

# First Sentier Wholesale Concentrated Australian Share Fund



Formerly the Colonial First State Wholesale Concentrated Australian Share Fund

## Quarterly Factsheet

31 December 2022

For Adviser use only

### Portfolio Description

The Fund invests in a concentrated selection of Australian listed companies, with between 20 to 30 stocks typically held in the portfolio.

### Investment Strategy

The Fund's strategy is based on the belief that, over the medium to long term, stock prices are driven by the ability of management to generate excess returns over their cost of capital in their chosen industry. The Fund generally invests in high quality companies with strong balance sheets and earnings in the S&P/ASX 300 Accumulation Index. The Fund predominantly invests in Australian companies and therefore does not hedge currency risk.

### Investment Objective

To provide long-term capital growth by investing in a concentrated portfolio of 20-30 securities. The Fund aims to outperform the S&P/ASX 300 Accumulation Index over rolling three year periods before fees and taxes.

### Key Investment Personnel and Experience (Industry / Firm)

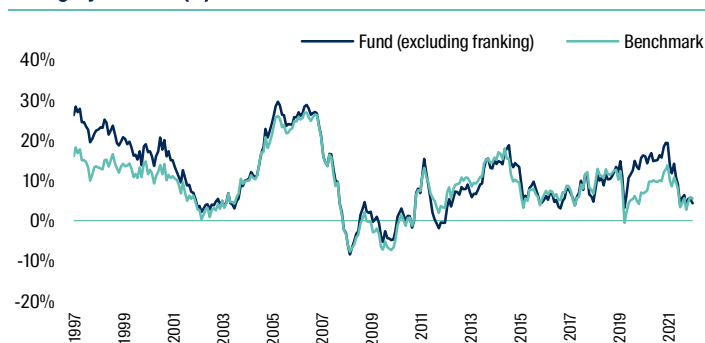
Dushko Bajic	Head of Australian Equities, Growth	(1996 / 2014)
David Wilson	Deputy Head	(1987 / 2015)
Christian Guerra	Head of Research	(1996 / 2016)

### Product Overview

APIR code	FSF0016AU
Inception date	20 December 1994
Fund Size (AS)	868 million
Benchmark	S&P/ASX 300 Accumulation Index
Number of stock holdings	28
Buy / Sell spread	0.10% / 0.10%
Minimum investment (AS)	5,000
Management fees and costs (p.a.)*	0.96%

\* Information on Management fees and costs (including estimated indirect costs) is set out in the Fund's PDS.

### Rolling 3 year return (%)



### Top 5 holdings

Stock
BHP Group
Commonwealth Bank
CSL
National Australia Bank
Woolworths

Sorted alphabetically

### Performance Summary (%)

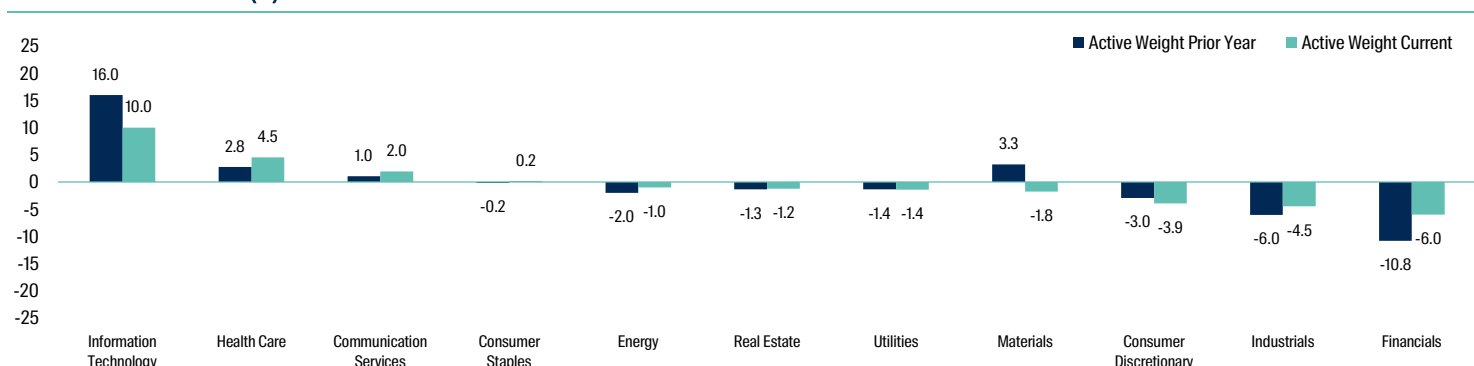
Period	3mth	1yr	3yr	5yr	7yr	10yr	SI
Net return	4.7	-16.4	4.4	7.7	7.3	9.1	11.1
Benchmark return	9.1	-1.8	5.5	7.1	8.4	8.7	9.4
Excess net return	-4.5	-14.7	-1.2	0.6	-1.1	0.3	1.7
Income return	0.4	3.2	2.4	2.5	2.7	2.9	7.4
Growth return	4.2	-19.7	2.0	5.2	4.5	6.1	3.7

### Risk Characteristics

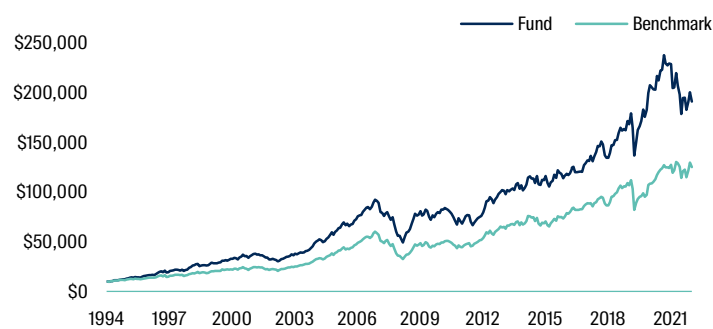
Period	1yr	3yr	5yr	7yr	10yr	SI
Fund standard deviation (%)	21.9	21.4	18.0	16.4	15.3	14.3
Benchmark standard deviation (%)	18.6	19.4	16.2	14.6	14.0	13.2
Tracking error (%)	6.6	8.3	7.0	6.3	5.9	5.1
Fund Sharpe ratio	-0.8	0.2	0.4	0.4	0.5	0.5
Information ratio	-2.2	-0.1	0.1	-0.2	0.1	0.3
Beta	1.1	1.0	1.0	1.0	1.0	1.0
Cashflow adjusted turnover (%)	19.1	29.3	35.6	43.5	51.2	

The benchmark from inception was the S&P/ASX 100 Accumulation Index, from 11 June 2013 the S&P/ASX 200 Accumulation Index, from 8 June 2020 the S&P/ASX 300 Accumulation Index.

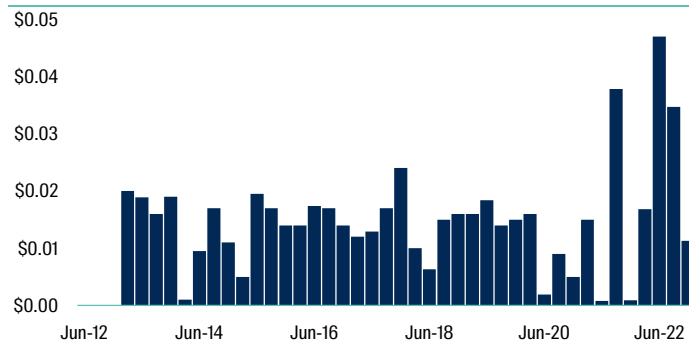
### Fund Active Sector Positions (%)



## Growth of AUD 10,000 Investment Since Inception



## Distributions



## Top 5 attributors to performance (3 months)

Sector	Attr.
Consumer Discretionary	0.71%
Real Estate	-0.02%
Financials	-0.10%
Consumer Staples	-0.16%
Energy	-0.17%

## Top 5 detractors to performance (3 months)

Sector	Attr.
Information Technology	-1.81%
Materials	-0.80%
Industrials	-0.63%
Health Care	-0.47%
Communication Services	-0.40%

Performance returns are calculated net of management fees and transaction costs. Performance returns for periods greater than one year are annualised. Past performance is not a reliable indicator of future performance.

Data source: First Sentier Investors 2022

Data as at: 31 December 2022

## Market Review

Despite facing increasing streams of mixed local and international economic data releases, varying news emanating from annual general meetings and global macro-driven volatility, Australian Equities found positive momentum in the December quarter. Market sentiment appeared to be fuelled by an increase in merger and acquisition activity and easing bond yields, encouraging a 'risk on' attitude. However, leading into quarter end Australian equities began to shift lower as bond yields returned on an upward trajectory and markets continued to be prompted to recalibrate their global outlook and growth expectations. Nonetheless, by the end of the quarter the S&P/ASX 300 Accumulation Index had risen +9.1% with all sectors posting positive gains.

The Utilities sector was a bright spot for Australian Equities in the December quarter, rallying +28.0% as all three constituents APA Group (+14.9%), AGL Energy (+18.0%) and Origin Energy (+49.3%) posted strong advances. The latter produced a standout performance following an \$18.4 billion takeover proposal from Brookfield and EIG Partners in November. Origin's Board announced they were extending the consortium's exclusive due diligence period to mid-January and maintain that the offer will be recommended to shareholders.

The ramp-up of support measures for China's under-pressure property sector and increasing civil protests in November, prompted the world's largest buyer of iron ore to begin easing its 'zero COVID' policy, evoking renewed commodity demand. Revitalised market optimism and the stronger pricing environment helped index-heavy iron ore miners Fortescue Metals Group (+21.9%), Rio Tinto (+24.7%) and BHP Group (+18.5%) produce robust returns. However, the strongest performers for the quarter were from gold miners including Capricorn Metals and Bellevue Gold delivering +53.3%, +50.7% respectively, to drive the Materials sector +14.7% higher.

Subdued sector sentiment in December resulted in negative performances from Information Technology constituents including Bravura Solutions (-28.9%), Codan (-27.7%) and EML Payments (-21.3%). However, these moves were largely offset by positive gains from Nitro Software (+37.9%), Technology One (+25.1%) and Link Administration Holdings (+24.6%) and saw the IT sector move +2.0% for the quarter.

The Consumer Staples sector was a relative underperformer in fourth quarter rising 'only' +1.7%. A2 Milk Company (+27.4%) was the strongest performer, benefiting from a number of announcements including an extension of their distribution arrangement with their partner in China and FDA approval to sell, import and distribute its products in the United States. Optimism further compounded following reports of China's gradual reopening and easing of travel restrictions, increasing the prospect of the daigou market reigniting.

## Fund Performance

The Wholesale Concentrated Share Fund underperformed its benchmark, the S&P/ASX 300 Accumulation Index, in the December quarter.

Contributing to the Fund's underperformance were overweight positions in the building materials company James Hardie (JHX) and cloud connectivity services provider Megaport (MPI). James Hardie fell -14.4% in the December quarter as investors were discouraged by a downgrade to profit guidance in their 2Q23 results update. The fibre cement company flagged a fastening deterioration in volumes seen in the last 45 days with order backlogs diminishing as a result of a weaker-than-expected construction market, change in building process whereby JHX products are used earlier and housing completions outpacing new starts. Management expect new builds to see a -30% decline in 2H23 as the US housing market slows. Whilst disappointing we were more sanguine on the result and note that JHX'S North America Fibre Cement business is only 30% exposed to the single family construction market with the greater majority 70% exposed to the residential repair & remodel (R&R) segment which is expected to be more resilient. We remain encouraged by continued strength in JHX's ColorPlus volumes (+31%) which we believe is demonstrative of the effectiveness of their strategy and recent marketing efforts. JHX's dominant market position and consistently strong price mix growth should support margins in near-term periods of volatility.

Megaport fell -19.0% given a softer first quarter trading update and broader weakness in the Information Technology sector. The market reacted poorly to MPI's trading update, focusing on: a moderate slowdown in underlying monthly recurring revenue (MRR) growth from MPI's record 4Q22; softer key metrics for new ports and customer additions; and higher capex for FY23. However, we were more optimistic on the quarterly given MPI delivered close to record metrics in 4Q22 and its September quarters have historically slowed after its June quarters, exhibiting some seasonality. Additionally, we are comfortable with the company spending moderately more on capex and working capital to fortify inventory and mitigate supply chain issues to ensure its growth runway is not hampered. We maintain our conviction in the strength of MPI's connectivity offering, with the Company's global footprint (MPI's network spans almost

800 data centres in 25 countries) a key competitive advantage. Further, the Company has built a rich, global ecosystem that is a key attraction for enterprises, data centre operators and cloud service providers (CSPs). We believe MPI has a strong, long term growth trajectory and forecast annual sales growth for MPI of over 40%.

Somewhat offsetting these negative contributions were overweight positions in the gold mining and exploration company Northern Star Resources (NST) and online travel services company Webjet (WEB). Northern Star Resources rallied +39.3% in the December quarter with positive momentum generated from stronger gold prices (+10%) as the US dollar weakened and increased market uncertainty drove investors into perceived 'safe haven' assets. Notably, earlier in the quarter the miner released a quarterly activities report and although production was slightly softer-than-expected, an optimistic outlook for the coming year was provided. We were also pleased that Management reaffirmed their production and cost guidance for FY23. A combination of operational efficiency efforts and number of growth initiatives in place such as the ramp-up of the Thunderbox mill capacity expansion should put NST in good stead to deliver strong second-half earnings growth.

Webjet advanced +29.8% in the fourth quarter, the catalyst for these gains being a product of a strong 1H23 trading update in November. All three of the travel company's businesses WebBeds, Webjet OTA and GoSee were profitable for the half resulting in the group posting \$72.5m profit, contrasting with the -\$15.9 loss made in the prior corresponding period. The result was indicative of the travel rebound underway with consumer demand being largely insulated from the effect of higher ticket prices and general rise in the cost of living. WebBeds, for example, reported booking volumes to be 13% higher than pre-pandemic levels and on track to reach pre-pandemic profitability in 2023. Over the last few years WEB has undergone a period of operational transformation to drive greater efficiency within the business through innovation such as automation, whilst leaning out their cost base and the fruits of these changes was evident in the result with expenses -16% lower than pre-pandemic. The combination of resilient travel demand, particularly as international capacity continues to unwind, and efficiency of WEB's business model should continue to drive earnings and margin growth and offset any near term macro weakness.

### Fund Activity

We continued to adjust the Fund's holdings across a variety of sectors in the December quarter.

We added to our holdings in a lithium miner over the December quarter. The company owns 25% of a high quality, long life spodumene asset in Western Australia and 49% of a lithium hydroxide downstream facility. Lithium accounts for 85% of our valuation with exposure to strong lithium pricing driven by Electric Vehicle demand. The remaining valuation is attributed to its nickel business consisting of two mines in Western Australia, with nickel sulphide another benefactor of the accelerating EV transition.

We also took the opportunity to introduce a mining services and operations company to the Fund. We were attracted to the company's diversified business divisions, consisting of two lithium mines, an iron ore business and mining services business, as well as having a strong leadership team whom we see as focused on delivery expansions within all three businesses. The miner has also recently made a gas discovery in the Perth Basin with the potential for development in the next few years.

These purchases were partially funded by our rotation out of South32 (S32) and trimming of our position in a gold miner. We exited S32 given the pricing for the miner's commodities mix has decreased over the past 6 months in particular, aluminium which has seen China increase production in a weakening demand environment. We expect this to have further adverse impacts on cash flows in the near term.

We decided to take profits from a gold miner following strong share price appreciation and redirected the money to fund other opportunities for the Fund.

### ESG Activity

The fourth quarter is typically a busy one for ESG-related issues as investors, fund managers and other financial market participants are tasked with the Australian proxy voting season. Importantly, company annual general meetings (AGMs) and accompanying meetings with boards present an opportunity to voice appraisals and/or concerns. This proxy season the AEQ Growth team voted on 63 meetings and voted against 8% of all resolutions.

Three companies held in the AEQ Growth team's portfolios received a 'strike', this identifying votes of more than 25% against the remuneration report - Goodman Group (GMG), EML Payments (EML) and Cleanaway (CWY). We supported all three remuneration reports for different reasons, explained below:

- **Goodman Group:** the overall pay potential at Goodman has been large for some time because a significant portion of equity is subject to lengthy testing and deferral for up to 10 years. While we acknowledge the large pay potential, we are pleased that the face value of the 10-year LTI awarded this year will be lower and we support the 10-year performance period in principle. This is the longest period of deferral in the Australian market.
- **EML Payments:** the company addressed many of the weaknesses in remuneration in 2022 and has committed to not using discretion to override STI and LTI hurdles in the short term. We are extremely disappointed with the sign-on grant to the new CEO and have raised this with the company.
- **Cleanaway:** we were disappointed by some of the adjustments to financials that affected bonus outcomes and raised these with the company but we were largely comfortable with the overall remuneration outcomes for the executive team.

When we have concerns on pay or governance-related issues, we typically raise these concerns in meetings with the company either ahead of the AGM or very soon after. We have found that providing clear and direct feedback in constructive conversation often leads to a commitment to addressing some, if not all, of our concerns. This is particularly the case if we have voted in support of resolutions. As part of our rigorous engagement program we will vote against resolutions if we have given the company an opportunity to address our concerns and they have failed to do so.

There was only one "Say on Climate" vote across our holdings this proxy season. This was for South32's (S32) transition plan, which we supported. The company improved its transition plan in 2022 with more ambitious emissions reduction targets, clearer scenario planning, and the disclosure of a shadow carbon price. There remains opportunities for improvement, including the need for short and medium term carbon reduction targets, which we will raise with the company in 2023.

Proxy season aside, climate-related litigation was a focus for the team in the fourth quarter. In December, Santos (STO) lost a challenge in the Federal Court of Australia related to the drilling permit for its Barossa project. The challenge succeeded because Santos's consultation with affected people before submitting the drilling plan was found to have been below the standard implied by the regulations.

Other cases we are monitoring include a challenge to Woodside's (WDS) Scarborough project by the Australian Conservation Foundation in the Federal Court and a claim by ACCR that Santos mislead or deceived the market with its 2020 transition plan and other disclosures in 2021. Both are likely to be important test cases for Australian companies generally.

### Market Outlook

In an unprecedented year of macro-driven volatility, surging inflation, oil prices and bond yields, coupled with a synchronous global tightening cycle has meant that financial market participants remain tasked with recalibrating economic growth expectations for 2023.

Economic data releases continue to demonstrate a general resilience in labour force gains, the impact of residual excess savings and consequently, consumer spending and activity. However, consumer confidence remains at recessionary levels, demonstrating signs that the impact of these headwinds is slowly but surely unfolding.

As the tightening cycle is further digested over time, high living costs and declining property and stock prices will erode household balance sheets and will ultimately restrict consumer demand and spending power. This will have a bull-whip effect on already easing supply chains demonstrated by falling global freight costs, as well as company supply-demand fundamentals including sticky costs, lower sales volumes and higher inventories which will deteriorate margins and their ability to raise prices.

With inflation decelerating as supply chain woes abate and demand is tempered, the inevitable economic slowdown is unravelling and placing company revenues and earnings under pressure. In our view, cyclical stocks will be most susceptible to the impact of this slowdown whilst high quality growth stocks will be better placed sources of earnings growth. This reinforces the need to invest in companies that have distinctive products/services that have the capacity to grow earnings and generate a strong return on invested capital.

**Portfolio Beta** measures the portfolio's sensitivity to benchmark movements. Mathematically, it is the covariance of the portfolio vs the benchmark divided by the variance of the benchmark.

**Turnover** is the average of sales and purchases divided by the average portfolio size. **Cashflow Adjusted Turnover** is the same as above, except that the lesser of sales and purchases is used in place of the average of the two. This is to adjust for turnover that is related to investing inflows or selling stocks to meet outflows rather than related to active management of the portfolio.

[www.firstsentierinvestors.com.au](http://www.firstsentierinvestors.com.au)

#### For further information

<b>Acting Head of Wholesale</b> Ross Crocker	+61 2 9010 5424	<b>Business Development Manager - VIC/TAS</b> Jack Heinz	+61 436 810 683
<b>Key Account Manager - NSW</b> Paul Sleiman	+61 4 2251 1231	<b>Business Development Associate - VIC/TAS</b> Shannen Jacobsen	+61 457 227 728
<b>Business Development Manager – NSW</b> Nicole Kremastos	+61 431 187 910	<b>Key Account Manager - QLD</b> Quin Smith	+61 455 095 505
Emerson Bloom	+61 472 633 201	<b>Business Development Manager - QLD</b> Julie Day	+61 466 413 176
Amelia McKinnon	+61 435 719 998	<b>Business Development Associate - QLD/WA/SA/NT</b> Pam Evans	+61 458 864 686
<b>Business Development Associate – NSW</b> Gabi Cheetham	+61 457 881 684	<b>Key Account Manager - WA/SA/NT</b> Nathan Robinson	+61 403 272 440
<b>Key Account Manager - VIC/TAS</b> Nicholas Everitt	+61 499 454 206		

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