

DNR Capital Australian Equities High Conviction Fund

APIR code: PIM0028AU

Performance Report August 2023

Performance

DNR Capital Australian Equities High Conviction Fund decreased -0.34% (net of fees) in August, outperforming the S&P/ASX 200 Total Return Index by 0.39%. Over the last 12 months, the Fund increased by 9.49%, underperforming the Index by -0.07% (net of fees).

Net active return as at 31 August 2023

	1mth %	3mth %	6mth %	1yr %	3yr p.a. %	5yr p.a. %	7yr p.a. %	Incep.* p.a. %
High Conviction Fund	-0.34	4.09	3.42	9.49	15.93	9.29	10.30	9.94
S&P/ASX 200 Total Return Index	-0.73	3.92	3.00	9.56	10.68	7.01	8.57	7.70
Excess return	0.39	0.17	0.42	-0.07	5.25	2.28	1.73	2.24

* Inception Date—June 2015.

Source: DNR Capital and Apex Fund Services.

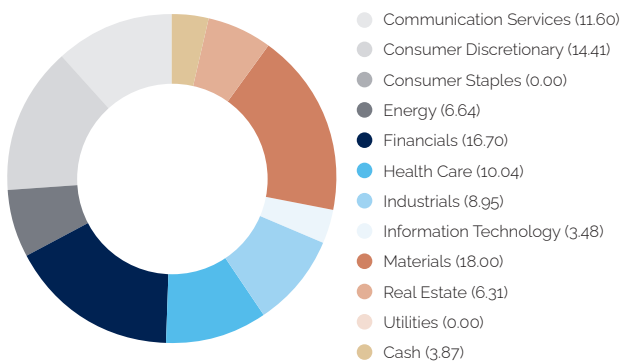
Past performance is not an indication of future performance. Total return shown for the DNR Capital Australian Equities High Conviction Fund has been calculated using exit prices after taking into account all of the product's ongoing fees and assuming reinvestment of distributions. No allowance has been made for entry/exit fees or taxation.

Growth of \$20,000 since inception



Source: DNR Capital and Apex Fund Services

Sector weightings %



Source: DNR Capital and Apex Fund Services

Top 5 active holdings

Security details

National Australia Bank (NAB)

CSL (CSL)

SEEK (SEK)

The Lottery Corporation (TLC)

Aristocrat Leisure (ALL)

Source: DNR Capital and Apex Fund Services

Monthly top contributors and detractors

Top 3 contributors

Carsales.com (CAR)

Domino's Pizza Enterprises (DMP)

James Hardie Industries (JHX)

Top 3 detractors

IRESS (IRE)

Ramsay Health Care (RHC)

Wesfarmers (WES, underweight)

Source: DNR Capital and Apex Fund Services

Experienced portfolio managers



Jamie Nicol
Chief Investment Officer



Scott Bender
Portfolio Manager

Performance attribution

Contributors

- Carsales.com (CAR):** delivered a solid FY23 result and FY24 guidance update. The Australian business delivered against expectations, whilst the Trader Interactive business in the US beat expectations, demonstrating both solid execution and confirmation of potential upside risks (including new customers, new products, pricing power and margin expansion).
- Domino's Pizza Enterprises (DMP):** outperformed following its FY23 result which missed expectations but provided trading updates with positive momentum in key Australian, NZ and European markets. Asian markets remain challenging but group restructuring, and declining cost of goods sold (COGS) headwinds provides a more constructive outlook.
- James Hardie Industries (JHX):** outperformed following 1Q24 earnings, with sales, margins and guidance all beating expectations, driven by stronger volumes and lower freight costs.

Detractors

- IRESS (IRE):** underperformed following FY23 results that saw large downgrades to forward earnings expectations. As the group continues to reset the business and sell off non-core assets, we observe years of underinvestment and poor capital allocation needing to be resolved.
- Ramsay Health Care (RHC):** was softer after highlighting the impact of higher interest costs flowing into FY24 which saw material downgrades to previous expectations.
- Wesfarmers (WES, underweight):** outperformed with the group's FY23 earnings exceeding expectations and showing resilient earnings in a tougher retail background with Bunnings and Kmart continuing to drive consumers into store through value and range.

Fund and market review

The S&P/ASX 200 Total Return Index was down 0.73% during the period. Consumer Discretionary (+4.6%) was the best performing sector, following strong annual results from Wesfarmers (WES +8.5%) and Domino's Pizza Enterprises (DMP +10.1%). A-REITs (+2.3%) also outperformed, with Goodman (GMG +13.7%) reporting solidly and indicating that its industrial asset pipeline will likely support a substantial move into data centres. Utilities (-4.3%) was the worst performing sector, with AGL Energy (AGL -9.0%) unable to sustain its momentum on the back of higher electricity prices. Consumer Staples (-4.1%) also underperformed, as grocer Coles Group (COL -10.6%) underwhelmed in its annual report to shareholders, seeing a need for increased capital expenditure (capex) to return to similar levels of operational efficiency as peers.

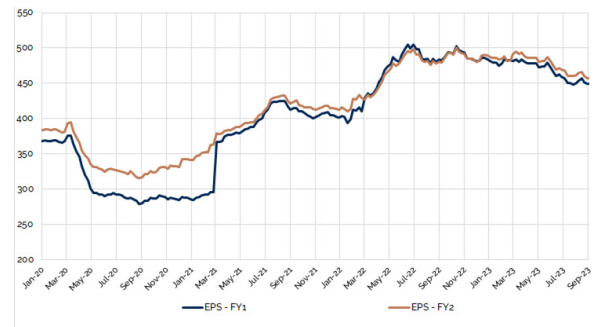
From several angles, the full year reporting season in Australia provided a uniquely important marker in the post pandemic economy. The second half of FY23 provided the cleanest set of underlying operating

results since the start of COVID-19. The direct effects of the pandemic may have receded, but the impact of government and social responses echo around the global economy in the form of inflation, associated with increasing interest rates. Many key trends have normalised in the economy, with repaired supply chain and logistic capabilities facilitating more normalised trade. However, several drivers face longer paths to restore equilibrium, most notably excess household savings and record low unemployment levels. All these factors played into reporting season results, with enterprises facing spiralling costs from labour and capital expenditures. As debt taken on during the era of ultra-low interest rates rolls into the new cost of capital reality, productivity and discipline take centre stage.

Earnings revisions

Overall, the S&P/ASX200 Index suffered modest negative earnings per share (EPS) revisions during reporting season, but remain significantly higher than pre-COVID-19 levels, despite large and dilutive capital raising during the early pandemic period.

ASX 200 Consensus EPS 1 & 2 Years Forward

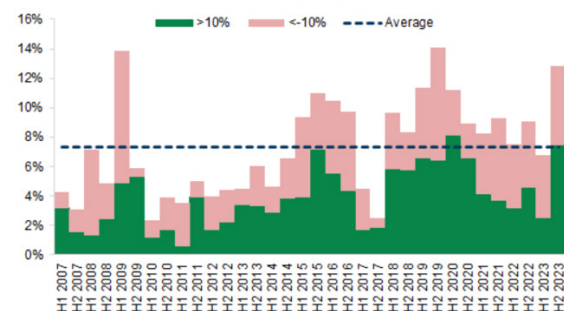


Source: DNR, FactSet

Overall, company profit results through August saw earnings (NPAT) beats outnumber misses. Materials (examining) and Communication Services saw the strongest beat rate, whilst the Consumer Staples and Information Technology saw the biggest skew towards earnings misses. The biggest surprise came from consumer stocks. Discretionary retailers noted consumer spending was slowing by less than expected, whilst staples suffered under cost and operational challenges.

The level of volatility across the portfolio and the market was particularly high during the reporting season period, with a number of outsized moves relative to the EPS revisions.

ASX 200% of Earnings Day Move >10%



Source: FactSet, Bloomberg, Goldman Sachs Global Investment Research

Earnings growth expectations were downgraded with FY24 seeing more revisions than FY23.

FY2023 consensus EPS growth

	Now	-1M	-3M	-6M
S&P/ASX 200	1.5%	2.5%	3.9%	5.0%
ENERGY	70.4%	69.5%	70.3%	74.5%
MATERIALS	-25.7%	-24.8%	-21.6%	-20.7%
INDUSTRIALS	129.1%	148.6%	144.4%	202.7%
CONS DISC	7.0%	6.6%	6.6%	5.7%
CONS STAP	4.2%	4.3%	4.3%	4.0%
HEALTH CARE	-18.2%	-12.2%	-10.3%	-7.9%
FINANCIALS	14.2%	14.3%	15.9%	17.1%
INFO TECH	48.6%	46.6%	47.6%	51.4%
COMM. SVS	1.9%	-0.1%	0.4%	2.7%
UTILITIES	54.1%	41.8%	27.5%	8.6%
REAL ESTATE	2.1%	1.4%	2.5%	3.1%

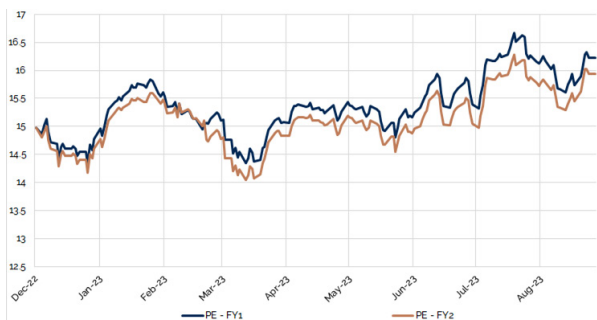
FY2024 consensus EPS growth

	Now	-1M	-3M	-6M
S&P/ASX 200	-5.7%	-0.8%	-1.7%	0.7%
ENERGY	-40.7%	-39.1%	-31.3%	-22.9%
MATERIALS	-6.6%	6.9%	-0.9%	-1.1%
INDUSTRIALS	18.7%	18.0%	18.2%	18.3%
CONS DISC	3.2%	4.0%	5.6%	6.1%
CONS STAP	1.8%	2.9%	4.1%	4.7%
HEALTH CARE	28.2%	22.0%	28.6%	25.6%
FINANCIALS	-4.1%	-3.2%	-2.6%	2.3%
INFO TECH	8.5%	11.6%	10.8%	19.3%
COMM. SVS	9.1%	11.7%	12.5%	12.1%
UTILITIES	53.0%	56.6%	63.1%	78.2%
REAL ESTATE	2.3%	4.6%	5.3%	5.0%

Source: UBS, Refinitiv

Despite this, the market continued to modestly re-rate upwards.

ASX 200 Consensus PE 1 & 2 Years Forward

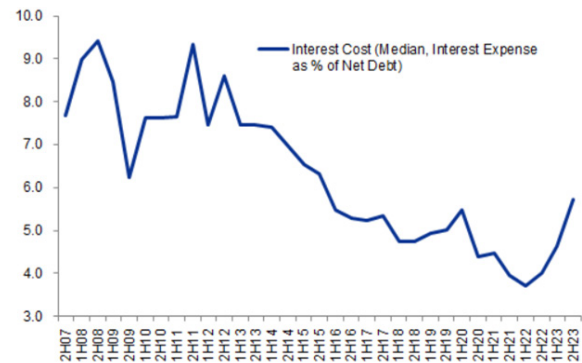


Source: DNR, FactSet

Several stocks negatively surprised the market on net interest cost. Higher debt levels and the rolling of ultra-low pandemic era interest rates places pressure on net income margins but acts with a lag.

What is clear is that interest costs have troughed, and whilst still low versus the longer run averages, the burden is set to increase.

Median ASX 200 ex-Fin Interest Expense as % of Net Debt

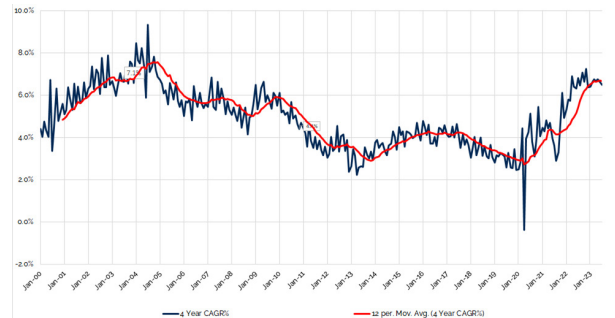


Source: FactSet, Goldman Sachs Global Investment Research

Retail still kicking (for now)

One of the more surprising takeaways from reporting season was the surprising resilience of the retail sector. ABS data continues to point to moderating year-on-year sales, but on a 4-year compound basis, sales do not reflect a consumer under severe duress.

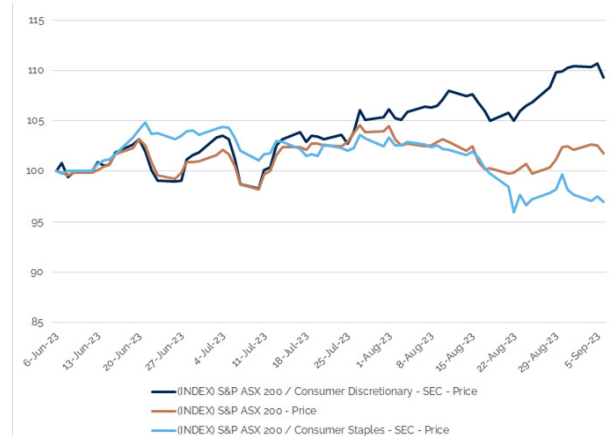
4 Yr CAGR Total (State) Total (Industry)



Source: Factset, DNR Capital

Despite headlines to the contrary, many (not all) discretionary retailers reported earnings and outlooks above market expectations. This led to the sector outperforming the market, and consumer staple stocks so far this financial year. This is potentially reflective of overcrowding in defensives names.

Discretionary vs Staples and ASX 200



Source: DNR, FactSet

There is still reason for caution with retail as ongoing cost of living pressures on consumers are compounded by increased labour expenses for retailers. Reporting season highlighted those who've proactively invested excess profits during COVID-19 into supply chain, digital capabilities and store networks, versus those who've simply harvested operating leverage during the COVID-19 induced retail boom.

Fund facts

Inception date: June 2015

Minimum initial investment: \$20,000

Risk level: High

Management fee: 0.90% (inclusive GST and RITC)

Performance fee: Nil

Entry/exit fees: Nil

Buy/sell spread: +0.20%/-0.20%

Valuation and unit pricing frequency: Each business day

Distribution frequency: Semi-Annual

Responsible Entity: The Trust Company (RE Services) Limited as part of the Perpetual Limited group of companies.

Target Market: The DNR Capital Australian Equities High Conviction Fund is an actively managed fund that offers investors exposure to a concentrated portfolio of high quality, large cap Australian listed equities. This product is likely to be appropriate for a consumer seeking capital growth to be used within an investment portfolio where the consumer has a medium or long investment timeframe, high or very high risk/return profile and needs daily access to capital.

About DNR Capital and the Fund

Concentrated: Investing in 15-30 highest conviction, quality large cap Australian listed equities.

Style neutral and quality focussed: A disciplined approach to quality and valuation. Concentrated portfolios of quality companies maximise the opportunity for outperformance.

Experienced and aligned team: The portfolio managers have more than 50 years of combined investment experience and are invested alongside our clients.

Proven process: DNR Capital was established in 2001 and a consistent firm-wide investment process has delivered more than 19 years of investment outperformance.

Disclaimer

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Office address

Level 23
307 Queen Street
Brisbane QLD 4000

Postal address

GPO Box 3263
Brisbane QLD 4001

Telephone

07 3229 5531

Email

info@dnrcapital.com.au

Website

dnrcapital.com.au