

BLACKROCK HIGH CONVICTION AUSTRALIAN EQUITY FUND

BLACKROCK®

FUND UPDATE

30 September 2022

Investment Performance (%)

	1 Mth	3 Mths	YTD	1 Yr	2 Yrs pa	3 Yrs pa	5 Yrs pa	Since Incep ¹ pa
The Fund (Net of Fees)	-8.40	1.66	-29.94	-30.49	-8.44	-4.18	0.90	4.17
Benchmark ²	-9.43	-3.14	-19.25	-17.55	2.81	-0.54	4.78	6.23
Outperformance (Net of Fees)	1.03	4.81	-10.70	-12.95	-11.25	-3.64	-3.88	-2.06
S&P/ASX 300 (for comparative purposes)	-6.29	0.45	-9.98	-8.00	9.73	2.73	6.83	7.99

¹ Performance of the fund is an adjusted combination of the past performance of class X and class D to illustrate performance of the strategy since inception of the fund. It is for illustrative purposes only to show the performance of class D as if its inception date of that class was 9 December 2015. The unadjusted past performance of class D is set out [below]. Please see ² in the footnotes for further information.

² S&P/ASX300 Industrials Accumulation Ex Top 5 Stocks by Mkt Cap Gross Index

	1 Mth	3 Mths	YTD	1 Yr	2 Yrs pa	3 Yrs pa	5 Yrs pa	Since Incep pa
Class D (net of fees)	-8.40	1.66	-29.94	-30.49	-8.44	-4.18	0.90	3.47

Please see ² in the footnotes of further information.

Performance Summary – September 2022

Fund Review

“Markets stop panicking when Central Banks start panicking” – Michael Hartnett – Chief Investment Strategist Bank of America.

After a short reprieve during August when investors could assess the fundamentals of corporate Australia during earnings season, September resumed with a vengeance in terms of macro volatility.

The economy is not the market, the economy lives in the present whilst the markets attempt to live in the future. Predicting the future is never easy but our sense is the market is looking for signs of economic weakness and perhaps more importantly a rolling over of inflation so that central banks take their foot off the brakes. We saw evidence of this during the month with a weaker than expected US Manufacturing PMI that came in at 50.9 and the lowest level in two and a half years. A level below 50 shows contraction. Perversely this sent stocks rallying. The next data point was US JOLTS (job openings and labour turnover) which fell by 1.1 million which was the biggest decline since April 2020. Markets again rallied on this print. A parade of Federal Reserve members was subsequently rolled out and were all singing from the same song sheet in terms of re-iterating their commitment to continue raising interest rates in their pursuit of their inflation targets. This combined with a stronger than expected Non-farm payrolls number saw the sharp gains in September reverse abruptly.

Outside of the US we have seen several central banks start to panic. The Bank of England pivoted 180 degrees from quantitative tightening to quantitative easing and committed to buy long term Government Treasuries (Gilts) to prevent the UK Pension system from collapsing as a result of systemic margin calls that would have seen bond yields dramatically increase leading to a doom loop of further margins calls.

The Bank of Japan doubled down on their commitment to keep interest rates low which saw the Yen continue its decline as the yield differential with other currencies widens further. This resulted in the Japanese Treasury intervening in FX markets in an attempt to stabilise the Yen whose weakness is starting to import inflation into the economy. Closer to home the RBA delivered a 25bps rate hike which was lower than the 50bps hike priced in by the market. This sent equities up almost 5% on the day and short term treasuries rallied aggressively. Poland paused their rate hikes despite double digit inflation still permeating in the economy. The Federal Reserve is still talking tough on the fight against inflation yet lead indicators suggest to us the economy and inflation are rapidly decelerating and whilst we don't expect a Fed pivot as such it will simply take a slight softening of the narrative to potentially set up a large reversal for markets from deeply oversold levels with sentiment at historic lows.

We are no better at reading the macro tea leaves than the next investor and our focus still remains on finding well managed companies with strong balance sheets that get stronger during down turns and recover quickly on the other side. It is worth remembering that equity investing

Portfolio Management Team



Charles Lanchester,
Portfolio Manager



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Sam Theodore,
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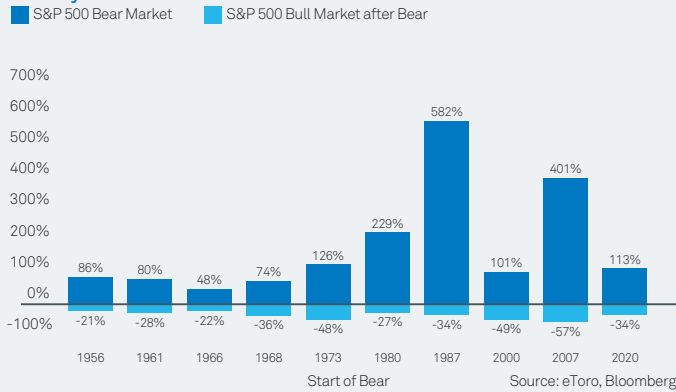
Nick Corkill,
Portfolio Manager

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- Market Insights & Commentary
- Fund Performance
- Unit Prices

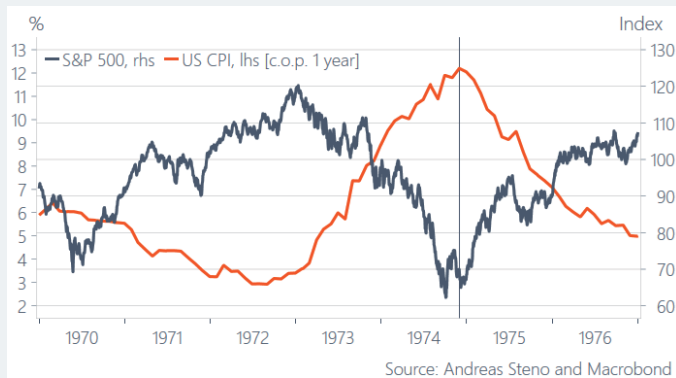
is a long-term game and that there **always is another side**. We can't predict when, but when it feels most uncomfortable it is usually a better time to put capital to work than when everything seems to be going well. Getting to the other side has been fruitful for investors historically and we have a high degree of confidence in the quality of the companies in the portfolio, many who are trading at fire sale prices.

Remembering the "other side" of bear markets throughout history.

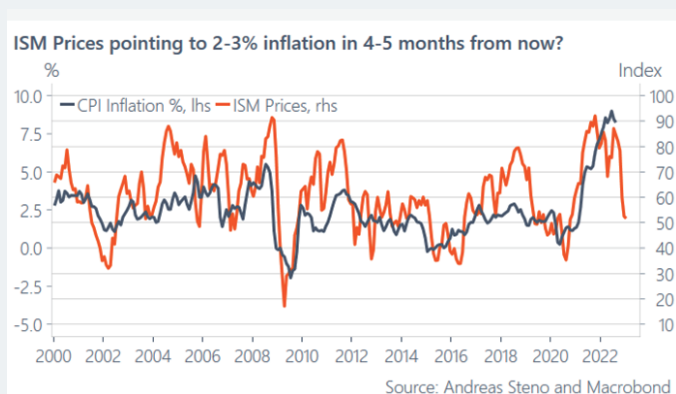
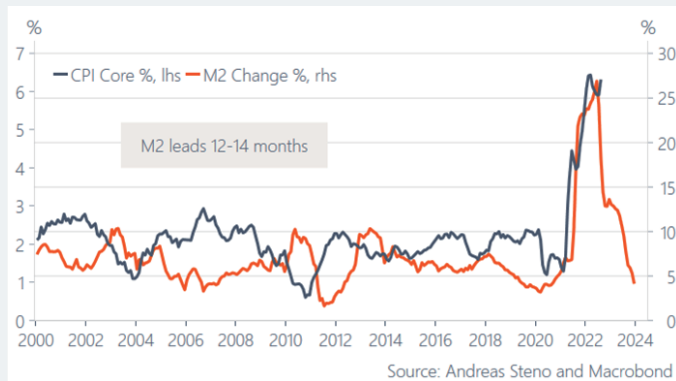


Inflation is the key – when inflation peaked in the 1970's it marked the bottom for equities.

No two periods are the same but the inflation readings over the next few months will play a significant role in determining central bank policy and the direction of markets.



On our recent webinar post reporting season (check with your relationship manager for a replay) we covered several indicators that show inflation may have peaked for now and below we have included two more charts that historically have provided a leading indication.



Fund Performance and Stock Selection

The fund returned +1.82% during the quarter, net of fees, outperforming its benchmark (ASX300 Industrials ex Top 5 Market Cap Index) return of -3.15% by 4.97%.

On a market adjusted basis, amongst the top contributors for the month were our positions in NRW Group (NWH), Peter Warren (PWR) and Austal Group (ASB) while Mass Group (MGH), Orica (ORI) and Goodman Group (GMG) were amongst the top detractors.

Contributors

PWR – Peter Warren is an Automotive Dealership group with 82 Franchise operations representing 28 OEMs. During the quarter it was disclosed that Sutton Motors had acquired the 9.4% stake of PWR owned by Quadrant private equity at a 25% PREMIUM to the latest share price. This is positive for 3 reasons:

1. It removes the overhang of private equity
2. PWR are now able to acquire Toyota Franchises including the 2 owned by the Warren Family (Toyota does not permit private equity ownership of its dealers).
3. Sutton Motors are a well-informed market participant and in our view know the assets and market place better than most ASX market participants.

In general, we have strongly believed for the past 12 months that small industrials have been dislocated from fair value by a wide margin and transactions like this, and other M&A activity we are starting to see on strengthens this view.

ASB – Austal was a top three performer during the quarter as the company was successful in securing a A\$4.7bn shipbuilding program from the US Coast Guard. The company gave guidance for FY23 of at least \$100m EBIT which was above consensus and is a transition year for the company before the steel yard ramps up in FY24 and beyond. This guidance was set when the AUD/USD exchange rate was much higher so there should be a decent buffer built in now with the AUD below 63c. The company remains attractive from a valuation stand point, has a net cash balance sheet as well as several opportunities on both shipbuilding and maintenance work going forward.

NWH – The stock was a strong performer over the quarter. We have written about the main drivers over the last 2 months – with an earnings upgrade delivered in July, and a further strong performance in August after the company delivered their result. We have been positively disposed to the contracting sector for some time now – and discussed our positive investment case in our post reporting season webinar in March. The sector generally (and NWH) was trading at very attractive multiples but were being ignored by the market in our view partly because of a perceived risk around cost inflation and ongoing Covid impacts – and hence likely margin pressure. The outlook for revenues for NWH continued to look positive – and key will be securing this work at good margin, and then delivering to expectations – but we believe we are seeing a rationale market where some of the risks are now being priced in the contractor's favour. This is part of the process we expect to see – but we do note the environment is tricky with labour shortages a real issue these companies will need to manage through.

Detractors

MGH – Mass Group delivered a result marginally above the top end of guidance. This was a solid result despite the heavy rainfall up and down the east coast which saw all the other listed construction materials companies report poor earnings. Guidance for FY23 was also 10% above consensus at \$180-\$200m EBITDA and does not include the benefit of acquisitions that could add \$22m to this number on an annual basis. The share price has continued to sell off, particularly after the Australian Bureau of Meteorology issued a La Nina warning for the third year in a row. This is extremely rare but will no doubt cause some impacts to all companies that have weather exposure. Any impacts from weather are short term with the work not disappearing but simply pushing out into subsequent weeks/months when the weather improves. The shares were cheap to begin with and by our estimates the market is capitalising poor weather into the long term which opens an attractive risk reward for investors who can look beyond the very short term

ORI – Orica underperformed following a capital raise in which the company over raised to strengthen the balance sheet during a period of considerable working capital build due to rising ammonia prices and supply chain pressures due to both covid and the war in Ukraine.

GMG – Goodman Group underperformed over the quarter caught up in the general down draft of the property sector as hawkish central banks around the world weighed on sentiment. We think that Goodman will be somewhat insulated from this difficult environment. They are in the enviable position of having very little debt within their own business. They are also focused on A grade commercial industrial properties where in many cases rental increases are in the double digits, well ahead of inflation. Goodman Group has a particular focus on last mile

delivery warehousing in the world's largest cities. This is still in high demand and is a great way to play the continuing shift towards online retail by both pure play operators like Amazon but also existing large bricks and mortar retailers. We have used this recent sell off to add to our position.

Top 10 Holdings Alphabetically

Stock
ALS LTD
ARISTOCRAT LEISURE LTD
GENERATION DEVELOPMENT GROUP LTD
GOODMAN GROUP UNITS
INSURANCE AUSTRALIA GROUP LTD
MAAS GROUP HOLDINGS LTD
PETER WARREN AUTOMOTIVE LTD
RESMED CDI INC
SUPERLOOP LTD
TREASURY WINE ESTATES LTD

Source: BlackRock

Sector Exposure

Sector	Weight %
Consumer Discretionary	17.65
Industrials	17.35
Financials	15.62
Real Estate	10.51
Health Care	9.66
Information Technology	9.26
Consumer Staples	9.20
Communication Services	6.63
Materials	1.42
Utilities	-

Source: BlackRock

About the Fund

Investment Objective

The Fund aims to deliver returns that are 4-6% (before fees) p.a. above those of the S&P/ASX 300 Industrials Accumulation Index ex top 5 stocks by market capitalisation (Benchmark) over rolling 3-year periods.

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Fund Strategy

Our investment style is based on the belief that a small team of experienced investment professionals focusing on the quality stocks in the market, will outperform over the long-term.

The Fund applies a fundamental approach that is focused on bottom up analysis, where detailed research is conducted prior to any investment decision. There is a strict focus on quality first and only those companies that meet the following quality filters will be considered for inclusion in the Fund:

- ▶ **Management:** engagement with key executives and board members to identify talented management teams.
- ▶ **Profitability:** rigorous evaluation of companies' ability to generate profits
- ▶ **Debt:** strict assessment of debt levels and the ability to service and repay debt.
- ▶ **Businesses:** superior businesses that are easy to understand.
- ▶ **Sustainability:** analysis of ESG risks and factors to identify companies well positioned to grow sustainability.

We believe that the focus on quality first adds significant outperformance, particularly in times of market dislocation, where successful investing is as much about avoiding the losses as picking the winners.

Fund Details

BlackRock High Conviction Australian Equity Fund	
APIR Code (D Class)	BLK0012AU
Fund Size/strategy Size	\$93m/\$237m
Buy/Sell Spread	0.275%/0.275%
Management Fee	0.70%
Performance Fee	15%
Liquidity	Daily

^ The BlackRock High Conviction Australian Equity Fund ("Fund") is structured to allow for different classes of units with different fee structures. The same investment strategy is applied holistically across all unit classes in the Fund. The first class of units for the Fund ("class X") was launched on 9 December 2015 with more than \$220m of assets. A second unit class ("class D") was launched for retail investors on 4 January 2016. This report is designed for class D unit holders. In order to illustrate the performance of the Fund's strategy across both classes since the official launch date of the Fund on the 9 December 2015, performance since inception quoted here is based on the period from 9 December 2015. Performance figures quoted here apply the fees charged to the class D units in order to provide class D unit holders with an estimated performance estimate over the period. This adjustment is estimated and unaudited and is for illustrative purposes only. Past performance is not a reliable indicator of future performance. Net of fees performance is calculated on exit-to-exit price basis, e.g. net of ongoing fees, performance fees and expenses.

^^ Performance figures represent past performance and are not indicative of future performance. Current performance may be higher or lower than that shown. Net performance figures are calculated after fund management fees and expenses, and assume reinvestment of distributions. Unless otherwise stated, performance for periods greater than one year is annualised and performance calculated to the last business day of the month.