Chester High Conviction Fund

Fund Update

May 2024

APIR OPS7755AU
ARSN OPS7755AU

At 31 May 2024	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)	1.1	5.1	11.9	11.7	9.4	13.4	12.3
S&P/ASX 300 Accumulation Index	0.9	1.1	10.7	12.8	6.5	7.8	8.0
Outperformance (after all fees)	+0.2	+4.0	+1.2	-1.1	+2.9	+5.6	+4.3

* 27 Apr 2017

“Markets are strong when broad, weak when narrow”

Bob Farrell’s rules of investing #9

Month in review

Trying to time a market cycle is near on impossible. Markets tend to make most people look foolish most of the time. Can they continue higher? Of course they can, however we are witnessing the Nasdaq driven Mag 7 rally narrow down to the Mag 1 (Nvidia). When Jensen Huang (Nvidia CEO) is signing autographs on the chests of female fans after a presentation, we believe we are close to peak AI hysteria.
The dispersion of metrics between high quality long duration assets and asset backed industrials with valuation support appears far too wide to us, as does the disconnect between the strength in the ASX Banks, relative to the growing economic concern we are hearing about on a daily basis. Over recent weeks, we have heard increasing concerns over the housing clearance rates from auctioneers, McDonalds year on year sales, various retailers (including large car dealers) and consumer confidence all suggesting in real time a weakening of the domestic economy. The economic surprise index is pointing to a similar weakening of US data over the past 4 weeks. Perhaps this most recent uptick in equity markets signals rate cuts are on their way. Bad news is good news? Until it isn’t.

From a Federal Reserve perspective, it appears patience is the current order of the day. Maybe the rate cycle only starts after extreme dislocation, which is nowhere near apparent with markets at record highs. Without material deterioration in the labour force, the Fed has been effective in pushing out rate cuts, given stickier inflation in 2024 so far. In our view, this makes payroll data and wage growth one of the more important clues as to when a rate cycle may start, both in Australia and the US. Canada has already been the first G7 country to start an easing cycle.
We remain surprised with the extent of the Australian bank outperformance over recent months, with CBA now trading on almost 22x FY25 PER and a 3.8% dividend yield, well below the return of the cash rate. A record high share price with extremely benign impairment charges. We wouldn’t want to be standing in the way when this cycle changes. The most logical explanation for the CBA relentless buying is passive flows, as fundamentally it looks increasingly illogical.

Portfolio review

During the month the fund returned 1.1% relative to the 0.9% rise in the ASX300. Outperformers for May were led by our position in Telix Pharmaceuticals (TLX). TLX had a particularly strong end to the month, rising 15% on the 31st off the back of positive results from the ProstACT SELECT Trial, with progression free survival being 8.8 months, an encouraging signal of the potential efficacy of TLX591. TLX591 is one of the additional products beyond Illucix (a therapy rather than imaging product) that has the potential to add material upside and TAM to the TLX thesis. Botanix (BOT) had a successful month with the company hosting a webinar regarding US commercial launch plans for Sofdra, their key product for hyperhidrosis (excessive sweating). FDA approval is expected for the product later this month. We have considered a range of valuation scenarios and still see a material upside case if commercialisation is successful. The position sizing is commensurate with its risk profile. GQG Partners is a large global fund manager with strong momentum from inflows and performance trading on 11x FY25 PER and a 8% dividend yield with eps upgrades pending.

Underperformers for the month were led by Nufarm (NUF) which delivered half year FY24 results below expectations on the back of mainly softer commodity prices and margins. A cyclical recovery of the crop protection business as excess inventory is cleared is entirely probable, but the share price weakness would suggest the cycle never returns. We continue to be attracted to the long-term fundamentals of the business, particularly Seeds, and highlight if they are able to achieve FY26 guidance (as they have reiterated) there is potential for the stock to materially rerate. Despite strong copper and zinc prices during May, Develop (DVP) remains under pressure, particularly after a recent sell down by Mineral Resources (MIN). There is one key reason: funding. Our impression is the market continues to believe DVP are going to raise capital to fund projects and the AUD20m contingent payment on Woodlawn. We see this pressure being alleviated in the near term via: a) actually completing a capital raise (not our base case) or b) alternative financing solutions (debt, project sell down(s), etc.). The optionality within the business remains compelling in our view.

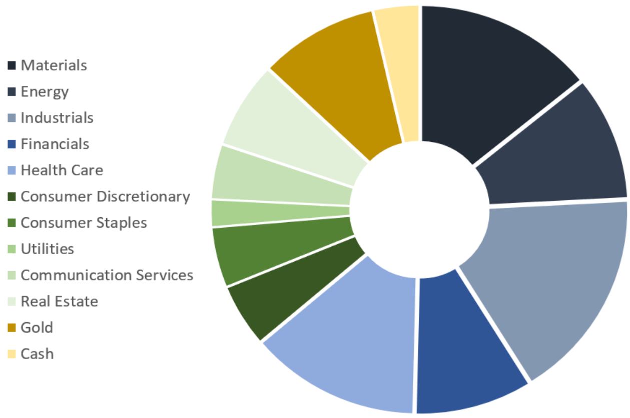
Top 3 holdings
CSL
Austal
Aurizon

Portfolio breakdown	
Industrials	17.0%
Materials	14.2%
Health Care	13.5%

Top 3 portfolio attribution
Telix
Botanix
GQG Group

Bottom 3 portfolio attribution
Nufarm
Develop Global
Aurizon

Fund weights - diverse sector exposure



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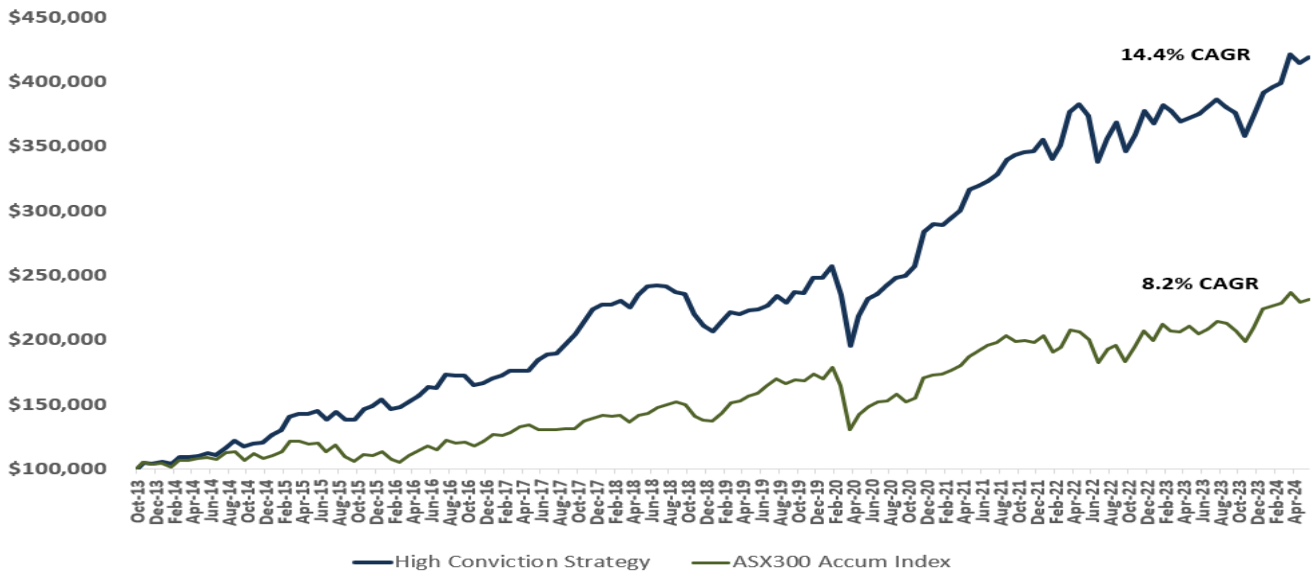
Accumulated Performance by Financial Year - Same Strategy

	FY14 (%)#	FY15 (%)	FY16 (%)	FY17 (%)*	FY18 (%)	FY19 (%)	FY20 (%)	FY21 (%)	FY22 (%)	FY23 (%)	FY24 (%)	Inc (%)
Same Strategy (after MER)	+11.2	+24.5	+17.4	+11.2	+28.3	-6.4	+3.9	+37.2	+4.8	+12.5	+10.9	+14.4
S&P/ASX 300 Accum Index	+7.8	+5.6	+0.9	+9.1	+13.2	+11.4	-7.7	+28.5	-6.8	+14.4	+10.1	+8.2
Value added (after MER)	+3.5	+18.9	+16.4	+2.1	+15.1	-17.8	+11.6	+8.7	+11.6	-1.9	-0.8	+6.2

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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