

Lazard

Select Australian Equity Fund

Oct 2021
Factsheet

High Conviction

Benchmark unconstrained, with high active share and best ideas

Disciplined 'Value' Investment Approach

Longer-term Independent thinking

Stability and Experience

Team together at Lazard for more than 19 years

Fund Facts

Number of stocks	30
Total Fund Size	\$55.4m
Inception Date	22 August 2002
Total Management Costs	W Class: 1.15% p.a.
Index	S&P/ASX 200
Minimum Investment	\$20,000
Buy/Sell Spread	0.20%/0.20%
Distributions	Quarterly ¹
APIR Code	LAZ0013AU

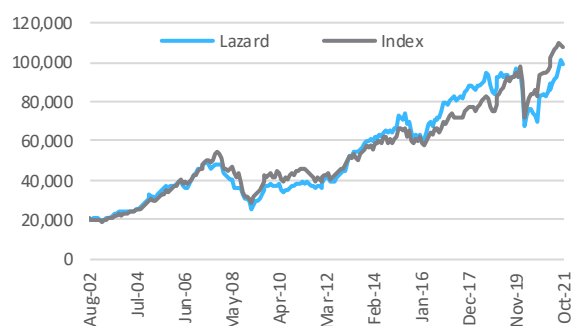
Investment Characteristics

	Lazard	Index
Price/Cash Flow	10.2	11.7
Price/Book Value	1.4	2.4
Dividend Yield (%)	3.2	3.4
Forward Price/Earnings	10.3	18.3
Active Share (%)	75.7	-
3 Year Turnover (%pa)	74.1	-

Performance² (%)

	Lazard	Index	Excess Return
1 Month	-2.7	-0.1	-2.6
3 Months	6.2	0.5	5.7
1 Year	40.6	28.0	12.6
3 Years (pa)	3.7	11.9	-8.2
5 Years (pa)	6.6	10.9	-4.3
10 Years (pa)	10.2	10.0	0.2
Since Inception (pa)	8.7	9.0	-0.3

Growth of \$20,000²



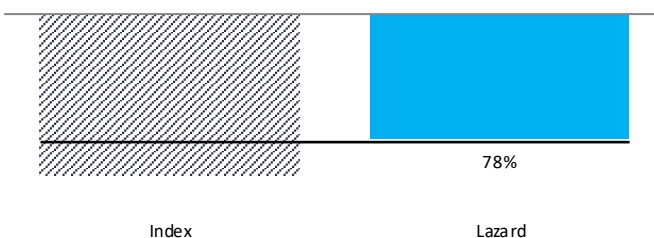
Allocations (%)

Sector	Lazard	Index	Overweight/Underweight
Communication Services	0.5	4.3	-3.8
Consumer Discretionary	3.1	8.4	-5.3
Consumer Staples	8.3	5.1	3.2
Energy	18.0	3.2	14.8
Financials	37.7	31.2	6.5
Health Care	1.1	10.5	-9.4
Industrials	10.6	7.0	3.6
Information Technology	3.8	4.7	-0.9
Materials	11.4	17.2	-5.8
Real Estate	2.0	7.0	-5.0
Utilities	3.3	1.5	1.8
Cash	0.2	0.0	0.2

Top 5 Holdings (%)

	Lazard	Index
QBE Insurance	10.3	0.8
Woodside Petroleum	7.7	1.1
Whitehaven Coal	7.3	0.1
Rio Tinto	6.5	1.6
AMP	5.8	0.2

Down Market Capture Ratio



Down Market Capture Ratio is calculated since inception and based on performance gross of all fees. Down Market capture is a statistical measure of an investment manager's overall performance in down markets, being calendar months where the Index experiences negative performance. A Down Market Capture ratio (or percentage) of less than 100 (or 100%) reflects that the manager, on average, has outperformed the Index during such down markets

¹ Distributions are made quarterly if of an economic size.

² Performance is presented net of W Class fees, please refer to www.lazardassetmanagement.com.au for performance of the I Class.

Investments can go up and down. Past performance is not necessarily indicative of future performance. Net returns are quoted after the deduction of Management Costs. Performance assumes reinvestment of all distributions.

Commentary

October 2021 showed general optimism for global equity markets, particularly the developed markets. The S&P 500 climbed 7.0% off the back of a strong U.S. earnings season and relatively low volatility. In comparison, the ASX 200 declined -0.1%, materially underperforming the global developed markets, as the Australian market lags in its pricing of higher-than-expected inflation and tighter monetary policy. This lag was significantly reflected in Australian 10-year bond yields rising 59bps to 2.08%, compared to U.S. 10-year bonds normalising after lifting 24bps in September 2021 to be flat across October 2021. Gold prices held off inflationary concerns and rose US\$26 to US\$1,769/oz, and Oil also climbed US\$6 to US\$84/bbl. Iron Ore dipped US\$3 to US\$108/Mt as China's industrial production growth moderated due to power shortages and production regulations.

During the month, the Lazard Select Australian Equity Fund returned -2.67% (net of W Class fees), underperforming the S&P/ASX 200 Accumulation Index which returned -0.10%.

Contributors to Performance

- The AMP share price rose by around 10% over October 2021, mostly as a response to the share price fall in September 2021, which was driven by selling by U.S. fund Harris Associates. The company also released Q3 2021 cashflows and a brief trading statement, which was well received on the day. This positive response wasn't so much due to great improvements, as it was due to the very low expectations in the market. The price thus returned to the lower end of the A\$1.10 to A\$1.20 range around NTA per share that it traded at over the last six months to 31 October 2021. AMP ended the month of October 2021 on a forward earnings yield of over 9% and a small discount to NTA, despite about 40% of the NTA not generating any net earnings at present. Exclusive of AMP Bank, the group trades on a about 60% of NTA, despite NTA being understated due to the book value of the China Life stake being well below market and the non-recognition of the carry and co-investment gains embedded within some AMPC funds. The focus during November 2021 will be the Investor Day on the 30 November 2021, the trustee decision and vote on the management of the AMP Wholesale Office Fund, which we assume will be lost by AMP.
- Monadelphous (MND) outperformed the broader market in October 2021 with its share price up ~10%. Whilst there was no new significant company news, other than reiteration of outlook in the release of the annual report, the share price has likely been buoyed by the gradual easing of inter-state border restrictions. As per our investment thesis, we believe the market is overly discounting MND due to its transient fall in productivity imposed by domestic border closures, as 40% of MND's WA-based workforce is typically sourced from the East Coast of Australia. MND generated A\$70m in EBIT in FY21 which would otherwise have been A\$100m under normal conditions. We believe that once domestic and international borders are fully and sustainably opened, then MND's profit margins will return to normal levels of ~5.5% EBIT margin vs. ~3.5% in FY21. The market is currently valuing MND on ~7.0x normal EBIT whereas we predict the fair value of at least 10x EBIT, based on its history.

Detractors from Performance

- Whitehaven Coal's (WHC) share price pulled back significantly in October 2021 after the stock rallied almost 300% from May 2021. During the month of October 2021, the Chinese government intervened the domestic coal market by proposing a price cap at the mine gate, restricting speculative trading activities and encouraging both state owned and private sectors to ramp up production in an effort to lower domestic energy prices and ensure security of supply for the coming winter. China imports about 200-300mtpa a year from a seaborne market of 1bntpa to satisfy coal demand in the southern provinces. These initiatives resulted in a sharp fall in the forward price for seaborne premium Newcastle (NEWC) (NAR 6,000 kcal/kg) which fell from over US\$200/t to around US\$150/t. US\$200/t thermal coal price was never a sustainable price and was reflecting an acute dislocation in supply and demand. The \$140/t is still well above our long-term coal price assumptions and reflects a very tight seaborne coal market. We continue to see WHC as attractively priced on a long-term basis with currently profitability implying on FCF yield well over 40%.
- Costa Group's shares fell 11% in October 2021, underperforming the market which rise modestly. There was little news during the month other than commentary from supermarkets on deflation in some produce categories, specifically avocados. This confirmed Costa's disappointing earnings projection for 2021 given at the AGM in May and was not new information. The market appears to be taking a 'wait and see' approach to Costa post the AGM downgrade and subsequent 2PH Farms citrus acquisition. The Fund continues to hold a position in Costa with the expectation that long-run profitability for the company is substantially above current levels.

Outlook

Looking back over the 18 months since the COVID-19 crisis hit, two major events of consequence have occurred that we believe will impact economies and financial markets in the coming years.

The first of these was the announcement of efficacious COVID-19 vaccines in November 2020. This, together with improved treatment options, should allow the eventual return of close-to 'normal' life and economic activity. While re-openings will occur intermittently as additional COVID-19 waves, new virus mutations and vaccination programs individually wax and wane, the end result seems clear, with timing being the variable up for debate. Even in this respect, locally, the 'Delta' strain out-breaks and consequent abandonment of suppression strategies and the rapid Australian vaccination roll-out over Q3 2021 have reduced the timing uncertainties.

Before COVID-19, equity markets were generally expensive with valuations dispersions between stocks and sectors at levels not seen since the TMT boom in 1999/2000. This bifurcation was pushed to record breaking levels during 2020 due to the peculiar dynamics of lockdowns. Stock market leadership and the portfolio relative performance changed from November 2020, however, coinciding with the vaccine announcements. Although there are only limited precedents, turns in market performance of the speed and size witnessed have typically continued for extended multi-year periods. While definitive market turning points are only clear in hindsight and never linear, gains for value strategies have now accumulated to significant levels and given the still prevailing distortions, our confidence has increased that the ultimately inevitable unravelling of the excess returns has commenced.

The second key development is the fully monetized fiscal stimulus undertaken by governments globally of a scale not seen since World War II. Positively, this has led to significant upgrades to economic growth forecasts and earnings expectations for stocks owned in the portfolio. What is less clear, and continues to be debated, is the potential for stimulus of this size and nature to cause inflationary pressures. While we continue to keep an open mind and assess the incoming evidence on inflation risks, given many asset prices seemingly require 'lower forever' rate expectations, any change could be a major event. To be clear, the emergence of inflation is not a forecast we make, nor that we depend on. However, we do believe that this is an increasing risk, and one that investors should be mindful of when considering broader portfolio positioning. Recent inflation outcomes across the Western nations from New Zealand to the UK, labour market indicators, commodity prices and particularly energy prices have increased the risks of an inflationary dynamic developing.

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or visit www.lazardassetmanagement.com.au

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