%**	18.58%

Since inception, the Active Growth Strategy has returned 12.30% per annum against 9.21% for the ASX 200 Accumulation Index. The International Equities Strategy has returned 18.58% per annum against 13.91% for its benchmark, while the Active Income Strategy has returned 9.67% per annum compared with 5.59% for its benchmark.

These are good outcomes. However, the full-year figures do not tell the complete story.

A strong first half, followed by a difficult second half

The first half of FY26 was exceptionally strong, particularly for the Active Growth and International Equities strategies. Active Growth gained approximately 11.8% in the first half compared with around 3.7% for its benchmark, while International Equities gained approximately 28.2% compared with around 8.7% for its benchmark.

At one point, Active Growth was approximately 10% ahead of the benchmark. Strong stock selection and portfolio positioning also generated substantial outperformance in International Equities. The second half was markedly different.

Strategy	Second-half return	Benchmark	Relative return
Active Growth	-3.05%	+2.37%	-5.42%
Active Income	+3.97%	+4.02%	-0.05%
International Equities	-8.27%	+5.59%	-13.86%

Both strategies still finished FY26 ahead of their benchmarks, but a meaningful portion of the first-half advantage was surrendered. We are pleased with the positive absolute and relative returns; however, we are disappointed by the extent to which significant outperformance was handed back.

The Active Income Strategy provided a useful contrast. It returned 17.68% for FY26, outperforming its benchmark by 8.51%, with its diversified mix of equities, listed credit and income securities producing a more balanced return profile.

Markets have changed

The structure of global equity markets has evolved. Passive investing, quantitative strategies, algorithmic trading and momentum now influence a larger share of short- and medium-term market movements.

- As capital flows into index funds, the largest and strongest-performing companies receive the greatest allocation. Rising prices increase index weights, attracting further passive buying and reinforcing positive momentum.
- Disappointments, earnings downgrades or lost momentum can trigger self-reinforcing selling, with quantitative, passive and risk-management flows driving shares lower regardless of valuation.

Market returns have consequently become more concentrated, particularly around large technology and AI-related companies. Stocks outside that narrow leadership group can experience sharp and extended declines, while the strongest performers can continue rising well beyond levels that traditional valuation analysis might initially suggest.

Momentum has always influenced markets. What has changed is the amount of capital responding to it and the speed at which trends can become self-reinforcing.

What we learned from FY26

The weaker second-half performance was not the result of one broad portfolio decision. Several individual positions had a disproportionate negative impact on returns, particularly within the Active Growth and International Equities strategies.

- The earnings outlook deteriorated through downgrades or weaker guidance.
- Execution or fundamentals weakened through operational disappointment or delayed catalysts.
- Market sentiment changed, with sustained relative weakness signalling a different assessment of the company or sector.

Our greatest weakness was not necessarily failing to identify these developments. It was not exiting quickly enough, or allowing too much time for the original investment thesis to recover.

As long-term investors, we have historically been prepared to look through periods of weakness when a company's underlying quality and long-term prospects remained intact. That remains an important part of active management. However, FY26 reinforced the need to distinguish more quickly between short-term volatility and a genuine deterioration in the investment case.

We will continue to give successful investments time to compound, while giving deteriorating investments less time to damage portfolio returns.

Fundamentals remain the foundation

We are not abandoning fundamental investing, nor are we becoming a momentum strategy. The long-term value of a company will ultimately be determined by its earnings, cash flows, returns on capital, balance sheet, competitive position and ability to reinvest profitably. These factors remain the foundation of our approach.

However, valuation alone does not necessarily provide protection when earnings expectations are declining and market momentum has turned decisively negative. A stock can appear inexpensive and continue to become cheaper if its earnings base is being revised lower. A high-quality company can also remain a poor-performing investment for an extended period if execution disappoints or anticipated catalysts repeatedly fail to emerge.

Our process already seeks to identify earnings changes and revisions at an early stage. The refinement is to respond more decisively when those changes move against us.

What will change

Going forward, we will apply greater discipline when both fundamental and share-price momentum move against an investment. This does not mean selling automatically when a share price falls or reacting to every disappointing announcement. It means being more willing to reduce or exit a position when credible evidence shows that the risk-reward profile has deteriorated.

- The investment thesis weakens through earnings downgrades, operational disappointment or deteriorating management execution.
- The risk-reward deteriorates as industry conditions worsen, catalysts are delayed or fail to materialise, or valuation no longer compensates for the risks.

- The market confirms the change through sustained relative underperformance and price action consistent with weakening fundamentals.

We will place greater emphasis on the direction of change, rather than relying solely on the absolute quality or valuation of a company. A good business is not automatically a good investment at every point in its earnings cycle.

Greater caution when averaging down

We will apply a higher threshold before adding to underperforming positions. Buying more can work well when weakness reflects a temporary issue and the market has overreacted. It can compound the damage when the underlying fundamentals are also deteriorating.

Before materially increasing a weaker position, we will require clearer evidence that the investment thesis remains intact, earnings are stabilising, management has a credible response, the balance sheet remains resilient and both fundamental and share-price momentum are beginning to improve.

Where that evidence is absent, preserving capital and maintaining flexibility will take priority over attempting to identify the precise bottom.

A more disciplined sell process

Investment managers spend significant time considering what to buy, but the decision to sell is equally important. Our sell discipline will be connected more explicitly to the same factors that drive our initial investment decisions.

- Does the macro and sector backdrop remain supportive?
- Are earnings momentum and company fundamentals strengthening or developing as expected?
- Does the position still offer compelling upside relative to its downside risk and the alternatives available today?

Where the conditions that supported the original purchase are no longer present, we will act more decisively. The price at which we purchased a stock will not determine whether we continue to hold it. The relevant question is whether the prospective return from today’s price remains attractive relative to other opportunities.

This may mean accepting a loss when an investment case has changed. While never desirable, a controlled loss is preferable to allowing a deteriorating position to have a disproportionate effect on portfolio returns.

Momentum as an input, not the strategy

We will give greater weight to momentum as both a source of information and a risk-management tool. Fundamental momentum tells us whether earnings, margins, cash flows and expectations are moving in the right direction. Price momentum tells us how investors are responding and whether confidence in the company is strengthening or weakening.

Neither should be used in isolation. Momentum without valuation discipline can lead investors to buy companies at prices that assume unrealistic outcomes. Valuation without attention to earnings direction can result in holding stocks that appear cheap while their intrinsic value continues to decline.

Business quality + reasonable valuation + positive earnings direction + appropriate price momentum

When earnings revisions, operational performance and share-price trends all move negatively, we will be less willing to assume the market is simply wrong. Conversely, when improving fundamentals are confirmed by positive earnings revisions and relative strength, successful investments will be given more room to compound.

Managing position size and portfolio impact

Because our portfolios generally hold approximately 20 positions, individual decisions can make a meaningful difference to returns. This concentration is deliberate, allowing our strongest ideas to contribute meaningfully. It also makes position sizing and downside management especially important.

We will be more proactive in reducing positions where the risk-reward profile has deteriorated. In some cases, this may involve initially reducing a holding rather than immediately exiting it. We will focus not only on whether we remain comfortable owning a company, but also on whether it continues to deserve its current weight in the portfolio.

A stock may remain a valid investment while no longer warranting a full position.

What will not change

The foundations of the Market Matters investment process remain intact. We will continue to:

- combine macroeconomic, sector and company analysis;
- focus heavily on earnings and earnings revisions;
- seek growth at a reasonable price;
- construct concentrated portfolios; and
- invest with a medium- to long-term horizon.

We are not becoming short-term traders or pure momentum investors. Momentum is becoming a more important input into our existing process, not a replacement for it.

Improving the consistency of returns

The purpose of this refinement is to improve the consistency and balance of portfolio outcomes. FY26 demonstrated that strong stock selection can generate significant outperformance. It also demonstrated how a small number of deteriorating positions can offset a meaningful portion of those gains when losses are allowed to compound.

We do not expect to eliminate losing investments. No active investment manager can do so, and attempting to avoid every loss would likely produce excessive trading and missed opportunities. Our objective is to ensure that individual mistakes remain manageable and do not have a disproportionate impact on overall returns.

Markets have changed, and we need to respond accordingly - without abandoning the principles that have produced strong long-term returns.

An evolution of a proven process

The Market Matters investment process has been developed, tested and refined over many years. It has produced strong long-term returns and remains the foundation of how we manage portfolios. The changes outlined in this letter are an evolution of that process, informed by both the experience of FY26 and the changing structure of modern equity markets.

We believe the increased emphasis on earnings revisions, price momentum, sell discipline and downside management will make our portfolios stronger and improve our ability to deliver attractive and consistent risk-adjusted returns over time.

Thank you for your continued trust and support.

Yours sincerely,

James Gerrish
Lead Portfolio Manager
Market Matters