

Formerly the Colonial First State Wholesale Geared Share Fund

## Quarterly Factsheet

30 June 2023

For Adviser use only

### Portfolio Description

The Fund invests in large Australian listed companies, with between 30 to 40 stocks typically held in the portfolio. The Fund utilises gearing to magnify returns from underlying investments.

### Investment Strategy

We believe stronger returns are achieved by investing in growing companies that generate consistent returns and reinvest above their cost of capital. In-depth industry, stock and valuation analysis is the foundation of our process. The Fund predominantly invests in quality Australian companies with strong balance sheets, earnings growth and high/improving returns on invested capital. The Fund utilises gearing to magnify investment returns.

### Investment Objective

To magnify long-term returns from capital growth by borrowing to invest in large Australian companies. The Fund aims to outperform the S&P/ASX 100 Accumulation Index over rolling 7-year periods before fees/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)

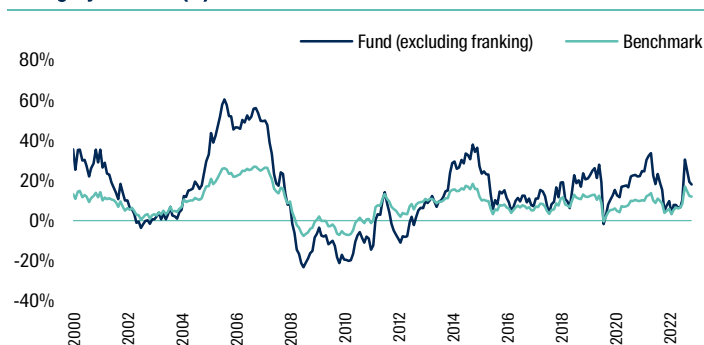
### Product Overview

APIR code	FSF0043AU
Inception date	15 August 1997
Fund Size (AS)	7,986 million
Benchmark	S&P/ASX 100 Accumulation Index
Number of stock holdings	36
Buy / Sell spread*	0.20 - 0.50% / 0.20 - 0.50%
Minimum investment (AS)	5,000
Management fees and costs (p.a.)*	1.03% (g) 2.15% (n)

\* Buy/sell spreads depend on the specific gearing level of the option.

\* 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 (%)

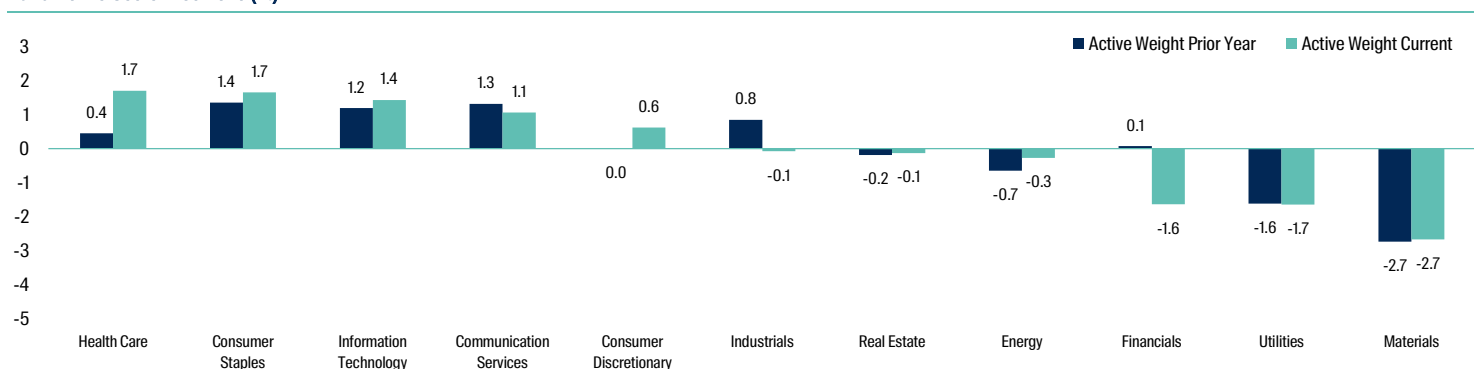
Period	3mth	1yr	3yr	5yr	7yr	10yr	SI
Net return	1.5	26.0	18.0	11.1	15.5	14.9	13.9
Benchmark return	1.2	15.1	11.9	7.8	9.3	8.8	8.6
Excess net return	0.3	10.9	6.2	3.3	6.2	6.1	5.3
Income return	4.5	5.7	17.1	14.4	15.7	13.9	9.3
Growth return	-3.0	20.4	0.9	-3.3	-0.2	1.0	4.6

Past performance is not a reliable indicator of future performance.

### Risk Characteristics

Period	1yr	3yr	5yr	7yr	10yr	SI
Fund standard deviation (%)	30.8	29.8	34.1	30.6	29.6	28.4
Benchmark standard deviation (%)	13.8	13.2	16.0	14.2	13.7	13.3
Tracking error (%)	17.3	17.5	18.8	17.0	16.6	16.2
Fund Sharpe ratio	0.8	0.6	0.3	0.5	0.4	0.3
Information ratio	0.6	0.4	0.2	0.4	0.4	0.3
Beta	2.2	2.2	2.1	2.1	2.1	2.0

### Fund Active Sector Positions (%)



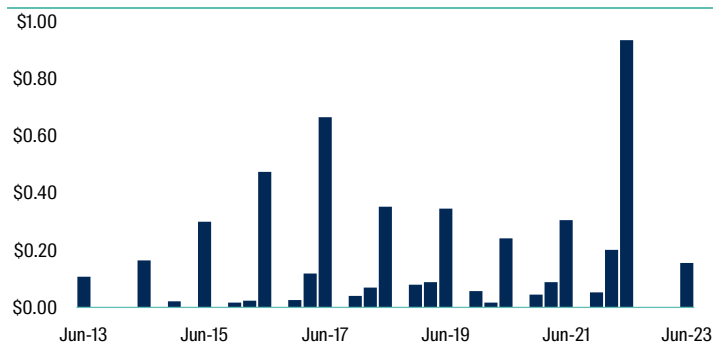
**Portfolio Beta** measures the portfolio's sensitivity to benchmark movements. Mathematically, it is the covariance of the portfolio vs the benchmark divided by the variance of the benchmark.

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 2023 Data as at: 30 June 2023

**Growth of AUD 10,000 Investment Since Inception**



**Distributions**



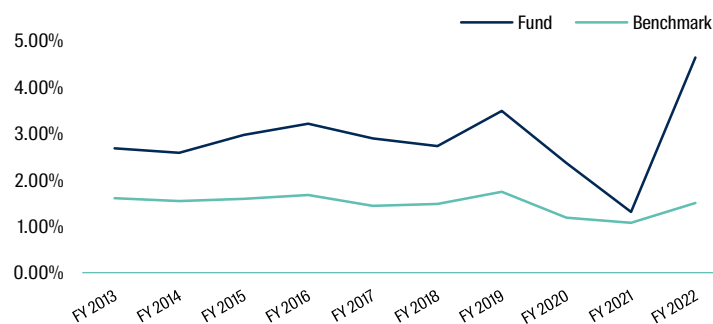
**Top 5 attributors to ungeared performance (3 months)**

Sector	Attr.
Information Technology	0.40%
Materials	0.28%
Energy	0.13%
Real Estate	0.07%
Communication Services	0.06%

**Top 5 detractors to ungeared performance (3 months)**

Sector	Attr.
Financials	-0.21%
Industrials	-0.19%
Utilities	-0.07%
Consumer Discretionary	-0.05%
Consumer Staples	-0.02%

**Franking Credit Return (%) by Financial Year**



**Market Review**

Australian equities finished the June quarter and financial year positively with a respective +1.2% and +15.1% gain, albeit masking the underlying volatility experienced by investors. Market movements in the S&P ASX 100 Accumulation Index over the quarter were dictated by a combination of domestic and international company announcements including a disappointing reporting season from the major banks in May, continuing bouts of mixed economic data, and persisting hopes that the global interest rate tightening cycle might be nearing its end.

The Information Technology sector was a bright spot for the market, surging +21.0% as investors embraced a preference for companies better positioned to deliver earnings growth in light of the growing risk of a slowing economy. Positive trading updates by Xero (+33.0%) and NextDC (+21.4%) further bolstered the sector, with the former producing one of the strongest performance for the index. The sector has risen by over 40% over the past 12 months, consistent with strong moves in technology-related stocks overseas.

A stronger performance from AGL Energy (+34.3%) bolstered the Utilities sector (+5.5%) in the June quarter, offsetting softer contributions from Origin Energy (+1.4%) and APA Group (-1.4%). Investors embraced a favourable trading update with AGL management indicating that gross earnings for FY23 is expected to be at the upper end of its previous guidance between \$1.33bn and \$1.38bn.

Health Care stocks Ramsay Health Care (-15.4%), Fisher & Paykel Healthcare (-8.3%) and CSL (-3.8%) all struggled and dragged the sector -3.6% lower. Index heavyweight CSL was the greatest detractor, losing ground after the management team announced that full year net profits will be adversely affected by stronger-than-expected foreign exchange headwinds. Profit guidance for 2024 also fell short of market expectations.

Economic indicators in China pointed towards a potential moderation for bulk commodities, limiting gains within the Materials sector (-2.0%) in the June quarter. Whilst the outlook started to improve in June, given reports that China may be preparing policy changes and fiscal stimulus plans to support demand, mining constituents including BHP (-4.7%), South32 (-14.0%) and Rio Tinto (-4.5%) succumbed to downward pressure.

**Fund Performance**

The Wholesale Geared Share Fund outperformed its benchmark, the S&P/ASX 100 Accumulation Index, in the June quarter and continues to deliver attractive levels of excess returns over longer periods as our be-spoke fundamental research process allows us to identify high quality, growth stocks that we believe will generate superior returns for our investors over time.

Contributing to the Fund's outperformance were the overweight positions in the building materials company James Hardie (JHX) and cloud accounting services provider Xero (XRO). James Hardie surged +24.9% in the June quarter with investors particularly pleased with the Company's FY23 result released in May. The result was largely in line with expectations with JHX's producing a FY23 adjusted net income of US\$605.5m which aligned with its guidance of US\$600-620m. We and the market were pleased to see evidence of JHX's margin performance improving, with the Company reporting better margins in every region in 4Q23 compared with 3Q23 with JHX's North America and APAC margin notably improving to 29.0% and 28.9% from 27.0% and 24.7% respectively. Another key takeout was that JHX's margin outlook appears strong, with the Company's guide for 1Q24 well above market expectations and reflective of the business' ability to increase prices in its less cost sensitive areas such as R&R through ColourPlus as well as JHX's ability to vary and control

its variable costs. While JHX remains cautious on the near term outlook, it nonetheless believes it can hold margins above 25%. Looking forward, we believe we are nearing the bottom in end-market demand across JHX's key exposures.

Xero rallied +33.0% higher with positive momentum stemming from a robust FY23 result (March Year End) that surpassed consensus expectations. A key highlight was the strong top line growth with revenue increasing +28% YoY supported by solid subscriber growth (+14% to 3.74m) and 10% lift in average revenue per user (ARPU). ARPU was supported by price increases, upgrades and strong uptake of platform adjacent products such as payroll and payments. Despite macro challenges faced in the past year, average monthly churn remains low at 0.9%, a testament to the sticky and vital services XRO provides and pleasingly, free cash flow also rose from FY21 NZ\$2m to FY22 NZ\$102m. We are of the belief that the new CEO's focus on profitability and disciplined cost controls are evident in XRO's target for operating expenses to fall from 82% to 75% of revenue in FY24 supporting further margin expansion, higher profits and greater free cash flow.

Somewhat offsetting these positive contributions was the Fund's zero-weight position in the major bank Australia and New Zealand Bank (ANZ) and overweight position in international education services company IDP Education (IEL). Australia and New Zealand Bank rose +7.0% in the quarter, outperforming the broader market. The major bank released its 1H23 result in May, presenting a 12% increase in cash profit compared to 2H22. ANZ's net interest margin (NIM) increased by 7bps to 175bps however, similar to its peers, the Company indicated that the benefits of higher interest rates was decelerating as deposit and mortgage loan competition intensifies. Investors were generally pleased with the proposed fully franked interim dividend of 81c (+9.5%). Later in the quarter, ANZ announced an agreement with the Queensland government as part of its proposal to acquire Suncorp Bank. The jobs and investment agreement promises to establish a 'tech hub' in Brisbane subject to the completion of the acquisition, following required approvals from the Australian Competition and Consumer Commission (ACCC) & Federal Treasurer.

IDP Education (-19.1%) underperformed in the quarter given an announcement that beginning in August 2023, the Immigration, Refugees and Citizenship Canada (IRCC) was granting approval for other English language proficiency providers for its Student Direct Stream (SDS). Prior to the decision, IEL's IELTS was the only test recognised for Canada's SDS however, the Company has since confirmed that they do not expect a material impact on FY23 earnings. Whilst this may see competition increase for IEL's IELTS business, the IELTS business continues to grow in other geographic locations including Australia, UK, Vietnam etc. Additionally, the Student Placement business is seeing volumes ramp-up across its major destinations. We remain attracted to IEL as we believe it is a high-quality business with a strong future growth runway – both in their market leading English-language testing business and their Student Placement business, which offers the most diverse sourcing network in the world.

#### Fund Activity

Over the June quarter we took an initial position in an insurance and banking organisation as we are now seeing insurance premiums rising faster than claims expenses which should benefit the Company. We were also attracted to the stock as its margins are also benefitting from the higher yields it is receiving on its large fixed income portfolio.

We also took the opportunity to increase the Fund's exposure to an insurance broking business. The Company continues to benefit from double-digit increases in Australian insurance premiums. This was most recently demonstrated by the Financial constituent's largest underwriter which reported a +11.3% increase in Australian premiums in the March quarter, an acceleration from the +9.9% achieved in the December 2022 half.

We exited our position in Cleanaway (CWY) as we have concerns about CWY's return on capital prospects in the near-to medium-term. CWY is progressing through a strategy that is highly capital-intensive and coupled with higher financing costs, we are cautious on the returns that these investments could generate in the near-term, and will re-evaluate the stock in the future.

We also exited our position in the flat steel producer Bluescope (BSL) as we saw a peaking in US steel spreads, which have fallen from \$700/t in early March to the current US\$415/t.

#### ESG Activity

The Australian Growth Equities team researched two ESG thematics during the quarter – corporate Australia's approach to traditional owner relationships and free prior and informed consent (FPIC), and the risks associated with carbon offsets and their place in transition plans. There is little research on both areas in an Australian context and FPIC in particular has the potential to materially impact miners and energy companies.

Carbon offsets have become controversial because of whistleblower claims that some offset projects are fraudulent or ineffective, with actual emissions from some projects (particularly forestry) being smaller than claimed. At the same time, companies have been turning to offsets to meet their voluntary or compulsory emissions reduction requirements. Some companies are relying on offsets to reduce emissions in the short term. Our preference is for companies to physically reduce as many emissions as they can, with offsets bought as a last resort for emissions that are hard to abate.

Australia's two largest oil and gas producers, Woodside Energy Group (WDS) and Santos (STO), held their annual general meetings during the quarter and both were controversial because of their growth plans. We voted against the re-election of Ian Macfarlane to the Woodside board but supported all other resolutions at Santos and Woodside. Our vote against Macfarlane was driven by our disappointment with Woodside's transition plan and the Company's reluctance to meaningfully address weaknesses in the plan, particularly its approach to Scope 3 emissions. We also identified weaknesses in both companies' approach to executive pay and encouraged them to address these.

We held meetings with Woodside and Santos' chairmen and climate teams during the quarter, along with meetings specifically on ESG with the four major banks, BHP Group (BHP), Rio Tinto (RIO), Endeavour Group (EDV) and Cleanaway (CWY).

We also progressed our collaborative engagement with JB Hi-Fi (JBH) on modern slavery and participated in a Climate Action 100+ meeting with Qantas (QAN).

#### Market Outlook

Although showing more cracks in its armour, inflation remains a challenge for global central banks. Services inflation in particular, continues to run hot as local housing prices begin to lift, rents increase in line with tight supply and increasing migration, and consumers continue to prioritise travel over other forms of discretionary spending supported by pent-up COVID savings buffers. As a result the market is coming to the conclusion that restrictive monetary policy will be required for longer.

Despite near-term earnings expectations decreasing, price to earnings multiples have increased over the last few months, largely driving year-to-date market gains and reflecting the market's focus on finding companies that offer long-term growth opportunities. This has also been evidenced by a recent reversal of style leadership with the MSCI Australia Growth Index outperforming its value counterpart in the calendar year to date. This is in contrast to 2022 where value stocks benefited from the economic recovery and associated rapidly rising interest rate environment. As the market landscape evolves to be centred on the

gradual global economic slowdown, investors such as ourselves are looking for high quality, market-leading companies with distinctive products/services and strong structural tailwinds that will be better placed to navigate the uncertainties of the future.

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

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