

At 30 November 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)	5.2	2.6	1.0	9.0	15.0	11.1	13.7
S&P/ASX 300 Accumulation Index	6.5	5.7	3.2	4.3	6.0	8.2	8.1
Outperformance (after all fees)	-1.3	-3.1	-2.2	+4.7	+9.0	+2.9	+5.6

* 27 Apr 2017

“Anybody that doesn’t change their mind a lot is dramatically underestimating the complexity of the world that we live in”

— Jeff Bezos

Month in review

We are often reminded of the notion that the share market will cause the most amount of pain to the most amount of people, aka “the pain trade”. We wrote last month *“China has three distinct challenges ahead of it as an economic growth engine. The first is President Xi consolidating power and being overtly anti-capitalist, the second being how and when China reopens the economy from its zero-COVID policy and the third being just how challenged the growth model is with a demographic issue that isn’t going away. The prospect of China “reopening” is more than a simple binary outcome to us, given there are 102 cities with more than 1m people, hence any “reopening” will most likely be gradual and staged.”* In hindsight we realise how consensus that thinking was.

The stark turnaround in President Xi’s stance towards the West post re-election raised eyebrows, as the rhetoric became conciliatory. Perhaps recognising that without being able to sell goods manufactured in China to the West, the most stable part of the Chinese growth engine is withering. Beyond that, the rapid unwinding of COVID restrictions suggests year on year data in 2023 vs 2022 will show significant improvement from a very low base. It is not lost on us that China will have accommodative monetary policy as we start 2023, while the Western World is still tackling inflation with restrictive monetary policy. The fund was not as prepared for this outcome as this simple explanation suggests we should have been.

While we think the Jeff Bezos quote above is very relevant, and despite the ‘China pivot’ and Government support to property developers we maintain limited exposure to iron ore. This stems from a view that China’s property market faces structural challenges from a combination of oversupply, developer working capital concerns, relative price (Shanghai ~4x more expensive than Sydney on a price to income ratio!) and demographics (dramatically ageing population = bad news for property).

Perhaps most of all is the simple fact that China has been urbanising for 20 years, so does 16% of the world’s population still need to produce over 50% of the world’s steel? We remain slightly bemused by the fact that if China is reopening, then the oil price (-6%) has seen a significant divergence from the iron ore price (+23%), which suggests to us, that at the very least one underlying commodity movement is wrong.

Portfolio review

During the month the fund returned 5.2% in a relatively strong month for the ASX, with the other barbell of the market, Metals and Mining delivering 18% (BHP 22%, FMG 32%) after the Banks’ 15% return in October.

Outperformers for the month were led by Origin Energy (ORG) which was the subject of a takeover bid at AUD9/share; the 3rd but first disclosed to the market, from a combination of Brookfield Asset Management and MidOcean Energy. We had added ORG to the portfolio mid 2021 at ~80% of its book value with conviction that the assets were being underappreciated and undervalued. Although regulatory risk has the potential to alter terms of the deal, we place a high probability on the transaction completing, hence remain holders.

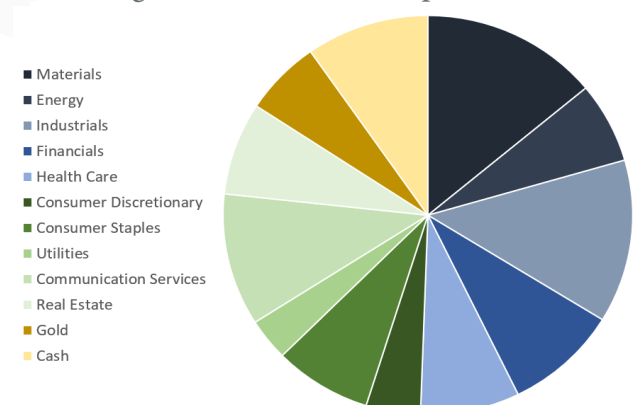
Mineral Resources (MIN) continues to offer exponential earnings growth through new projects, with a compelling gas project in the Perth Basin adding to its medium term appeal. Our gold holdings performed well throughout the month with recent addition Northern Star (NST) rising 22% during the month. Our current view is that gold equities offer meaningful upside in 2023 in a world where many companies are either fully valued or face earnings headwinds as economic conditions bite.

Jervois (JRV) was and continues to remain weak after a large USD150m equity raise to fully fund restart of Sao Miguel Paulista (SMP) nickel + cobalt refinery (Brazil), Idaho Cobalt mine restart (USA) and a study of the expansion of their Kokkola cobalt refinery (Finland). Notwithstanding its weakness we believe JRV represents one of the more reasonably priced exposures to battery materials with a highly credentialled management team and now strengthened balance sheet. Lendlease, in what has now become somewhat of a frustrating pattern delivered a further downgrade during the month. LLC now trades on <0.8x book value and ~9x FY24 earnings, on expectations that have dramatically reduced over the past 18 months. It is definitely unloved.

Top 3 holdings	Portfolio breakdown	
CSL Ltd	Industrials	13.9%
QBE Insurance Group	Materials	13.9%
Mineral Resources	Comm Services	10.5%

Top 3 portfolio attribution	Bottom 3 portfolio attribution
Origin Energy	Jervois Mining
Mineral Resources	Lend Lease Group
Northern Star Resources	Ridley Corp

Fund weights - diverse sector exposure



Accumulated Performance by Financial Year - Same Strategy

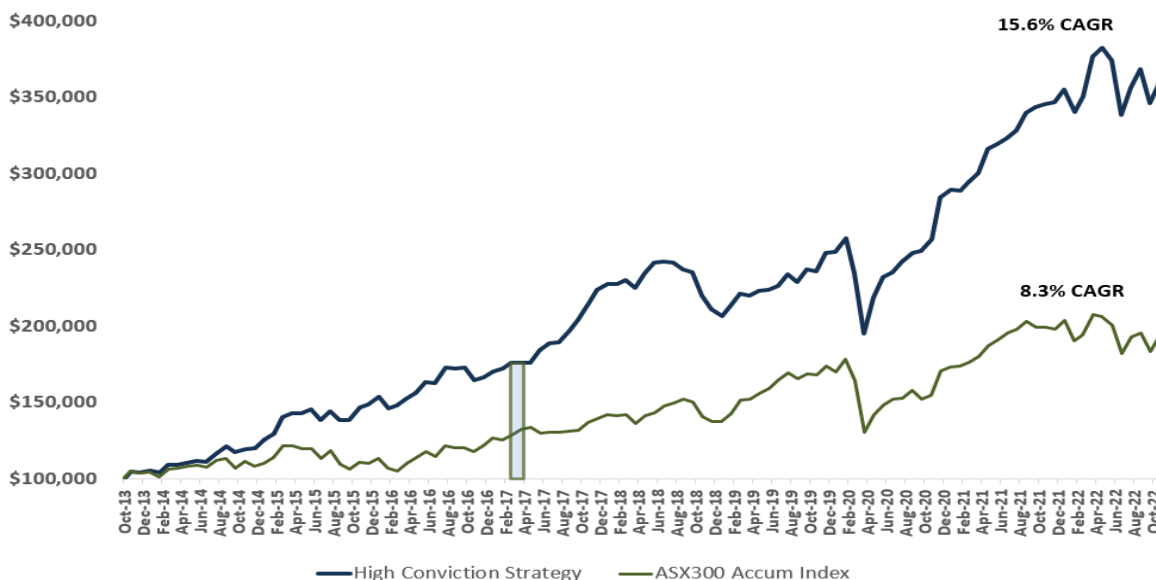
	FY14 (%) [#]	FY15 (%)	FY16 (%)	FY17 (%) [*]	FY18 (%)	FY19 (%)	FY20 (%)	FY21 (%)	FY22 (%)	FY23 (%)	Since Inc (%)
Same Strategy (after MER)	+11.2	+24.5	+17.4	+11.2	+28.3	-6.4	+3.9	+37.2	+4.8	+13.4	+15.6
S&P/ASX 300 Accum Index	+7.8	+5.6	+0.9	+9.1	+13.2	+11.4	-7.7	+28.5	-6.8	+11.8	+8.3
Value added (after MER)	+3.5	+18.9	+16.4	+2.1	+15.1	-17.8	+11.6	+8.7	+11.6	-1.6	+7.3

[#] 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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