# BLACKROCK HIGH CONVICTION AUSTRALIAN EQUITY FUND

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**FUND UPDATE** **30 April 2024**

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- Market Insights & Commentary
- Fund Performance
- Unit Prices

## Investment Performance (%)

| | 1 Mth | 3 Mths | YTD | 1 Yr | Since Manager Incep[3] pa | 2 Yrs pa | 3 Yrs pa | 5 Yrs pa | Since Incep[1] pa |
|---|---|---|---|---|---|---|---|---|---|
| Class D (Net of Fees) | **-2.18** | **1.60** | **2.93** | **10.08** | **12.77** | **-2.71** | **-5.55** | **1.30** | **4.59** |
| Benchmark[2] | -2.92 | 1.23 | 2.34 | 9.04 | 12.18 | 3.60 | 4.51 | 5.74 | 7.55 |
| Outperformance (Net of Fees) | 0.74 | 0.37 | 0.59 | 1.03 | 0.59 | -6.30 | -10.05 | -4.43 | -2.96 |
| S&P/ASX 300 (for comparative purposes) | -2.92 | 1.23 | 2.34 | 9.04 | 12.18 | 5.53 | 7.05 | 7.98 | 9.33 |

[1] Unadjusted class D performance since inception date of 4th January 2016

[2] The Fund benchmark from inception to 9 March 2023 was the S&P/ASX300 Industrials Accumulation Ex Top 5 Stocks by Mkt Cap Gross Index. From 9 March 2023 the Fund benchmark was S&P/ASX300 Accumulation Index

[3] With an inception of 29th March 2023, Pendal Group took over management of this strategy on a sub-advisory basis

Please see ^^ in the footnotes of further information.

## Performance Summary – April 2024

### April Market review

Some stronger-than-expected inflation data in both the US and Australia saw expectations about the timing and scale of potential rate cuts in both countries dialled back for 2024.

In the US, March's headline and core consumer price indices (CPI) came in in at +0.4% month-on-month, versus +0.3% expected.

In Australia, the Q1 2024 consumer price index slowed from 4.1% year on-year in the previous quarter to 3.6%, but this was still ahead of expectations and the "trimmed mean" preferred by the RBA rose +1.0% versus +0.8% expected.

At the same time economic indicators remained broadly resilient which, along with some better-than-expected data from China, helped underpin a rebound in commodity prices.

Bond yields rose over the month. The US ten-year government bond yield rose 48bps to 4.68% while the Australian equivalent was up 46bps to 4.42%.

This weighed on equity markets and on the rate-sensitive sectors within it. The S&P/ASX 300 fell -2.92%.

Utilities (+4.77%) was the only sector to make material gains, on the back of AGL Energy (AGL, +13.43%) and Origin Energy (ORG, +5.98%).

Materials (+0.59%) were mixed. A 15.8% gain in the iron ore price helped Rio Tinto (RIO, +7.17%) and Fortescue (FMG, +1.36%). BHP (BHP, -2.80%) had also made gains, but lost them late in the month on the news of its bid for Anglo American. Copper strengthened 12.7%, helping South32 (S32) up 19.67%, while the gold miners continued to outperform. However construction-related names such as James Hardie (JHX, -12.01%) and BlueScope Steel (BSL, -4.02%) underperformed.

Real Estate (-7.64%) fell as rate cut expectations were pared back. Falls were broad-based with Goodman Group (GMG), Scentre Group (SCG) and Stockland (SGP), the three largest property stocks in the index, falling -6.27%, -6.19%) and -8.25% respectively.

Consumer discretionary (-5.31%) fell as some companies sounded a warning about softness in demand. Again, weakness was broad-based. Wesfarmers (WES) fell -2.35%, Aristocrat Leisure (ALL) -7.16% and retailer JB Hi-Fi (JBH) -4.98%.

## Fund Performance

The fund registered a -2.18% return, outperforming the benchmark return of -2.92% by +0.74%. The portfolio outperformed the index in April. The overweights in Qantas, Metcash and Pro Medicus helped. So too did the mining exposure via South32, Rio Tinto and Mineral Resources, as commodity prices rebounded on some improvement in sentiment towards China. Within energy, owning Santos and not owning Woodside Energy was beneficial.

## Contributors

**Overweight Qantas (QAN, +8.26%)**

Qantas revamped its loyalty programme as part of the strategy to repair brand. The fear that this would lead to increase costs did not eventuate as the expected $120m impact will be absorbed by the $230m investment in improving customer experience that is already flagged for FY24. At the same time, the announcement cleared the way for the $448m stock buyback, which is expected to be complete by 30 June 2024.

**Overweight Evolution Mining (EVN, +13.41%)**

Evolution Mining reported a better than expected quarterly production update, maintaining guidance against expectations of a downgrade. At the same time gold prices continue to appreciate and have risen 10.8% over the year to date. It Cowal and Ernest Henry mines are performing reasonably well, but on the negative side, Red Lake in Canada and Mungari in Western Australia remain problematic, with little visibility of mooted cost improvements.

**Overweight South32 (S32, +19.67%)**

South32 reported better than expected Q3 production with free cash flow back in positive territory for the first time in eighteen months. The improvement was mostly down to a working capital unwind and slightly better pricing, rather than an improved operational performance - which again was generally weak versus expectations. Importantly, the improvement comes prior to the recent rally in pricing which can help further momentum.

## Detractors

**Overweight Orora (ORA, -19.49%)**

ORA sold off after surprising the market with a material downgrade to the 2H24 earnings of its North America packaging distribution division. This business is seeing a weaker than expected demand cycle and pricing pressure. The company had been expecting de-stocking to wind down in 4Q24 but is not yet seeing this happen. Although the market largely expected a downgrade for this business given weak demand for alcoholic spirits, the scale of it was larger than anticipated.

**Overweight Xero (XRO, -8.43%)**

Xero sold off along with most technology growth stocks as expectations around rate cuts were reeled in. Late in the month the company announced product changes and price increases for its Australian business, which is in keeping with management's focus on more disciplined decisions around return on capital and finding pathways for clients to move to higher value products. This resulted in small earnings upgrades.

**Overweight Charter Hall Retail REIT (CQR, -9.97%)**

CQR fell along with the rest of the property sector on tempered expectations around the timing and scale of rate cuts. The company continues to form part of the portfolio's more defensive exposure. Its retail malls tend to be focused around more non-discretionary anchor and speciality tenants, which may hold up better than other areas such as apparel if we start to see a material slowdown in consumer demand and economic growth.

## Performance and outlook

While acknowledging that the previous disinflationary trend had seen a setback and the need for rates to stay on hold for longer than previously thought, US Fed Chair Powell noted following the recent FOMC meeting that policy is already restrictive. The question is therefore how long they keep rates at the current settings.

He noted the criteria which could allow rates to fall – such as unexpected easing of the labour market - rather than the factors which could lead them to raise rates. This was likely a deliberate signal on where the Fed is focused.

He also noted that the Fed expects inflation to move back down this year.

Some recent data points support this view – notably the JOLTS "Quits" rates, which has been falling and has historically been a good lead indicator on wage growth. This can help ease near term pressure, although we note that there are still factors supporting structurally higher inflation.

Our conclusion remains that while the Fed retains its current "hold" bias, there is a skew towards looking for reasons to cut rather than reasons to raise rates.

Broadly speaking, the economy in both the US and Australia continues to hold up well, which is important as it underpin current expectations for earnings.

At this point ASX 200 FY24 earnings per share (EPS) are expected to fall 4%. This is driven largely by the resource sector, with Industrials (ex Financials) expected to see EPS grow 5.8%.

The market is content to look through the near-term earnings decline at this point and has re-rated in response to a receding risk of recession and in anticipation of a return not earnings growth in FY25.

That said, we are mindful of anecdotes of slower demand in Australia from consumer-facing companies. In the US, too, there have been some softer readings in recent business surveys.

This is something to monitor and the risk of recession remains, which is why we retain some defensive exposures within the portfolio.

The other risk scenario is that inflation rebounds, taking rate cuts off the table and risking economic growth as rates stay higher for longer.

For the moment though, we seem to be an environment where the path of inflation, while bumpy, is trending lower and central banks are looking for an opportunity to begin cutting rates. At the same time the economy, on the whole, remains in reasonable shape.

This is supportive for markets. So too is the liquidity situation as the Fed has scaled back quantitative tightening and the US Treasury retains its skew to the short end of the bond yield curve for funding.

| Top 10 Holdings Alphabetically |
|---|
| Stock |
| BHP GROUP LTD |
| COMMONWEALTH BANK OF AUSTRALIA |
| CSL LTD |
| NATIONAL AUSTRALIA BANK LTD |
| QANTAS AIRWAYS LTD |
| QBE INSURANCE GROUP LTD |
| SANTOS LTD |
| TELSTRA GROUP LTD |
| WESTPAC BANKING CORPORATION CORP |
| XERO LTD |

Source: BlackRock

**Sector Exposure**

| Sector | Weight % |
|---|---|
| Financials | 25.50% |
| Materials | 23.42% |
| Health Care | 10.96% |
| Communication Services | 7.77% |
| Energy | 6.69% |
| Industrials | 6.21% |
| Information Technology | 6.20% |
| Real Estate | 4.98% |
| Consumer Staples | 2.76% |
| Consumer Discretionary | 2.26% |
| None | 0.10% |
| Utilities | - |

Source: BlackRock

## About the Fund

This strategy is sub-advised by Pendal Group. The strategy is operationally managed by BlackRock and aims to replicate the Pendal Focus Australian Share Fund as closely as possible.

## Investment Objective

The Fund aims to provide a return (before fees, costs and taxes), that significantly exceeds the S&P/ASX300 (TR) Index over the medium to long term.

## Description of Fund

This Fund is designed for investors who want the potential for long term capital growth and tax effective income from a concentrated portfolio of primarily 15-30 Australian shares and are prepared to accept higher variability of returns. The Fund may also hold cash and may use derivatives.

Pendal's investment process for Australian shares is based on our core investment style and aims to add value through active stock selection and fundamental company research. Pendal's core investment style is to select stocks based on our assessment of their long term worth and ability to outperform the market, without being restricted by a growth or value bias. Our fundamental company research focuses on valuation, franchise, management quality and risk factors (both financial and non-financial risk).

Derivatives may be used to reduce risk and can act as a hedge against adverse movements in a particular market and/or in the underlying assets. Derivatives can also be used to gain exposure to assets and markets.

## Fund Positioning

The Fund is designed to complement a conventional, core share portfolio by providing satellite exposure to selected Australian equities with the potential for performance enhancement.

## Investment Team

Pendal's nineteen member Equity team is one of the largest in the Australian fund's management industry. The portfolio manager for the Fund is Crispin Murray, who has more than 31 years' industry experience. Crispin is also Head of Equity.

**Fund Details**

| BlackRock High Conviction Australian Equity Fund | |
|---|---|
| APIR Code (D Class) | BLK0012AU |
| Fund Size/strategy Size | $14m/$188m |
| Buy/Sell Spread | 0.25%/0.25% |
| Liquidity | Daily |

| Investment Guidelines | |
|---|---|
| Ex-ante tracking error | 3.0% - 6.0% |
| Max absolute stock position | 15% |
| Min/Max sector position relative to Index | +/- 15% |
| Min/Max BARRA style factors | +/- 0.5 SD |
| SIRA style factors | Within 1 SD |
| Maximum cash level | 30% |
| Shorting | No |
| Borrowing | No |

^^ Performance figures represent past performance and are not indicative of future performance. Current performance may be higher or lower than that shown. Net performance figures are calculated after fund management fees and expenses, and assume reinvestment of distributions. Unless otherwise stated, performance for periods greater than one year is annualised and performance calculated to the last business day of the month.



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