Ed Reekie:

(silence). Good afternoon everyone. Thanks for joining us. We'll start in just a couple of minutes. Thank you for joining. (silence). Right. It's just after the hour, so let's get started. Good afternoon, everyone. A very warm welcome to you all. And thank you for taking the time to join the Hyperion CIO this afternoon in this discussion. Why successful investing in sustainable businesses is fate not fad? By way of introduction, my name is Ed Reekie, I'm one of the directors at Pinnacle Investment. I know a number of existing investors and supporters are on the line today. And I thank you for your support. And for those, for whom this is a first introduction, then welcome to the club. I hope this is the start of a long and rewarding journey for you and for your families.

Ed Reekie:

I'm delighted to be joined today by Hyperion CIO, Mark Arnold, and deputy CIO, Jason Orthman. These guys are one of the best and arguably the best investment team in Australia and have driven successful outcomes and compounding returns for high-paying investors for many years. Remember Mark being part of the founding team and building the investment process back in 1996, that's 25 years ago, and Jason becoming a key part of the team over 14 years ago. It's a process that is proven and it's a team that is enduring. The timing of our conversation today is also ideal. Morningstar Australia have just named Mark and Jason's team as the fund manager of the year 2021. This is for the second time, having won that highly coveted award only five years ago.

Ed Reekie:

And secondly, Mark and Jason have also just launched listed access to their global fund. Direct investors can now enter or exit the flagship fund with just a click of a button via any online share trading platform. The fund is a concentrated portfolio of 25 elite global winners that have demonstrated that they have a sustainable and a competitive advantage that allows them to target EPS growth of 20% or more on average each year for the next decade.

Ed Reekie:

The agenda today is wide ranging conversations for 35 to 40 minutes covering sustainability and other areas where you have focused. Mark and Jason published regular white papers, host regular webinars, all of which are available on hyperion.com.edu. Today the format be less webinar presentation, and more interactive discussion and an opportunity for you to raise questions directly with Mark and Jason. Thank you for those that have asked already questions. We've got them and we'll probably start with them and we'll do our best to focus on issues that are most important to you. And please use the Q&A button to get those questions that are most important to you.

Ed Reekie:

There's a Q&A button on the bottom of your screen. I would note there's also a chat button, which doesn't help. But it's the Q&A button that is the one, please hit that to raise your questions. I'll try and group questions together. So in the time available, we can cover as much ground as possible and focus where you have interests. Mark, Jason, thank you for being here today. Mark, probably get the ball rolling with you to get some context and history behind Hyperion's approach to sustainable investing. I mean, obviously we're seeing increased interest from investors around ESG, around green investing, around sustainability, a lot of different views on exactly what that all means. Could you give us an overview of Hyperion's approach to sustainable investing, what it looks like and also a little bit of history as part of your investment process, given this probably been embedded in your approach for years and even decades before it became the hot topic that it is today.

Mark Arnold:

Thanks Dd. Good afternoon. Everyone. Sustainability has always been core to Hyperion's investment philosophy and process since it was established in 1996. Our values include long-term thinking and acting as business owners. We're not short-term share traders. The investment horizon that we have is 10 years or greater when we're investing in a company. And our average stock holding period in the portfolios is approximately 10 years. We invest our client's capital in high quality businesses with strong and sustainable value propositions to all stakeholders, not just shareholders.

Mark Arnold:

The stakeholders include the wider community and assessment of the company's future long-term impact on the overall natural environment, including its carbon footprint. We think that this approach to long-term sustainability as a core part of our philosophy assists in reducing the risks of permanent loss of capital across our portfolios. The typical market participant only hold stocks for between nine months and 15 months. And we believe that these types of market participants are really speculators and not investors. Short term renders of stocks don't care about the long-term fundamentals and sustainability of the business. Sustainability becomes less relevant over shorter periods of time.

Mark Arnold:

Without a strong value proposition to all stakeholders, including customers, staff, suppliers, government, and society generally, businesses will eventually fail. Any party in this ecosystem that begins to reject the businesses and value proposition will put at jeopardy the long-term health of the organization. Back to you, Ed.

Ed Reekie:

Yeah. Thank you, Mark. And also thank you for your questions that are coming in. Lots around kind of inflation downside protection, which we will cover. Please keep those sustainability questions coming in. Carbon obviously is a big factor that Hyperion's taken very seriously. Mark, do you want to sort of make some comments about that? I think you've made efforts to neutralize your past footprint. You've got a portfolio that's very low carbon, some comments around that.

Mark Arnold:

Yeah. We think that you need to lead by example. That's why we've neutralized out the business's carbon footprint. We think that that's important for credibility when we're talking to third parties, including management teams and boards. Our companies already have a really low carbon footprint, as you can see from the chart that Ed's put up. And it sits around 14% compared to the benchmarks. And we think that this is important in terms of risk reduction because carbon emissions are one of the largest externalized costs of most businesses. And we believe that externalized costs will eventually be internalized. And that's going to adversely affect many businesses that are listed on the stock exchange today. We think that society will eventually demand a price on carbon as awareness grows of the negative impacts of climate change.

Ed Reekie:

Yeah. Very interesting. You mentioned externalized costs. I think we'll probably come back to that because that's obviously going to be a big feature. Jason, risk, I mean, a lot of it is risk reduction as much as enhanced returns. Do you want to sort of make some comments about, in that context, how you see sustainability?

Jason Orthman:

Yeah. Well, we think as long-term investors sustainability does reduce the fundamental business risk in your portfolio and therefore enhances returns because if you are a business that's taking shortcuts, you are externalizing costs like Mark mentioned, you might be polluting the environment, pushing carbon into the atmosphere, causing health issues for customers, eventually society. And those parties will make you pay for that.

Jason Orthman:

And so you end up getting these black swan events or a drop in permanent value or a loss in the intrinsic value of these businesses. And so there's high levels of fundamental risk if you're not operating sustainably. And then what that means is obviously at an individual stock level if you don't behave appropriately and your intrinsic value to clients, that reduces returns at an individual stock level and therefore impacts your overall returns at a portfolio level. Being a business analyst, a long-term shareholder, you absolutely need to get a risk out of the portfolios and maximize your overall long term returns.

Ed Reekie:

You talk about individual stock level, without throwing mud in there examples, I guess of stocks where you haven't invested because of ESG issues. And I guess, are you able to have those issues that you envisaged already played out in the market? Or do you think in the case, one of the examples I know, is it yet to play out?

Jason Orthman:

Yeah. Well, that's a good point because often you don't see those stocks as we screen them out and avoid them [inaudible 00:12:32] get caught up in some of that stuff. But over time there's numerous high profile companies, which have been good growth companies at times. And I recall looking at Leighton Holdings, which they basically dominated construction because they had a number of subsidiaries bidding in these projects, often one work and it was quite at high margins. And so we looked at that as a growth investor, but we couldn't get comfort in terms of, they were pretty tough on their suppliers and I guess it is a tough industry.

Jason Orthman:

And as well, when you looked off shore, a lot of their revenue was coming from pretty exotic places, I guess. We just had some concern around the sustainability and how hard that industry and they were a market leader, but we couldn't get comfort as a long-term business owner and obviously had a bit of a patchy history and was eventually taken off the exchange. There's numerous examples like that, that Hyperion never talks about or mentions because we've just screened them out upfront. And at times this are good companies, but eventually it does catch up to you.

Ed Reekie:

And when you say eventually, what kind of time horizon?

Jason Orthman:

Yeah. Well, our investment horizon is 10 years. And that's the difference, Mark mentioned the market turns over nine to 15 months, and so they're not investors. And so maybe you're thinking of trade out of these positions, but it's a pretty competitive space to that short end and it's easier just to compound capital over 10 or 20 year periods. And that's why we're so focused on issues like carbon, you know what's happening around pollution and how you treat the vendors around you, because it will play out in that 10 year time horizon.

Ed Reekie:

Yeah. I mean, it is interesting, if you own a piece of paper for a month and the chances that the regulation hits you during that one month, I guess is quite low. If you own it for a decade, then the chance that you're going to be owning that company when that regulation comes, I guess is almost guaranteed, over a 10 year horizon. You talked about screened out. We might cover that later on because I'd be interested, and I guess the audience would be in terms of, is a one screen or two screens that really you notice really pick out a lot or really trim it down. So we might come to that.

Ed Reekie:

We talked about, the title of this is, is it fad or is it fate? And I guess Mark, I don't know whether you want to sort of make some comments about this, is it a gimmick, this ESG? I know the acronym ESG gets thrown around with [inaudible 00:14:54]. In fact some even get the words wrong, environmental social governance, what the S stands for. But it's run about with [inaudible 00:15:05] abandon. Is it a gimmick? And I guess in answer to that, are there other things that you think might be gimmicks? I mean, I know that's not sustainability, but elsewhere that you think might be gimmicks in the marketplace.

Mark Arnold:

Well, we think true sustainable investing is not a marketing gimmick, but greenwashing does go on and so there are some businesses that try to address themselves up as being environmentally friendly, but they're not. But to us sustainability really relates to long-term fundamental outcomes. If you compare that to something like shorting, shorting really relates to the short term to share prices and there's outcomes based on short term metrics. We think shorting is about protecting portfolios against short-term share price movements, regardless of whether the share price movements are representative of long term fundamentals. If you sort of compare and contrast sustainability and shorting, we think sustainability stands for substance and longterm-ism, but we think shorting is more suffered superficial and relaxed to the short term.

Ed Reekie:

And I guess your process is all around compounding. How much kind of short compound?

Mark Arnold:

Yeah, that's right, because the upside is really 100% if the company goes broke that you're shorting. We're interested in compounding way above 100% over time. There's not real longterm exponential growth in shorting, is by definition really a short term tactic.

Ed Reekie:

There's a question in here too, which we might just cover at the same time, talking about hedging. Obviously some of you make a big noise about hedging, the fund is unhedged. Can you just talk us through the logic behind that?

Mark Arnold:

Well, we think that the wealth creation is going to be driven by the compounding of EPS, underlying the portfolio over long periods of time. We've got a bunch of businesses in each portfolio that can grow organically at double digit rates over long periods of time. And it's really that compounding effect of earnings and cashflows going up at double digit rates. It's really going to dominate the long-term return profile of our portfolios. Currencies will fluctuate from time to time, but there's not really a compounding effect that goes on there. And so we like to keep things simple so we can explain how we manage money to external parties. And that's an important component of how we run the business so we don't hedge.

Ed Reekie:

And just to put that into numbers, the global funds got a EPS forecast going forward of high twenties. How much do you think hedging might impact that? Sorry. How much do you think currencies might impact that one way or another?

Mark Arnold:

Very little over long periods of time, [inaudible 00:18:45] shorter periods of time where the currency can move fairly materially. But over longer periods of time I think it really nets out. And it's really that, as I said before, that EPS compounding in that exponential growth that drives the wealth creation underlying the portfolios.

Ed Reekie:

Yeah, absolutely. Now, my knowledge of Friedman's being, or lack of knowledge is being highlighted here. There's a question about the overlap between Friedman and sustainability, can sustainably co-exist with Friedman's raison d'etre for business, or does this need to rethink. Mark, are you going to take that one on?

Mark Arnold:

Yeah, I'll have a go. I think Friedman's theory does need a rethink. Friedman's focus was really on short-term profit growth, whereas sustainability has a focus on long-term economics and it has a focus on a broader range of stakeholders. Friedman believed that the social responsibility of business is to increase its profits. And he's famous for that belief that basically short-term profit maximization should be the sole focus of management and that basically companies only exist to benefit shareholders. We disagree with that. We think that you should take a broader approach. We don't like a focus on short-term outcomes. We think that that's sub-optimal way to manage portfolios. Also pure focus on a narrow group of stakeholders is also unhealthy and unsustainable we think as well. So yeah, we think that the theory does need to be rethought about.

Ed Reekie:

Yeah. And I guess it's over what time horizon as well. Over a longer time horizon, all those costs will come back to shareholders but they'll, those time horizons. Going slightly off, we've got a few, quite a lot of questions just about this rotation that's happening at the moment. We come in and out of sustainability. Jason, there's few here actually that talk about the reporting season. It was obviously very good for banks minors. I think in a old world companies, as you might call them, did pretty well. How do you see the reporting season and how do you react to these old world businesses having time in the sun?

Jason Orthman:

Yeah. Well, I mean, the Hyperion portfolio has had a really strong reporting season as well. We were accruing excess returns above the benchmark as we ran through January and February, because the company that we own produced really resilient results. And they're not that sensitive to economic conditions. But what happened about five days out from the end of February was that a rotation started with bond yields sort of rising. But we look out again longer term, so we go back and think, well, was there any issues with reporting? No, that was incredibly strong for us. Is there any change with our valuations? No, there wasn't. The US tenured money has to rise from here and that's embedded in our valuation, so no change there.

Jason Orthman:

And then when we think about the macro economic outlook, well, once the vaccines come in, we get through this COVID-19. Well, it's still going to be a really tough, difficult world, and it's just with more debt. We don't think anything's fundamentally changed and chasing minors or major banks is pretty unlikely for us. And they're commoditized, particularly the larger mining companies, they're price takers. It's hard to add value in forecast over a 10 year period. And then as we move into thinking about fossil fuels, traditional coal, oil and gas, I think the odds of us owning a business like that from, you probably guessed would be like zero.

Jason Orthman:

And then the major banks, we don't think they're relevant to the next generation and haven't really been particularly treating their staff and the next generation with the respect they deserve. And that's why other companies come in and offered a better value proposition are starting to take share. Chasing minors or major banks or those lower quality stocks is not a sustainable strategy, and it's not a way to generate wealth over a long period of time. It'll be temporary and we're very confident that the fundamentals are with us.

Ed Reekie:

It's interesting. You talk about old world, I've seen some analysis where you split the markets globally and Australia and sort of old world, new world. Do you want to make some comments about what that split looks like? And I guess what new world to you looks like?

Jason Orthman:

Yeah, there's a few elements there. Obviously defining old world is so we're all on the same page, which for us means low growth, no growth and the risk of disruption by the next generation changing their purchasing decisions or just better products coming along, so that's how we defined old world, no growth and losing relevance. And to your point, when we look at the ASX 300, which is obviously the

Australian Stock Exchange effectively and what we're benched to, 77% of that is old world by market weight.

Jason Orthman:

And then when we go globally, the MSEI world, which is developed markets at 64%, and then even when you go into the US at the S&P 500, it's 53%. And so these benchmarks are just full of incumbent businesses, which their intrinsic values actually declining. And so then you think, well, what are we going to do? And obviously we're looking out with a 10 year timeframe and investing is about looking forward. So we've got to go and move from the old world and then to the new world. And what that really means is we need a bunch of modern businesses. They were written in a really strong value proposition or reason for existing. Often that's a 10X improvement in the price they're offering consumers at 10 times but a better product. You need strong, competitive advantages as well, because if you've got a new business, you need to defend this other stuff to copy. Just because you lead a category doesn't mean you can sustain that. And so they're the type of characteristics that we want, but again, it's the opposite of old world, it's modern, relevant, defendable, sustainable businesses.

Ed Reekie:

I've just pulled up some themes there that might give a clue. And also some names there that, again, we might sort of jump back to at some stage. We've talked about externalized costs in the opening few minutes. I mean, I think this is a fascinating concept that you guys talk about. Can you just give us a little bit of a history lesson? What do you mean by externalized costs? And who's going to force them to become internalized? Mark, do you want to have some comments on that?

Mark Arnold:

Yeah. The externalized costs associated with the business that are not actually paid by the business. And they end up being borne by third parties including the community and in some cases future generations. Externalizing these costs effectively means that the businesses profits are higher than they would otherwise be. And then the community or third parties are actually paying for those costs. Eventually companies with externalized costs are forced by stakeholders to internalize them either through regulation or changing expectations of society.

Mark Arnold:

A good example, a recent example was VW and [inaudible 00:27:08], where VW effectively boosted their short term profits by avoiding the costs of having to manufacture cars that produce less air pollution. And regulators came in and basically find VW as a result of that. So that is externalized costs were internalized by regulators. Other examples are tobacco companies, for many years are externalizing costs because they were selling products that caused illness. So that was really increasing healthcare costs and basically killing their customers. Eventually the regulators ended up taxing those companies. And similarly with CO_2 emissions. We think that over the longer term fossil fuel related companies will be forced to internalize the costs of climate change. And that will happen through government bodies and regulation over time and some sort of carbon tax or carbon pricing.

Ed Reekie:

If you're renting a piece of paper that certainly has to internalize those costs, it's obviously a pretty uncomfortable experience through that journey. We also talked a lot of headlines, maybe jump into a couple of stocks. As you can imagine, we've had heaps of questions on Tesla. I guess that fits quite well just in terms of the sustainability angle and moving away from carbon. Jason, could you make some comments about Tesla and maybe one other holding if anything comes to mind. The questions on Tesla are a lot about how do you have confidence about 10 year earnings? A lot of EV competition is going to come, those kinds of areas.

Jason Orthman:

Yeah. Well, I think you highlighted 12 structural themes earlier, and probably the most important to us is actually that transition to sustainable energy and transport. I mean, society can get combustion engines off the road. That's one of the easiest things we can do to address these climate issues. And you mentioned Tesla and Tesla is really leading that, and that's one of our most important holdings too. It's our top holding around a weight of 12%. But it sells 500,000 cars per annum, so it's just started on that journey.

Jason Orthman:

And Mark mentioned VW, Volkswagen, and those leaders like general motors as well, they sell 10, 11, 12 million cars per annum, and we believe that Tesla will take that mantle and take that leadership over the next 10 years and sell 10 million themselves because the product is simply better. But I mean, Australians have done great getting solar up on the roofs. And the next thing linking that together is actually getting a Tesla or some of EV in the garage. And then also getting storage and we're quite optimistic as the price has really come down and battery technology improves, that trifecta will occur. As I said, [inaudible 00:30:18] have done a great job getting solar running. The next thing is to get batteries and storage in your home.

Jason Orthman:

I think Tesla will lead the world in that transition to sustainable energy. And we've been on the right side of that investment, the last 12 months has been great. It's probably gone up six times since we bought it, because we waited five years before we did it. We got an inflection point, but we're only one year into that 10 year plus journey. And we think this upsides absolutely significant when we look over the next decade plus.

Ed Reekie:

And Jason on that, when you look at the relative size of the markets, people think this is worth an 8 trillion car addressable market, how big are the energy markets? How big are the ride share markets? How big are the bigger prize for Tesla?

Jason Orthman:

Yeah, it's a 20 trillion US market for us. And we believe that might end up being conservative. It's hard to size up those markets, but obviously Tesla is doing sort of 30 billion plus of revenue and call it 20 trillion plus market, the opportunity size is huge and energy is sort of only 7% of their business. And at the moment, any spare capacity and batteries they get goes into pushing autos out onto the road. There's not just one revenue stream. Obviously we mentioned the auto and scaling from 500,000 cars to 10 million plus. And by the way Tesla is dream is, and Elon's dream is to go to 20 million per annum. There could be upside to what we think, but there's a handful of other revenue streams, and you try to touch on them, Ed.

Jason Orthman:

And people can't capture them unless you actually think seriously about it, act as an investor and try and think out 10 years. If you're looking out 12 months or even just taking the results today, trying to value it on 500,000 cars or the energy business as is today makes no sense. Again, investing it's about the future and what's going to happen.

Ed Reekie:

Yeah. And this might be a just good moment. I can't help but just shares numbers because that's a single stock man. And when we just put it all together, I've just thrown out. I don't know whether you can see on the screen, the recent performance numbers. This is basically when you put it all together and build a 25 stock portfolio looks like. I mean, it looks like just a barrage of numbers. And I think it's worth noting that the team talk about protect and grow. We've talked about, there's no shorts in these portfolios. There's also no derivatives. For Hyperion, I guess the best protection is just vanilla long, only investment in high quality earnings.

Ed Reekie:

If we just look on total return since inception, left-hand column, that really demonstrates the enormous power of compounding, adding out for the long periods of time, the lower of the two blocks to the Australian growth fund. Now second column in funds down 12.4% versus benchmark of nine. Put that in real terms that's difference between, they're doing 756% returns versus 389 for the index. And that's just what Mark and Jason talk about compounding. And if we look at the upper two, which is the global growth, the same compounding outcome is definitely becoming evident here over just under seven years delivered 300% return, more than double what the market has done at 124.

Ed Reekie:

I think, this is real numbers. And I should mention at this time too, for those that are new to the fund, the pricing structure is low and aligned. It's a 70 basis point management fee and the performance fee is only earned when the fund outperforms the MSEI. So just thought I'd quickly share that. Inflation lower for longer. Lots of questions about ... A lot of the audience are seeing an anemic world, a low growth world. What's your view on lower for longer? What are your thoughts about what's just happened in the last six weeks with US 10 years? Who wants to pick up that one?

Mark Arnold:

I'll have a go. We think that the world is permanently stuck in a low growth environment. There'll be a cyclical recovery over the next 12 months, but that's really just recovering back to zero. We think that the money printing that's been going on for quite a period of time and has been stepped up since the COVID-19 crisis is unlikely to be inflationary because it's really the aggregate demand side of the equation is quite weak. We think there's quite a few reasons why inflation will stay low longer term. There could be a short term cyclical pickup in inflation, but the structural reasons why inflation will stay low include energy becoming cheaper, that's deflationary.

Mark Arnold:

We think electricity is basically going to go down in price and the marginal cost of electricity longer term is going to be very, very low. We think transportation's also going to become cheaper and better. EVs are going to drive that in combination with autonomy. And so we think that that will be deflationary in nature.

Ed Reekie:

Can you put some numbers around that, the cost per mile of a car with a chimpanzee like me driving it versus a cost per mile of an EV.

Mark Arnold:

The cost will come down if you look at an autonomous car or a ride by taxi, we think that eventually the cost ... well, if you compare it to a number today, sort of the numbers generally around $2.50 to $3 per mile, and a taxi is more expensive generally than that. We think that an autonomous sort of ride by taxi network, you could easily price that transport at a dollar per mile or even less over time. And ultimately it would be that the cost per mile will be less than 50 cents. That will be very deflationary and there'll be a lot of people that don't end up buying cars because it won't make sense anymore, particularly if you're living in a high density sort of major capital cities. We think that that will be deflationary.

Mark Arnold:

The other thing is that AI, better computers and robots is going to be disruptive to human capital markets. Traditionally inflation has been driven by humans demanding higher wages, we think that that's going to be unlikely because surprising power of human capital is likely to go down as some machines and computers get better. And the final element of low inflation and low interest rates as a result of low inflation is we think aggregate demand is likely to stay weak because of aging populations and lower population growth and [inaudible 00:38:03].

Ed Reekie:

And we've got some questions on Japan, which if we have time we might just touch on because I guess that leads onto that. Mark, we have a couple of questions here about the IRR for the funds. Do want to make some comments about the IRR and I guess hand in hand with that a few questions on cash levels, are they related? Do higher IRRs mean low cash and vice versa or? Can you just make some comments on those two?

Mark Arnold:

We think the IRRs attractive at the moment particularly for the global fund. It's IRR sitting at around 20% per annum. We think it's a good time to get exposure to to the global fund. Particularly in a world that we think will be low growth over the longer term, so it's going to be difficult for passive benchmarks to produce the sorts of returns that they have done historically. So that would be our view and as a result of the high IRRs at the moment, the cash levels are still fairly low in the portfolio. That's a bit different if you go back to pre COVID-19, we ramped up the cash weights to around sort of 13%, 14% prior to the crisis. But that's because the IRRs were materially lower at that stage. We're quite positive on the outlook for the returns from the portfolios and the cash weight reminds fairly low.

Ed Reekie:

Thank you. Jason, a couple of sort of related questions that sort of coming in kind of, I guess momentum stretched valuations. I think a lot of people are agreeing here with your views about lower for longer, but in that environment still see current valuations of many of the companies that are excessive and is there momentum or we get the risk of getting caught up from the crowd, just because a lot of the crowd seem to be doing this. What are your sort of comments on that I guess?

Jason Orthman:

Yeah. I mean, that's a perennial issue. I mean there's no free lunches in market. So these businesses, if you're getting them at the inflection point and they are becoming the world's next best businesses, they're optically expensive. I guess the trick is to actually differentiate between those which become the next REA or realestate.com.au or the next Amazon, rather than a whole bunch of momentum stocks or concept stocks that just fade away. And it goes back to that turnover in the market that we talked about earlier, we really believe most people can't tell the difference between an average business and above average business and an exceptional business.

Jason Orthman:

And that's why you get these basket of growth stocks and momentum stocks or concept stocks. And you can't generate sustainable wealth owning a basket of those stocks because people do pay up, people pay up for the future. But the trick is selecting opportunistically within that basket of stocks those that actually come out the other side, those 1% to 4% of businesses that lead the market higher and that can grow sustainably. There's absolutely pockets of exuberance and overvaluation and most people do pay up for the future. But the reality is within that there are some businesses that are exceptional businesses and they are undervalued. And because when you look out in 10 years time, and Tesla is a perfect example on our earnings forecasts. They're trading on really low single digit P/E multiples or earnings multiples, and that's not realistic. As you keep producing the results and time go goes past and those earnings do compound, the share prices do follow. So you do need to know the system and that's that 10 year valuation mechanism and the quality mechanisms we've got in the process.

Ed Reekie:

Do you want to make a comment forward looking versus backward looking? Because I guess that's integral to that answer.

Jason Orthman:

Yeah, that's right. I mean, theoretically, how do you value a business? Its cash flow, future cash flows into perpetuity discounted back today. I mean, and that's unrealistic to forecast out a hundred year model. But the point of that is it is about future cash flows, not past cash flows. And again, using Tesla as an example, okay, does the valuation make sense on 500,000 cars? Well, absolutely it doesn't. But does it make sense if they achieve our forecast? Well yes, it does, and more. I mean, historical cash flows and results, they are a guide post, but investing is about the future and not about looking backwards.

Jason Orthman:

It's really what's valuable, is what are those cashflow going to be in 10 years time, not what they were today or next year. And that's the continual problem people have. And I think the reality is there's just not that many business analysts and longterm investors left in the market. So you get the momentum loops, you get the short term catalyst. But again, we don't believe that's a sustainable process to outperform.

Ed Reekie:

Talking about, we mentioned Japan there just briefly, Mark, do you want to just make a comment on that? I mean, the questions we're getting here is, is Japan, is there enough similarities to mean that we can use it as a playbook or is it too different?

Mark Arnold:

No. There's a fair few similarities, but it really relates to just the world adopting the policies that the Japanese government and central banks had for 30 years. But it's all in reaction to those structural headwinds that we mentioned before. That's really, the governments are reacting to that and trying to stimulate growth, but there hasn't been much success in Japan with those policies. And we think that it's pretty likely that governments and central banks, banks get the same results or very similar results to what they achieved in Japan, which is basically low or negative growth for a long period of time.

Ed Reekie:

Thank you for that. Couple of questions here, just in terms of downside protection, related momentum, I should have probably caught up with that one, but about the 2000 tech wreck, is it different this time, Mark, do you want to make some comments on that?

Mark Arnold:

Yeah. Well, a tech boom back in '99 was really, it related to the fact that the world knew that the internet was going to radically change economics and globalize everything and make information available to anyone that had access to the internet. But it was really difficult back then to work out who the winners would be. And a lot of the tech stocks that were bought up during that boom were merely concept stocks. Many of them had very little revenue let alone profits. So that was then if you look at the situation now, the tech sector has got some of the best business models in the world. They're real businesses, they've got significant revenue, they've got strong and sustainable competitive advantages, many of them, and they've got large addressable markets and they're quite innovative as well. Their products are getting better over time and they're developing new products. We think it's quite a different situation now compared to back in 1999.

Ed Reekie:

Thank you. Now I'm just aware that we're 146, so we're basically going to have to wrap up. There's one question that will probably just take, because I think I know what your answer is going to be, highest conviction idea over the next five years. But maybe let's talk 10 because that's how you guys look.

Mark Arnold:

Yeah. Tesla would be, it's our largest position at the moment. We just think for the reasons that Jason alluded to, we just think are in the best position in terms of EVs. EVs are a very small percentage of the overall car market today. But we think that over the next five or six years the penetration of EVs is going to grow dramatically. And technically the best position to grab a lot of that market share. The other thing that we like about them is that they're really a software business. And that's really at the core of that DNA and that makes them radically different to the legacy manufacturers that really don't have any expertise in software.

Mark Arnold:

And the EVs that Tesla produce are really computers on wheels. They're more like an iPhone than a traditional car. We think that that's important. And as Jason mentioned we think the energy business is going to be massive for Tesla longer term. They've got a very good solid roof product that we think will be a large revenue and profit generator for them long-term. And they've got the best battery technology as well, and they'll be able to leverage the battery technology they have across both their car business and also the grid business and the residential energy storage business. They'll get economies of scale that the other car manufacturers won't have.

Ed Reekie:

Thank you. And I guess one, typically this portfolio has been a 21, 22 stock portfolio, so it's currently 25. I guess the competition to be in this portfolio is higher than ever as you might be looking to trim two or three names to get back to your sort of standard numbers. Now in the interest time, I'm sorry to say, we're going to have to draw a line there. There's lots of ... I'm just trying to group the questions that are outstanding, and we will send you each a response to those questions that you've asked. Plastic specific questions, carbon offset specific questions, income distributions, bitcoin feature fair bit.

Ed Reekie:

The one I will just talk for 30 seconds on is the active ETF, lots of questions around that in terms of trading at NAV, et cetera, et cetera. Obviously it's the [inaudible 00:49:28] and the [inaudible 00:49:28] that have had problems in the past about discounts and premiums. Now, so the point about the active ETF is that the NAV is set every night as for the unlisted fund, and there's an INF that operates during the day for the short window between those two NAV publications. It looks as though it's only been trading three days, but the NAV that we provide to the market seems to be very, very accurate and working well. There should be very, very tiny movements in discount or premium to NAV, all of which are closed out every 24 hours.

Ed Reekie:

I think that's an important factor and just remind everyone online that it's one house and two doors. So you're owning exactly the same fund. It's just which door you walked into to own that fund. I guess just leaves me to thank Mark and Jason for making themselves available today. But more importantly to thank you, the online audience for your participation, for your questions. Like I said, there's been buckets of them. We won't be able to get back to them within the next 24 hours, but we will definitely work our way through and get a response to you as we go.

Ed Reekie:

Also say that we'll send a recording of this webinar to you on your email, and we'll also post it on the website, hyperion.com.au, where you can also stay connected on that website, reading the teams articles, all our white papers under insights, et cetera. Also sign up for regular updates from investment teams. Please jump on the website there. If you're interested in investing the two avenues like I mentioned, the global growth fund's now got two doors. You can enter via the unlisted door or the listed door. If you want to use the unlisted door, then there's an apply now button on the Hyperion website. If you want to use the listed door, then you can do it either using your online trading platform under the ticket, HYGG, or talk to your financial advisor or stock broker to access it that way. Thank you once again for taking the time today. We look forward to picking up the dialogue again in the very near future and wish you the best for the rest of the day. Thank you very much for your participation.