



SG HISCOCK & COMPANY

SGH High Conviction Fund

30 November 2022

Investment objective	The Fund invests in a concentrated portfolio of Australian stocks that aims to offer long-term returns in excess of the S&P/ASX 300 Accumulation Index (after fees).		
Investments held	A portfolio of 15 to 30 stocks that are listed on the Australian Securities Exchange.		
Investment Manager	SG Hiscock & Company Limited	APIR	ETL0042AU
Commencement	28 October 2004	mFund Product Code	SHF01
Management costs¹	0.90% p.a.	Buy spread	+0.25%
Performance Fee²	15%	Sell spread	-0.25%
Minimum initial investment	\$20,000	Fund size	\$21.42 million

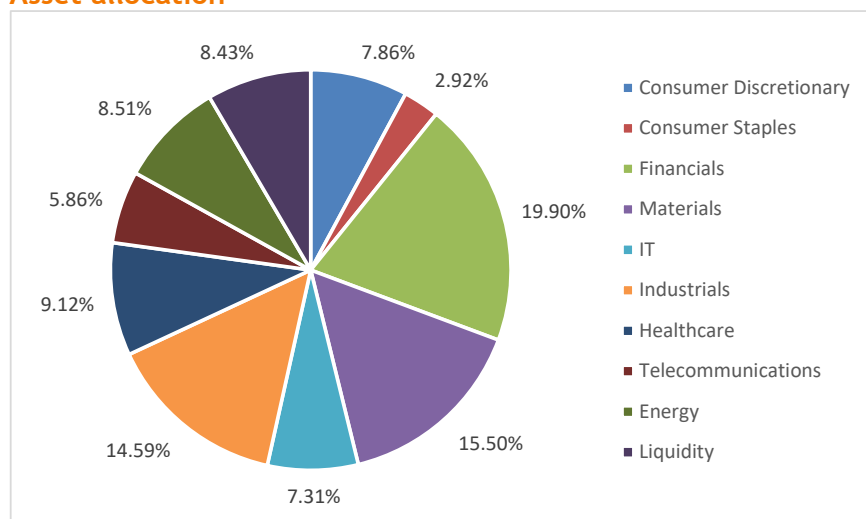
Unit Price	Application	Net Asset Value	Withdrawal
	\$ 1.5076	\$ 1.5038	\$ 1.5000

Performance ³	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	Inception % p.a.
Distribution Return	0.00	0.00	12.95	14.44	10.12	11.03	7.52
Growth Return	4.38	3.63	-10.98	-12.79	-4.16	-3.94	2.29
Total Net Return	4.38	3.63	1.97	1.65	5.96	7.09	9.81
S&P/ASX300 Accumulation Index	6.49	5.74	3.19	4.27	5.97	8.22	8.14
Total Net Return vs. the Index	-2.11	-2.11	-1.22	-2.62	-0.01	-1.13	1.66

Past performance is not a reliable indicator of future performance.

Distribution Period	31-Dec-20	30-Jun-21	31-Dec-21	30-Jun-22
Distribution rate (cents per unit)	0.7331	10.8854	3.0211	19.8711

Asset allocation



Top 5 holdings

CSL Limited
 National Australia Bank Limited
 BHP Billiton Limited
 Woodside Energy Group Ltd
 Chorus Ltd

Top 5 holdings represent 36.37% of the total Fund.

- Includes estimated GST payable, after taking into account Reduced Input Tax Credits ("RITC").
- Effective 1 December 2018, a performance fee of 15% (net GST and an estimate of RITC) of any investment return above the fund's benchmark may also be payable as an expense of the fund, subject to a highwater mark
- Performance: Distribution Return is the return due to distributions paid by the Fund, Growth Return is the return due to changes in initial capital value of the Fund, Total Net Return is the Fund return after the deduction of ongoing fees and expenses and assumes the reinvestment of all distributions.



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Monthly Observations

Equity markets resumed where they left off in October with the S&P/ASX300 Accumulation Index rallying strongly, closing up 6.5%. This was driven by risk-on sentiment on the back of expectations inflation may be close to peaking (or peaked), a shift in China's policy to property restrictions and COVID lockdowns and softening in the US dollar.

As we have seen during the course of the year sector dispersion was high during the month with utilities (+20.8%) and Metal & Mining (+18.3%) strongly outperforming and skewing performance. All other sectors struggled to keep up and underperformed the market by around 4% at best.

The large cap mining stocks rallied hard on the back of the surge in the iron price (+25.9%) with BHP (+19%), Rio Tinto (+21%), and Fortescue Metals (+27%). Base metals (Copper +8.6%, Nickel +16.9%) also rallied strongly, as did gold (+7.3%) on the weaker US Dollar Index (-5.4%).

The strength in resources was driven by the 20 optimisation measures announced mid-month by the Chinese government to ease COVID lockdown restrictions and reopen the economy in a controlled manner. Growing social unrest and slowing economic growth appear to have driven the decision. Coupled with the relaxation in the property developer financing policy restrictions announced in October, it has seen growing expectations for improving economic growth and inventory restocking.

With limited ways to directly play the China thematic through the ASX, it is unsurprising to see the pivot to resources, however this didn't spill over to the oil price which fell 12% during the month. One would expect China's reopening to be positive for oil demand (Goldman Sachs estimate by up to 1 million barrels per day), but concerns around slowing global growth seem to be crowding this out for now.

Being first in and last out of the COVID pandemic makes us believe there is ongoing opportunity for imports and consumer demand to recover in China into 2023. As the economy reopens and we have seen elsewhere, it seems not unreasonable to assume a recovery first in goods and then services. We expect there will be pent up demand for international travel and overseas students which should be supportive for portfolio holdings in Corporate Travel and IDP Education.

Despite the strong rally in markets and potential for an improvement in momentum from China reopening we continue to believe we are in the 'twilight zone' where the impact of higher rates is yet to fully be reflected broadly in slower growth and earnings.

As we have been highlighting the risk in a rising inflationary environment is investors are lulled into a false sense of confidence as sales in nominal terms continue to meet or beat expectations. If demand softens and volumes start to fall, it will be harder for companies to pass on prices and margins will come under pressure. We are also conscious that until recently many companies have still been enjoying new cycle high profit margins. There has been no urgency to cut costs, and in fact many companies have been increasing wages as they have looked to retain staff in a tight labour market.

It needs to be remembered that ultimately the intention of raising rates is to tame demand and thereby inflation. We expect the real impact will start to be felt in the first half of calendar 2023 as financial conditions start to tighten. We continue to consciously avoid more consumer discretionary businesses and those companies that were COVID beneficiaries where we have reservations about the sustainability of demand and benefits accrued.

Portfolio positioning and performance

For the month the portfolio returned 4.38% (after fees) underperforming the S&P/ASX300 Accumulation Index by -2.11%. During the month we sold out of TPG Telecom. We initially entered the stock earlier this year, but the recovery in global roaming, a key earnings driver has been slower to play out than expected. Further, the company has increased its guidance around the investment in the business and seen a material increase in its interest expense due to rising rates on its floating debt. The positive fixed cost leverage

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we originally invested for has been diluted and balance sheet become more challenging making the risk/reward less compelling. Further, the deferral of the ACCC decision on regional infrastructure sharing arrangements with Telstra, has been deferred to the end of this year with both parties likely to appeal any decision creating a headwind to performance.

We also sold out of Lendlease during the month following the company strategy update, where it downgraded its 2023 financial year guidance targets primarily due to lower than expected activity across its business and a more challenging macro outlook. Management also advised they plan to pivot the portfolio towards investing more capital in its funds management investment business over developments resulting in lower construction earnings and a lower return on equity. This will result in a lower recycling of capital and has necessitated the need to reduce the dividend payout policy. The risk is in a rising rate and slowing economic environment the recovery in earnings has been pushed out yet again and risk-reward declined. The stock looks attractively priced versus history, but we see better opportunities to deploy capital elsewhere in the current environment.

We added to our gold exposure in Northern Star (NST) on expectation that we are close, or at, the peak in US inflation and potentially peak interest rate expectations. This is should see the USD weaken from current levels and be better for gold in the months ahead.

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