Chester High Conviction Fund

Fund Update

May 2022

APIR OPS7755AU
ARSN OPS7755AU

At 31 May 2022	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a	Incep. % p.a. *
Chester High Conviction Fund (after fees)	-2.2	6.7	7.9	17.0	18.7	15.2	14.9
S&P/ASX 300 Accumulation Index	-2.8	3.1	1.0	4.7	8.0	9.0	8.2
Outperformance (after all fees)	+0.6	+3.6	+6.9	+12.3	+10.7	+6.2	+6.7

* 27 Apr 2017

"It's tough to make predictions, especially about the future."

— Yogi Berra

Month in review

Don't fight the Fed. Since the GFC the FOMC has erred on the side of being market friendly, with a dovish tilt at the first sign of economic weakness. This created the mindset of "buying the dip" any time equities were sold off more than 10-15%. Unfortunately for equity investors, the US monetary policy since the GFC has been an effective on/off switch. Most of the time, the switch has been on. It's currently turned off. We still have market expectations of another 5-6 interest rate hikes in 2022, combined with the unwinding of the QE program post the COVID inspired central bank largess, which makes for the fastest change in financial conditions in the past 40 years.

So what would see a central bank pivot? Simplistically the dual mandate of fighting inflation and maintaining full employment are the Fed's stated objectives, hence a change in momentum in either metric would suggest expectations for ongoing rate hikes would be wound back. Whilst many of the forward looking economic data points suggest pending consumer weakness ahead (confidence, forward orders), the backward looking unemployment rate remains very strong. Thus to this end, the Fed appears set to raise rates again in June and July (while the RBA is on the same path). We would truly need to see inflation peaking and the unemployment rate to start going up for this current trajectory to change course. In this sense, economic weakness again becomes good news for asset pricing. We don't profess to offer a view on the timing of either, agreeing wholeheartedly with Yogi Berra.

Many stocks that benefited from the excessive speculation post March 2020 have now wound back all of the pandemic inspired gains. We say this using the ARKK ETF as the poster child for long duration narrative driven speculation. The ARKK ETF quadrupled in 12 months from USD40.00/share to USD160/share off the March 2020 lows. It is currently trading around USD43.00. The question we ask ourselves is, "has the bubble already burst?". We are looking at screens where many stocks listed on the ASX are down more than 70% from their peak. We are trawling through these stocks as during June, the tax loss selling normally heralds the peak in capitulation. We find this a genuinely interesting time to be an investor.

As always, holding a diverse range of stocks for the uncertainty over the next 12 months appears to us to be the most prudent path in preserving capital. Whilst it appears easy to be pessimistic in the current environment, opportunities always present themselves.

Portfolio review

For the month of May the fund returned -2.2%, relative to the ASX300 Accumulation Index return of -2.8%. We hold the notion that the best prospects of protecting capital and growing earnings in a highly inflationary environment is a bar bell approach. For margins to hold, and therefore profits to hold/grow, we need to see one of two things. Either strong commodity led tailwinds (hydrocarbons, electricity etc), or extremely strong pricing power, whereby we hold the view that only a select handful of Australian stocks have true pricing power.

GQG Partners (GQG) was the strongest performing stock in May. A position we entered in March as we watched a high quality global fund manager, with strong inflows sell off over 45% from its November 21 IPO. Buying a highly cash generative business with growth momentum on less than 10x PE and a 10% dividend yield was compelling in our view. Mineral Resources (MIN) continues to be our preferred commodity exposure.

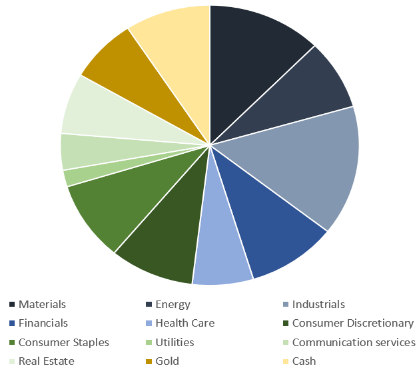
Nufarm (NUF) was sold off in May after a strong earnings release that was followed with a 15.9% equity sell-down from Sumitomo Corp, having bought the stake in 2010. This has left NUF facing an equity overhang, which has little to do with the medium term fundamentals of the business. The Nuseed platform remains compelling in our view, and remains significantly undervalued in the current corporate structure of NUF. With 31% eps upgrades to FY23 earnings since the start of the year, we are somewhat surprised by the 20% sell off since the result. But markets continue to challenge us.

Top 3 holdings
CSL Ltd
The Lottery Corp
Mineral Resources

Portfolio breakdown	
Industrials	15.0%
Materials	12.4%
Financials	9.8%

Top 3 portfolio attribution	Bottom 3 portfolio attribution
GQG Partners	Nufarm Ltd
Mineral Resources	Aurelia Metals
Stanmore Resources	News Corp Ltd

Fund weights - diverse sector exposure



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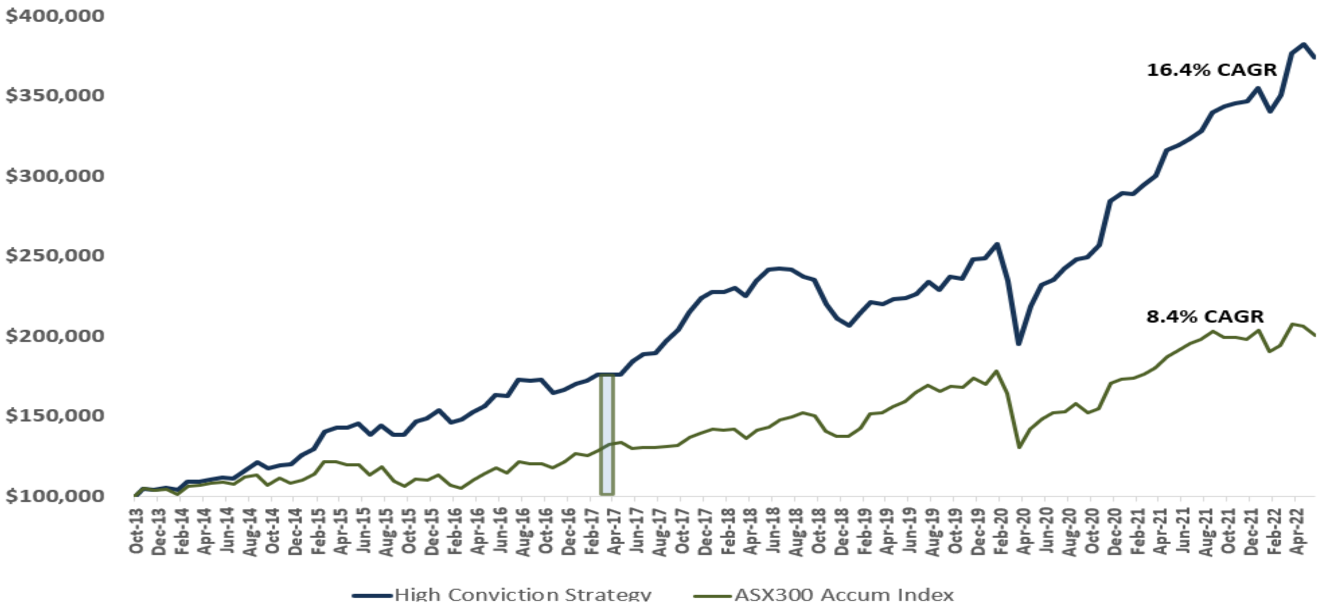
Accumulated Performance by Financial Year - Same Strategy

	FY14 (%)#	FY15 (%)	FY16 (%)	FY17 (%)*	FY18 (%)	FY19 (%)	FY20 (%)	FY21 (%)	FY22 (%)	Since Incep (%)
Same Strategy (after MER)	+11.2	+24.5	+17.4	+11.2	+28.3	-6.4	+3.9	+37.2	+15.8	+16.4
S&P/ASX 300 Accum Index	+7.8	+5.6	+0.9	+9.1	+13.2	+11.4	-7.7	+28.5	+2.4	+8.4
Value added (after MER)	+3.5	+18.9	+16.4	+2.1	+15.1	-17.8	+11.6	+8.7	+13.4	+8.0

Per Annum. The inception date of SGH Australia Plus was the 8th of October, 2013, where Rob Tucker was the sole Portfolio Manager, until his departure on February 28th, 2017.
* The inception date of the Chester High Conviction Fund was April 26th, 2017, hence FY17 reflects 8 months of SGH Australia Plus and 2 months of the CHCF.
We note this is a statement of fact of the performance achieved by the fund during the time which Rob Tucker was the sole Portfolio Manager making active decisions on the SGH Australia Plus portfolio. We note performance is the record of the firm not the individual however past performance has been constructed from publicly available unit price data. Past performance is not necessarily indicative of future performance and should not be relied upon in making investment decisions.

High Conviction Strategy - accumulated performance



Note this graph is representative only of the combination of the same Portfolio Manager running the same strategy, and would only represent actual returns for unit holders that invested money at inception of SGH Australia Plus, withdrew those funds at the end of February 2017 and then invested all those initial funds again at inception of the Chester High Conviction Fund in April 2017. Note, this depicts returns after fees.

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