

Formerly the Colonial First State Wholesale Imputation Fund

## Quarterly Factsheet

31 December 2022

For Adviser use only

### Portfolio Description

The Fund invests in a broad selection of Australian listed companies, with between 30 to 40 stocks typically held in the portfolio. The Fund targets longer-term tax effective income growth over near term yield by favouring companies that can sustain long term dividend growth by reinvesting capital at high returns.

### 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.

### Investment Objective

To combine long-term capital growth with tax-effective income by targeting Australian growth companies with highly franked dividends. The Fund aims to outperform the S&P/ASX 300 Accumulation Index over rolling 3-year periods before fees/taxes.

### Key Investment Personnel and Experience (Industry / Firm)

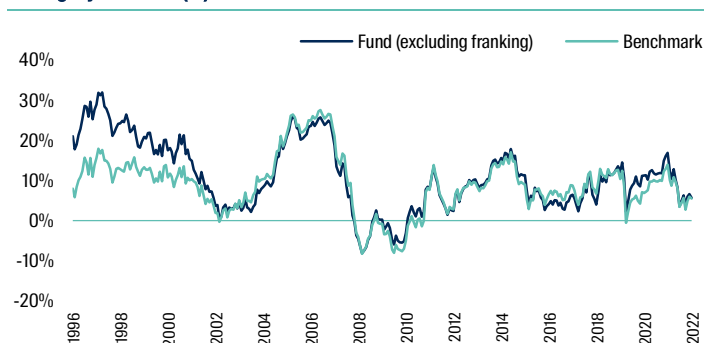
|                  |                                     |               |
|------------------|-------------------------------------|---------------|
| Dushko Bajic     | Head of Australian Equities, Growth | (1996 / 2014) |
| David Wilson     | Deputy Head                         | (1987 / 2015) |
| Christian Guerra | Head of Research                    | (1996 / 2016) |
| Jason Lye        | Portfolio Manager                   | (1996 / 1996) |

### Product Overview

|                                   |                                |
|-----------------------------------|--------------------------------|
| APIR code                         | FSF0003AU                      |
| Inception date                    | 31 December 1993               |
| Fund Size (A\$)                   | 971 million                    |
| Benchmark                         | S&P/ASX 300 Accumulation Index |
| Number of stock holdings          | 36                             |
| Buy / Sell spread                 | 0.20% / 0.20%                  |
| Minimum investment (A\$)          | 5,000                          |
| Management fees and costs (p.a.)* | 0.96%                          |

\* 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 |
| Woodside Petroleum      |

Sorted alphabetically

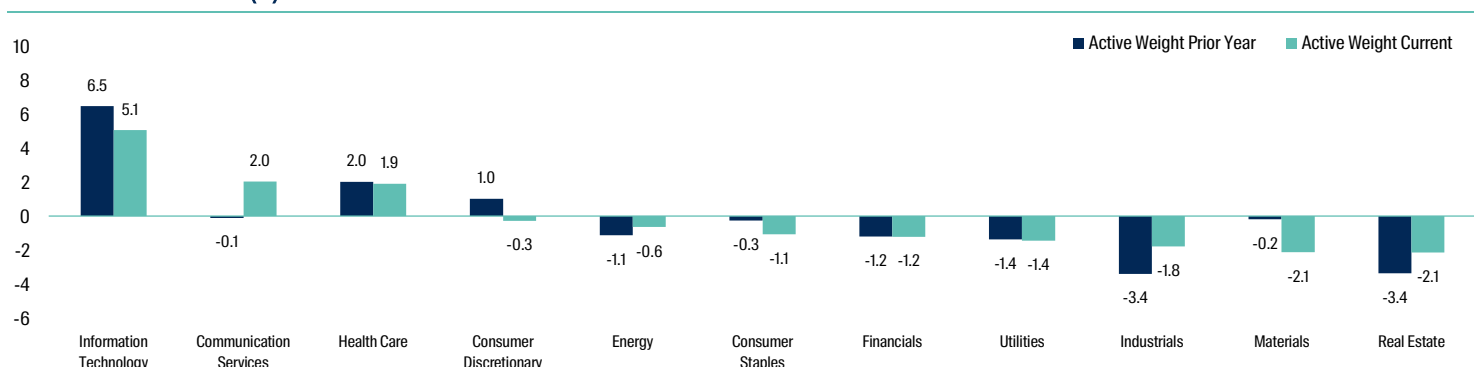
### Performance Summary (%)

| Period            | 3mth | 1yr   | 3yr  | 5yr  | 7yr  | 10yr | SI   |
|-------------------|------|-------|------|------|------|------|------|
| Net return        | 7.2  | -7.2  | 5.7  | 8.2  | 7.6  | 8.7  | 10.6 |
| Benchmark return  | 9.1  | -1.8  | 5.5  | 7.1  | 8.4  | 8.6  | 8.5  |
| Excess net return | -1.9 | -5.4  | 0.2  | 1.1  | -0.9 | 0.1  | 2.2  |
| Income return     | 1.5  | 12.8  | 11.0 | 10.2 | 10.8 | 9.5  | 8.1  |
| Growth return     | 5.7  | -19.9 | -5.3 | -2.0 | -3.2 | -0.8 | 2.5  |

### Risk Characteristics

| Period                           | 1yr  | 3yr  | 5yr  | 7yr  | 10yr | SI   |
|----------------------------------|------|------|------|------|------|------|
| Fund standard deviation (%)      | 19.9 | 19.5 | 16.8 | 15.2 | 14.4 | 13.4 |
| Benchmark standard deviation (%) | 18.6 | 19.5 | 16.3 | 14.7 | 14.0 | 13.3 |
| Tracking error (%)               | 3.5  | 4.0  | 3.8  | 3.7  | 3.3  | 3.6  |
| Fund Sharpe ratio                | -0.4 | 0.3  | 0.4  | 0.4  | 0.5  | 0.5  |
| Information ratio                | -1.6 | 0.0  | 0.3  | -0.2 | 0.0  | 0.6  |
| Beta                             | 1.1  | 1.0  | 1.0  | 1.0  | 1.0  | 1.0  |
| Cashflow adjusted turnover (%)   | 37.5 | 37.1 | 38.9 | 43.7 | 37.8 |      |

### Fund Active Sector Positions (%)

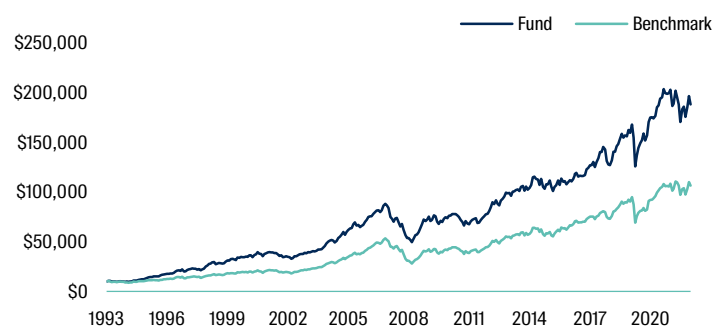


**Portfolio Beta** measures the portfolio's sensitivity to benchmark movements. Mathematically, it is the covariance of the portfolio vs the benchmark divided by the variance of the benchmark.

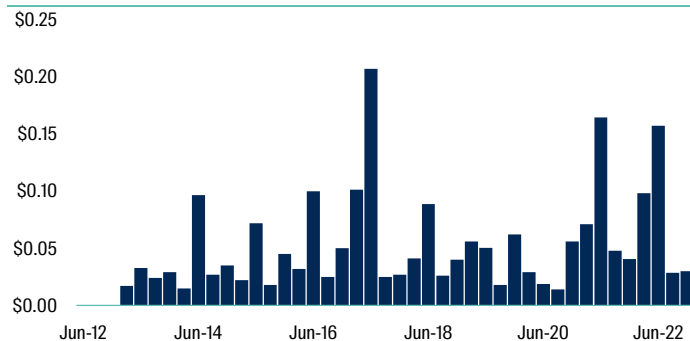
**Turnover** is the average of sales and purchases divided by the average portfolio size. **Cashflow Adjusted Turnover** is the same as above, except that the lesser of sales and purchases is used in place of the average of the two. This is to adjust for turnover that is related to investing inflows or selling stocks to meet outflows rather than related to active management of the portfolio.

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 2022, Data as at: 31 December 2022

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



**Distributions**



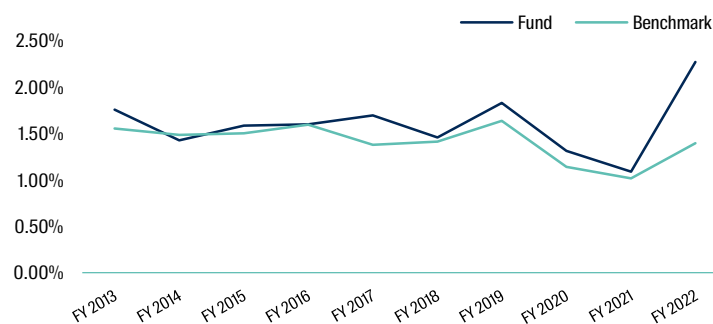
**Top 5 attributors to performance (3 months)**

| Sector                 | Attr.  |
|------------------------|--------|
| Consumer Discretionary | 0.52%  |
| Energy                 | 0.34%  |
| Materials              | 0.07%  |
| Financials             | 0.03%  |
| Consumer Staples       | -0.02% |

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

| Sector                 | Attr.  |
|------------------------|--------|
| Information Technology | -0.84% |
| Health Care            | -0.51% |
| Industrials            | -0.41% |
| Communication Services | -0.32% |
| Utilities              | -0.23% |

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



**Market Review**

Despite facing increasing streams of mixed local and international economic data releases, varying news emanating from annual general meetings and global macro-driven volatility, Australian Equities found positive momentum in the December quarter. Market sentiment appeared to be fuelled by an increase in merger and acquisition activity and easing bond yields, encouraging a 'risk on' attitude. However, leading into quarter end Australian equities began to shift lower as bond yields returned on an upward trajectory and markets continued to be prompted to recalibrate their global outlook and growth expectations. Nonetheless, by the end of the quarter the S&P/ASX 300 Accumulation Index had risen +9.1% with all sectors posting positive gains.

The Utilities sector was a bright spot for Australian Equities in the December quarter, rallying +28.0% as all three constituents APA Group (+14.9%), AGL Energy (+18.0%) and Origin Energy (+49.3%) posted strong advances. The latter produced a standout performance following an \$18.4 billion takeover proposal from Brookfield and EIG Partners in November. Origin's Board announced they were extending the consortium's exclusive due diligence period to mid-January and maintain that the offer will be recommended to shareholders.

The ramp-up of support measures for China's under-pressure property sector and increasing civil protests in November, prompted the world's largest buyer of iron ore to begin easing its 'zero COVID' policy, evoking renewed commodity demand. Revitalised market optimism and the stronger pricing environment helped index-heavy iron ore miners Fortescue Metals Group (+21.9%), Rio Tinto (+24.7%) and BHP Group (+18.5%) produce robust returns. However, the strongest performers for the quarter were from gold miners including Capricorn Metals and Bellevue Gold delivering +53.3%, +50.7% respectively, to drive the Materials sector +14.7% higher.

Subdued sector sentiment in December resulted in negative performances from Information Technology constituents including Bravura Solutions (-28.9%), Codan (-27.7%) and EML Payments (-21.3%). However, these moves were largely offset by positive gains from Nitro Software (+37.9%), Technology One (+25.1%) and Link Administration Holdings (+24.6%) and saw the IT sector move +2.0% for the quarter.

The Consumer Staples sector was a relative underperformer in fourth quarter rising 'only' +1.7%. A2 Milk Company (+27.4%) was the strongest performer, benefiting from a number of announcements including an extension of their distribution arrangement with their partner in China and FDA approval to sell, import and distribute its products in the United States. Optimism further compounded following reports of China's gradual reopening and easing of travel restrictions, increasing the prospect of the daigou market reigniting.

**Fund Performance**

The Wholesale Imputation Share Fund underperformed its benchmark, the S&P/ASX 300 Accumulation Index, in the December quarter but 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 underperformance were the overweight positions in the essential human services provider APM Human Services (APM) and medical device company ResMed (RMD). APM Human Services (-19.6%) underperformed in the December quarter following concerns regarding FY23 earnings forecasts given the slower-than-expected ramp up of the UK restart employment programme and higher borrowing costs following recent interest rate rises. We remain attracted to APM's strong growth pipeline within their core divisions with many of the government programmes such as Workforce

Australia, in their early phases of multi-year opportunities, as well as continued investment and development in other growth areas including Allied health and their Disability and Aged Care Support Services business. We are of the view that APM faces a number of tailwinds in the medium term including benefit from 15,550 Disability Employment Services (DES) participants being relocated from underperforming service providers, as new Workforce Australia and Canadian contracts ramp up and recent acquisitions including Equus and Everyday Independence make contributions. Therefore, APM's strong organic and inorganic growth coupled with accelerating scale as the constituent expands within existing and new geographical markets should bolster profit growth in 2H23 and FY24.

ResMed moved -8.3% lower off the back of a mixed first-quarter trading update released in October. We were encouraged by evidence of increased device availability given the innovation of RMD's AirSense 10 Card-to-Cloud (CTC) device which eliminated the need for 4G semiconductor chips, a key production bottleneck over the last few years. This increased availability translated into a strong +23% YoY increase in the Americas device sales over the quarter however, there was a notable contraction of device sales for RMD's rest of the world (ROW) locations (-18%). Lower adoption of the CTC devices in ROW can be attributed to the current incentive structures in countries such as France and Japan which are tailored for connected devices only, in comparison to the United States. Whilst disappointing, Management noted that supply chain complexities have been steadily easing and there will be sequential improvement and consistency of chip availability over the next year to supply demand. Easing freight and logistic costs and excess demand given competitor Phillip's absence from the market also remain as significant tailwinds for RMD and are expected to bolster strong top-line growth.

Somewhat offsetting these negative contributions were overweight positions in the gold mining and exploration company Northern Star Resources (NST) and online travel services company Webjet (WEB). Northern Star Resources rallied +39.3% in the December quarter with positive momentum generated from stronger gold prices (+10%) as the US dollar weakened and increased market uncertainty drove investors into perceived 'safe haven' assets. Notably, earlier in the quarter the miner released a quarterly activities report and although production was slightly softer-than-expected, an optimistic outlook for the coming year was provided. We were also pleased that Management reaffirmed their production and cost guidance for FY23. A combination of operational efficiency efforts and number of growth initiatives in place such as the ramp-up of the Thunderbox mill capacity expansion should put NST in good stead to deliver strong second-half earnings growth.

Webjet advanced +29.8% in the fourth quarter, the catalyst for these gains being a product of a strong 1H23 trading update in November. All three of the travel company's businesses WebBeds, Webjet OTA and GoSee were profitable for the half resulting in the group posting \$72.5m profit, contrasting with the -\$15.9 loss made in the prior corresponding period. The result was indicative of the travel rebound underway with consumer demand being largely insulated from the effect of higher ticket prices and general rise in the cost of living. WebBeds, for example, reported booking volumes to be 13% higher than pre-pandemic levels and on track to reach pre-pandemic profitability in 2023. Over the last few years WEB has undergone a period of operational transformation to drive greater efficiency within the business through innovation such as automation, whilst leaning out their cost base and the fruits of these changes was evident in the result with expenses -16% lower than pre-pandemic. The combination of resilient travel demand, particularly as international capacity continues to unwind, and efficiency of WEB's business model should continue to drive earnings and margin growth and offset any near term macro weakness.

### Fund Activity

We continued to adjust the Fund's holdings across a variety of sectors through the December quarter.

We introduced a retail conglomerate to the Fund as we believe this constituent will be a beneficiary of strong trade hardware performance over the next 12-18 months due to the pull forward of government stimulus for the building industry along with rebuild for the recent floods. An accretive acquisition made in the trade space should drive store numbers from 60 to 170 over the next five years which will bolster strong growth for the company's hardware divisions. Overall, new management and strong capex program has contributed to increased market share and will continue to drive stronger growth for the business.

We also took the opportunity to add to our holdings in a mining services and operations. We were attracted to the company's diversified business divisions, consisting of two lithium mines, an iron ore business and mining services business, as well as the miner's strong leadership team whom we see as focused on delivery expansions within all three businesses. The miner has also recently made a gas discovery in the Perth Basin with the potential for development in the next few years.

We exited our position in securities exchange company ASX Limited (ASX) given the increased regulatory, earnings and capex risk arising from the CHES replacement delay. We have also been disappointed in the absence of any meaningful recovery in the financial services company's Derivatives volumes.

We trimmed our holdings in a mining and metals company given the pricing for the miner's commodities mix has decreased over the past 6 months in particular, aluminium which has seen China increase production in a weakening demand environment. Whilst we remain optimistic on the company's long-term growth trajectory, we expect these factors to affect cash flows in the near term.

### ESG Activity

The fourth quarter is typically a busy one for ESG-related issues as investors, fund managers and other financial market participants are tasked with the Australian proxy voting season. Importantly, company annual general meetings (AGMs) and accompanying meetings with boards present an opportunity to voice appraisals and/or concerns. This proxy season the AEQ Growth team voted on 63 meetings and voted against 8% of all resolutions.

Three companies held in the AEQ Growth team's portfolios received a 'strike', this identifying votes of more than 25% against the remuneration report - Goodman Group (GMG), EML Payments (EML) and Cleanaway (CWY). We supported all three remuneration reports for different reasons, explained below:

- **Goodman Group:** the overall pay potential at Goodman has been large for some time because a significant portion of equity is subject to lengthy testing and deferral for up to 10 years. While we acknowledge the large pay potential, we are pleased that the face value of the 10-year LTI awarded this year will be lower and we support the 10-year performance period in principle. This is the longest period of deferral in the Australian market.
- **EML Payments:** the company addressed many of the weaknesses in remuneration in 2022 and has committed to not using discretion to override STI and LTI hurdles in the short term. We are extremely disappointed with the sign-on grant to the new CEO and have raised this with the company.
- **Cleanaway:** we were disappointed by some of the adjustments to financials that affected bonus outcomes and raised these with the company but we were largely comfortable with the overall remuneration outcomes for the executive team.

When we have concerns on pay or governance-related issues, we typically raise these concerns in meetings with the company either ahead of the AGM or very soon after. We have found that providing clear and direct feedback in constructive conversation often leads to a commitment to addressing some, if not all, of our concerns. This is particularly the case if we have voted in support of resolutions. As part of our rigorous engagement program we will vote against resolutions if we have given the company an opportunity to address our concerns and they have failed to do so.

There was only one "Say on Climate" vote across our holdings this proxy season. This was for South32's (S32) transition plan, which we supported. The company improved its transition plan in 2022 with more ambitious emissions reduction targets, clearer scenario planning, and the disclosure of a shadow

carbon price. There remains opportunities for improvement, including the need for short and medium term carbon reduction targets, which we will raise with the company in 2023.

Proxy season aside, climate-related litigation was a focus for the team in the fourth quarter. In December, Santos (STO) lost a challenge in the Federal Court of Australia related to the drilling permit for its Barossa project. The challenge succeeded because Santos's consultation with affected people before submitting the drilling plan was found to have been below the standard implied by the regulations.

Other cases we are monitoring include a challenge to Woodside's (WDS) Scarborough project by the Australian Conservation Foundation in the Federal Court and a claim by ACCR that Santos mislead or deceived the market with its 2020 transition plan and other disclosures in 2021. Both are likely to be important test cases for Australian companies generally.

### **Market Outlook**

In an unprecedented year of macro-driven volatility, surging inflation, oil prices and bond yields, coupled with a synchronous global tightening cycle has meant that financial market participants remain tasked with recalibrating economic growth expectations for 2023.

Economic data releases continue to demonstrate a general resilience in labour force gains, the impact of residual excess savings and consequently, consumer spending and activity. However, consumer confidence remains at recessionary levels, demonstrating signs that the impact of these headwinds is slowly but surely unfolding.

As the tightening cycle is further digested over time, high living costs and declining property and stock prices will erode household balance sheets and will ultimately restrict consumer demand and spending power. This will have a bull-whip effect on already easing supply chains demonstrated by falling global freight costs, as well as company supply-demand fundamentals including sticky costs, lower sales volumes and higher inventories which will deteriorate margins and their ability to raise prices.

With inflation decelerating as supply chain woes abate and demand is tempered, the inevitable economic slowdown is unravelling and placing company revenues and earnings under pressure. In our view, cyclical stocks will be most susceptible to the impact of this slowdown whilst high quality growth stocks will be better placed sources of earnings growth. This reinforces the need to invest in companies that have distinctive products/services that have the capacity to grow earnings and generate a strong return on invested capital.

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

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