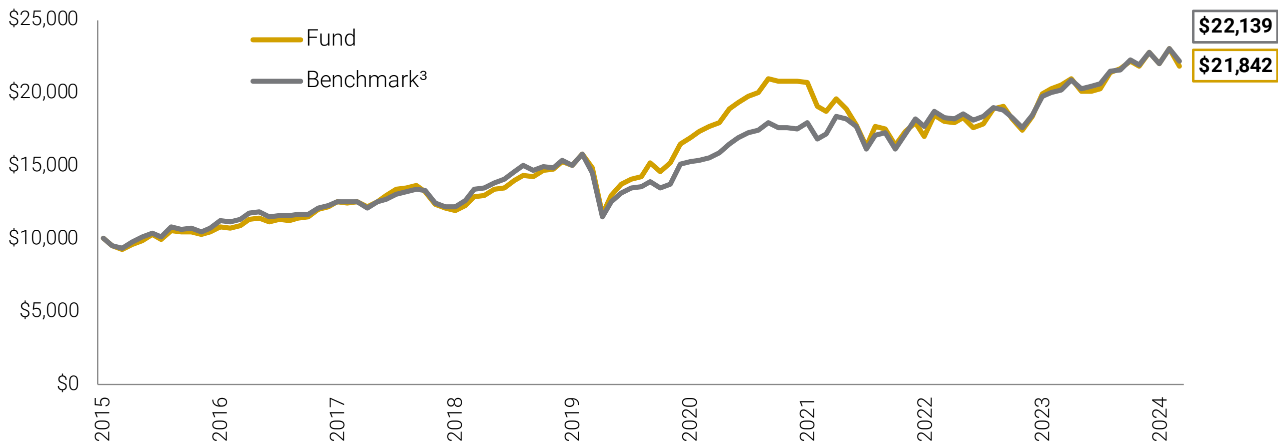
BAEP
Bennelong Australian Equity Partners

Investor Commentary | 28 February 2025

Bennelong Twenty20 Australian Equities Fund

Long-term Fund performance

Growth of $10,000 since inception[1,2]



Past performance is not indicative of future performance.

Market review

The ASX300 delivered a -3.8% return in February. Defensive sectors led during the month with Utilities (+3.2%), Communication Services (+2.6%), Consumer Staples (+1.5%) and Industrials (+1.4%). The laggards during the month included Information Technology (-12.3%), Health Care (-7.7%) and REITs (-6.4%).

February included the 1H25 reporting season, with the elevated volatility of the market being the most notable feature. Twenty percent of ASX200 stocks moved +/-10% on their result day, the most volatile earnings season on record. When looking across all companies that reported, the result day high and low difference produced an average return swing of 7.9%. To put this volatility in a historical context, 22% of stocks experienced a 4 standard deviation move, which is almost double the level of reporting season volatility around the GFC and 50% higher than what was experienced during COVID.

Looking through the volatility, reporting season saw around 30% of companies beat consensus earnings expectations and 21% miss – a strong outcome. The key driver of better 1HFY25 earnings was better margins, reflecting ongoing focus on cost control and lingering pricing power. The issue with many results was softer management outlook comments. Around 23% of companies delivered outlook comments that were above expectations while 19% were below. The fact that 30% of companies beat on earnings, but only 23% then used that first half strength to upgrade their outlook, shows that companies are uncertain – given the volatile geopolitical outlook – and so are being cautious with market commentary.

The 12 month forward earnings for the ASX300 were downgraded by around 1.9% such that the FY25 EPS is now expected to be below FY24. The Resources sector was again the biggest drag on earnings with FY25 EPS for the sector downgraded -3.5% to a decline of -18.3% YoY. Industrials earnings were downgraded 0.5%, with a larger downgrade for Domestic Industrials (-1%) than those with international earnings (-0.1%). International Industrials still offer the stronger forecast EPS growth in FY25 at 10% (and accelerating to +14.3% in FY26). On average, stocks in the BAEP portfolios had small beats on 1H25 earnings of around 1% with 12-month forward earnings on average experiencing small downgrades (~2%).

The increased level of uncertainty seen in markets over February, largely as a result of changing US policy, caused a broad market valuation de-rating, with the PE of the ASX300 falling by around 4% to 18.0x.

Consistent with the strength in the month from more defensive sectors, Macquarie Research data showed that on average, stocks with positive earnings momentum leading into results did beat on earnings, but their share prices did not subsequently outperform. Meanwhile, those with poor momentum (often with high short interest) outperformed, even though they had net negative surprises from results overall. We have included further discussion on the major stock contributors and detractors of the portfolio in the Portfolio Review section.

The RBA delivered its first long-awaited rate cut in February, but pushed back on expectations for further easing, given a tight (and tightening) labour market. Wages growth remains solid and productivity is falling. Compensation of employees accelerated further in the 4Q national accounts, +2.0% QoQ and +6.1% YoY.

Real GDP rose 0.6% QoQ in the December quarter and 1.3% YoY (in line with consensus). GDP per capita finally rose +0.1% QoQ (-0.7% YoY). That anaemic growth comes after the longest per capita recession of seven successive quarters since the 1930s. The modest growth was again driven by a boom in public demand (+1.0% QoQ, +5.5% YoY) versus private sector which continues to struggle (+0.4% QoQ, +0.8% YoY). It was encouraging to see real household consumption starting to show some improvement (+0.4% QoQ, +0.8% YoY). There are some signs the domestic economy is starting to improve but the gains are modest and from a low base. Consumers are starting to spend their tax cuts and governments are promising to spend even more leading into the election. Conversely, inflation looks sticky and may accelerate in 2H25 if the recovery continues given the tight labour market. It was notable that Wesfarmers (which operate across many industries in Australia) made the comment at its earnings release that *"domestic cost pressures are likely to persist with higher labour, energy, supply chain costs"*.

The US February PMI fell back from 52.7 to 50.4. The overall number did mask two diverging trends: Services fell from 52.9 to 49.7, conversely Manufacturing rose from 51.8 to 53.8. The US ISM Manufacturing Index fell 0.6ppt to 50.3 in February, however it was the mix which caused concern. New Orders (48.6) and Employment (47.6) moved into contractionary territory, while Prices Paid for materials surged to 62.4 as tariff concerns increased. The real threat from tariffs however, is if they impact consumer spending, which is just under 70% of US GDP. The University of Michigan Consumer Sentiment Index decreased to 71.7 in February, down from 73.2 in January. This decline was consistent across various demographic groups indicating a broad-based deterioration in consumer sentiment. About 40% of respondents mentioned tariffs as an area of concern. The abrupt way in which Trump is announcing policy (notably with Tariffs and DOGE) is obviously leading to more caution from households and businesses. The consumer discretionary sector ETF in the US has fallen by around 19% from its December 2024 peak while the S&P500 is down by around 10%. This is having some flow-on effect to consumer stocks globally, particularly those which have businesses in the US.

The stated aim of Trump's MAGA program is to improve the balance of the US's global trading relationships and reshore some manufacturing, particularly where that de-risks supply chains for critical industries such as those related to defence. This would also put the US on a more sustainable fiscal path, lowering trade deficits and controlling government debt. A key risk to the US achieving this is the strong USD (as represented by the US dollar currency index, the DXY). During the GFC the DXY bottomed at around 70. It then more or less rose for 15 years fuelled by low interest rates in many countries, notably Japan. This gave rise to the 'yen carry trade' where institutions could borrow yen at close to zero and then invest in US assets with higher returns. This started with US treasuries, but expanded to sectors like US Tech, many credit instruments and various Australian assets. Many of these trades were highly leveraged. There is a risk that if Trump succeeds in weakening the USD, it will force the unwinding of many of these carry trades which have seen inflows for many years. The DXY has already fallen from its January high of ~110 to ~103. This is leading to volatility in crowded assets such as we saw in August 2024 when the Bank of Japan (BOJ) raised interest rates and people started talking about the unwinding of yen carry trades. We note that Kazuo Momma, the former director in charge of monetary policy at the BOJ, was recently quoted as saying *"June is the favoured option in my base case [to raise interest rates again] ... It's important for the BOJ to maintain expectations that it will move roughly every six months."*

Fund performance

	Fund	Benchmark[3]	Value added
1 mth	-5.25%	-3.79%	-1.46%
3 mths	-4.09%	-2.59%	-1.51%
CYTD	-0.66%	0.50%	-1.16%
1 year	6.43%	9.65%	-3.22%
3 years p.a.	5.26%	8.89%	-3.64%
5 years p.a.	8.06%	8.79%	-0.74%
10 years p.a.	na	na	na
Since inception[1] p.a.	9.04%	9.07%	-0.03%

Performance figures are net of fees and expenses. 'Value added' calculation does not use rounded performance figures.
Past performance is not indicative of future performance.

Portfolio characteristics

	Fund	Benchmark[3]	Profile
Return on Equity	13.5%	11.8%	Premium Quality
Debt/Equity	29.1%	39.2%	
Sales Growth	3.5%	3.3%	Typically More Growth
EPS Growth	2.8%	4.8%	
Price/Earnings	20.3x	18.0x	Reasonable Valuation
Dividend Yield	2.8%	3.6%	
Beta	1.08	1	
Active Share	35%	na	Genuinely Active
No. of Stocks	41	297	

Source: broker consensus estimates for the next 12 months

Portfolio review

The Fund delivered a return of -5.25% for February which was -1.46% below the -3.79% benchmark return. The Fund's primary active contributors in the month were Corporate Travel (CTD), The Reject Shop (TRS) and Universal Stores (UNI). The primary active detractors included Fisher & Paykel (FPH), WiseTech Global (WTC) and Block (XYZ).

At a sector level, the Fund received a small benefit from the underperformance of the Energy and Banks sectors which was partially offset by a rally in Gold miners which we are underweight.

Top five active holdings

At month end, in alphabetical order

Company
Breville Group Limited
CAR Group Limited
Fisher & Paykel Healthcare
Supply Network Ltd
Universal Stores

Top three contributors

To monthly relative performance, in alphabetical order

Company	Avg active position
Corporate Travel Management	Overweight
The Reject Shop	Overweight
Universal Stores	Overweight

Corporate Travel (CTD)

The company delivered a strong 1H25 result with EBITDA of $77.4m ahead of consensus (which was in line with guidance) at $73.5m. This was driven by the ANZ result, with 18% revenue growth and 53% EBITDA growth. The division had strong client wins including returning clients, plus good success with sleep space. The US business delivered revenue growth of 6% and EBITDA growth of 49%. The stronger US margin was due to the uptake of the company's Lightning booking tool. This translated to stronger profit outcomes given it is on their own software and hence no leakage of fees. While FY25 is a transition year for the European business, there is now more clarity on the UK Government's travel program which has been the key issue for the business. In addition, CTD has achieved strong wins in the UK which should see growth from Q4. Overall the result was strong with the outlook more certain. Maiden FY26 guidance was provided which was ahead of consensus. EPS upgrades were around 5%.

The Reject Shop (TRS)

The company posted a solid result with EBIT increasing 16.2% on pcp. Sales grew +2.9% and comp sales +1.5% (with improvement from 0.3% in 1Q to +2.5% in 2Q). Sales growth was driven by the success of their refreshed product ranges and successful events such as Halloween and Christmas. Stock loss deteriorated slightly more than they expected with theft being an industry wide issue. GP margin improved 125bp to 41.6% with further benefit to GP margin if they can improve their product mix. Management noted they are tracking slightly ahead of their target for 40.5% GP for FY25. Costs were also well managed in a challenging environment, but CODB did increase 0.7% to 35.5% as a percentage of sales.

Universal Stores (UNI)

UNI reported a strong result with sales +16% on pcp. NPAT was 3% ahead of expectations. Gross Margins increased 90bps to 60.6% which offset an increase in CODB due to an investment in the team capability as well as general inflation. The outlook comments were also solid with the trading update for the first seven weeks of 2H25 reporting group direct to consumer (DTC) sales up +31.8% vs pcp. This was driven by strong growth in all brands, with Universal Stores' sales +27.6% (LFL: 22.5%), Perfect Stranger sales +90.1% (LFL: +38.8%) and CTC sales +40.1% (LFL: 37.8%). Management expect the wholesale channel to remain challenging in 2H25, however this represents less than 5% of Group sales. The company continues to execute well at a time when competitors have been struggling. They have plenty of opportunity to increase store numbers and may gain a tailwind from improved consumer spending.

Top three detractors

To monthly relative performance, in alphabetical order

Company	Avg active position
Block	Overweight
Fisher & Paykel Healthcare	Overweight
WiseTech Global	Overweight

Block (XYZ)

Block fell sharply after reporting 4Q24 results. 4Q24 gross profit growth of 14% was in line with guidance while EBIT was slightly ahead. While Block re-iterated 2025 guidance for at least 15% gross profit growth and margin expansion, 1Q25 guidance of 11% gross profit growth was below consensus of 14% due to short-term impacts (Leap year, FX, weather headwinds) and the timing of product launches. Therefore, 2025 guidance implies an acceleration from 11% gross profit growth in 1Q25 to high teens growth in 2HCY25. The market became nervous on the required 2H acceleration and execution needed to deliver this growth. Block called out clear visibility in the drivers required to achieve the 2025 guidance. These include the expectation for improved Square GPV growth from high single digit to low double digit growth by the end of 2025 as the benefits of recent product improvement, significant hiring and marketing expansion begin to contribute. In addition, Block

launched the integration of Buy Now Pay Later into Cash App in February and also plans to expand Cash App Borrow eligibility, both of which will accelerate growth in CashApp through 2025. We note that the selling in US payments stocks was indiscriminate during February with many of Block's US listed peers suffering similar falls: Toast (TOST) fell 13%, Affirm (AFRM) fell 14.5% and Shift4 Payments (FOUR) fell 10%.

Fisher & Paykel (FPH)

The company did not report in the period as they have a March year end. The stock fell following the threatened imposition of tariffs on Mexico where 60% of FPH's US imports are supplied from. There remains significant uncertainty as to what might be the final quantum of tariffs on FPH's product and when those tariffs would start, if at all. FPH is planning to significantly mitigate tariffs by supplying more of the US imports from NZ and using the Mexican facility to supply other parts of the world. They could also consider increasing prices to share the impact with their customers. Operationally the company is performing well. They had earnings upgrades through the second half of last year as new products are selling well (both in hospitals and in home care). The company is achieving the margin expansion they promised the market. Consensus earnings growth is expected to be +36% this year with consensus forecasts of mid to high teens earning growth over the next few years.

WiseTech Global (WTC)

WTC reported 1H25 results in line with prior guidance and expectations, with organic Cargowise revenue growth of 20% and EBITDA growth of 28%. However, the focus was on governance matters and guidance that FY25 earnings will be at the lower end of the previously guided range. There has been months of speculation over the future role of WTC founder Richard White since stepping down from the CEO role in Oct-24. Mr White was supposed to remain at WTC under a consultancy arrangement running product development, but this agreement was never executed. In February, four of the independent directors on the board resigned due to intractable differences between the board and founder Mr White. This has led to Mr White becoming executive chairman. Two long term directors have remained on the Board and one former director has rejoined as Lead Independent Director. WTC updated the market and said that a search for a permanent CEO continues, and a board renewal process is underway with another independent director to join in less than four weeks. A further update on the investigation into Richard will be provided in Mid-late March. WTC updated FY25 guidance which is now expected to be at the lower end of the previously provided revenue range (~20% Cargowise organic growth in 2H25) and the upper end of EBITDA margin range, implying ~25% EBITDA growth. This saw low to mid single digit reductions to consensus FY25-26 earnings. This was due to further delays to the release of the three new break-through products which are now rolling out during 2H25 and therefore won't contribute to revenue in this period.

Outlook

A large part of the Market Review was spent discussing the extraordinary volatility seen in markets recently. The question which invariably follows is 'so how do you position the portfolio?' While we continue to maintain our high intensity of research and we are more mindful of position sizes and risk, the fact remains that the best way to deal with volatile and uncertain markets is to own quality companies that are less reliant on favourable government policy or broader macroeconomic trends.

With that in mind, BAEP's investment philosophy and approach remains unchanged. We invest in high-quality companies that are global leaders in their niche that can sustainably compound their earnings at above market growth rates, over the medium to long term. They do this by investing in R&D to develop a superior product or service which enables them to take market share and grow earnings largely irrespective of the cycle. We take a bottom-up research approach driven by extensive company and industry contact to deepen our understanding of the companies we invest in and where earnings prospects may be under-appreciated by the market. Over the long term we believe earnings delivery drives company share prices. So, investing in quality companies delivering sustainable compound earnings growth is what will drive attractive returns for our portfolios over the medium and long term.

It is interesting to note recent comments by Scott Bessent (US Treasury Secretary) and President Trump. Bessent recently said *"Could we be seeing this economy that we inherited starting to roll a bit? Sure. Look, there's going to be a natural adjustment as we move away from public spending. The market and the economy have just become hooked, and we've become addicted to this government spending… There's going to be a detox period."* Even Trump, who many believed would have no stomach for market weakness, said, *"I'm not even looking at the stock market, because long term the United States will be very strong with what is happening here*".

The past couple of weeks has seen some extraordinary events. Germany is now proposing a 400bn Euro additional spend on defence plus a longer dated 500bn Euro spend on infrastructure. This is Germany's largest shift on spending and military involvement since 1945. Both UK and France are proposing smaller but significant accelerations of defence spending. This is highly stimulatory to the broader European economy. We also have China increasing liquidity and making greater efforts to stimulate its domestic economy. So while there may be stocks that face more protracted downturns, there will also be many winners from the changes we are seeing. It is also important to remember that the US economy is solid and Trump's agenda of lower energy prices, lower taxes and deregulation is broadly positive for US businesses. The Fed is forecast to cut rates three times this year and if a deeper slowdown was to occur they could cut a lot further. The RBA is also expected to cut interest rates again this year.

We continue to focus on the expected earnings growth of the portfolio as over time share prices follow earnings. To achieve superior returns we need to own stocks with

superior earnings growth. The cumulative forecast three-year earnings growth for the portfolio using market consensus forecasts is 17.0%, which is similar to the ASX300's growth. This similar growth is explained by the portfolio's index position in the ASX20. The portfolio is higher quality, however, with an ROE of 13.5% versus the ASX300 of 11.8%. This higher ROE also comes despite lower levels of debt. The portfolio's gearing of 29.1% compares to the ASX300 at 39.2%. Over the long term, we expect the high quality to drive superior returns.

About the Fund

The Bennelong Twenty20 Australian Equities Fund provides a cost-effective exposure to the S&P/ASX300 universe through a combination of actively managed ex-20 securities and a passive exposure to the top 20 securities. It typically holds 40-55 names.

The Fund is a single portfolio made up of two parts:

1. **An indexed position in the S&P/ASX 20 Index ('the top 20') –** The Fund has a position in each top 20 security in the same weight it has in the S&P/ASX 300 index. This means the Fund's largest positions are the largest companies on the ASX. For example, if Commonwealth Bank has a weight of 7% in the index, it will also have a weight of 7% in the Fund.
2. **An active position comprising BAEP's best picks from outside the top 20 ('the ex-20') –** The Fund is also invested in a selection of ex-20 securities we believe will outperform, which in turn allows the Fund to outperform the benchmark. These securities are chosen using our proven approach that focuses on fundamental factors such as earnings, growth and valuations.

Benefits of the Fund

- Cost-effective, with a low management fee (plus a performance fee where applicable)
- Provides broad exposure to the Australian market via a combination of passive and actively managed securities
- The Fund's ex-20 exposure is managed as per the Bennelong ex-20 Australian Equities Fund's strategy. which has a track record of adding value by outperforming the market over the long term
- Managed in accordance with BAEP's robust, disciplined and proven investment philosophy and process

About BAEP

Bennelong Australian Equity Partners (BAEP) is a boutique fund manager investing in Australian listed equities. It was founded in 2008 by Mark East, in partnership with Bennelong Funds Management.

BAEP is a genuinely active, award-winning and highly-rated fund manager with an experienced and performance oriented team. Its investment philosophy is to selectively invest in high quality companies with strong growth outlooks and underestimated earnings momentum and prospects. Its investment process is research-intensive, with a focus on proprietary field research, and is supported by macro-economic and quantitative insights.

Portfolio sector allocation

Sector	Fund Weight	Benchmark Weight[3]	Active Weight
Discretionary	21.2%	8.1%	13.1%
Communication	7.5%	4.0%	3.6%
Health Care	11.3%	9.4%	1.9%
Liquidity	-0.1%	0.0%	-0.1%
Financials	32.4%	33.1%	-0.7%
IT	2.2%	3.1%	-0.9%
Energy	2.7%	3.9%	-1.1%
Consumer Staples	2.5%	3.8%	-1.3%
Utilities	0.0%	1.4%	-1.4%
Industrials	3.9%	7.6%	-3.7%
REIT's	2.5%	6.8%	-4.2%
Materials	13.7%	18.9%	-5.2%

The Fund at a glance

Feature	Fund facts
APIR code	BFL0017AU
Benchmark	S&P/ASX 300 Accumulation Index
Investment objective	2% p.a. above benchmark measured over rolling 3-year periods
Active stock limit	± 5%
Cash limit	0 - 10%
Inception date	02 December 2015
Recommended investment period	Long term (five years plus)
Buy/sell spread	+/-0.20%
Entry/exit fees	Nil
Management fees and costs[4]	0.44% p.a. of Net Asset Value of the Fund
Performance fee	15% of any amount by which the Fund's return is greater than the return generated by the S&P/ASX 300 Accumulation Index

How to invest

The Fund is open to investors via the PDS (available on our website), mFund (code: BAE04), or the following platforms.

- AMP (Elements Investment, Elements Pension, iAccess, My North, North, Portfolio Care, Portfolio Care eWrap, PPS, Summit, Wealthview eWrap Inv)
- BT Asgard (Master Trust, Employee Super, Infinity eWrap)
- BT (Panorama)
- CFS (FirstWrap)
- Dash
- Hub 24 (Super, IDPS)
- Macquarie Wrap (IDPS, Super)
- Mason Stevens
- Netwealth (Super Service, Wrap Service, IDPS)
- Praemium (Non Super, Super)

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1 Inception date is 2 December 2015

2 Calculations are based on net returns (after fees and expenses) and assume the reinvestment of distributions.

3 S&P/ASX 300 Accumulation Index

4 Management fees and costs consist of annual management fee rate and capped recoverable expenses. For a detailed split of the fees and costs, please refer to the fund(s) PDS.

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