MONTHLY REPORT
DECEMBER 2023

PENGANA AUSTRALIAN EQUITIES FUND

DESCRIPTION

The Pengana Australian Equities Fund aims to enhance and preserve investor wealth over a 5- year period via a concentrated core portfolio of principally Australian listed securities. The Fund uses fundamental research to evaluate investments capable of generating the target return over the medium term. Essentially, we are in the business of seeking to preserve capital and make money – we are not in the business of trying to beat the market. We remain focused on acquiring and holding investments that offer predictable, sustainable and well-stewarded after-tax cash earnings yields in excess of 6% that will grow to double digit levels as a percentage of our original entry price in five years. We believe that building a well-diversified portfolio of these "gifts that keep on giving" represents a meaningful way to create and preserve financial independence for our co-investors.

STATISTICAL DATA

VOLATILITY[3]	NUMBER OF STOCKS	BETA[4]	MAXIMUM DRAW DOWN
11.5%	24	0.63	-23.1%

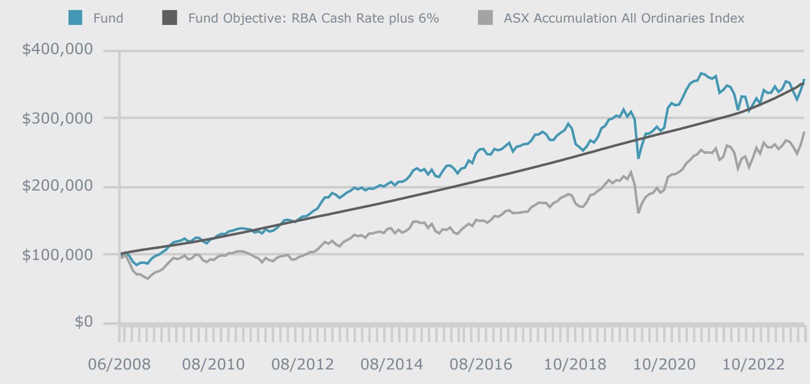
PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 31 Dec 2023[1]

	1 MTH	1 YEAR	3 YEARS P.A.	5 YEARS P.A.	10 YEARS P.A.	SINCE INCEPTION P.A.
Australian Equities Fund	5.1%	11.3%	3.6%	7.2%	6.1%	8.6%
Fund Objective: RBA Cash Rate plus 6%	0.8%	9.8%	7.7%	7.3%	7.6%	8.4%
ASX Accumulation All Ordinaries Index	7.4%	13.0%	8.9%	10.7%	8.2%	6.9%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

BHP Group Ltd	Materials
CSL Ltd	Health Care
Evolution Mining Ltd	Materials
Medibank Pvt Ltd	Financials
National Australia Bank Ltd	Financials
nib holdings Ltd/Australia	Financials
ResMed Inc	Health Care
SG Fleet Group Ltd	Industrials
Telstra Group Ltd	Communication Services
Woolworths Group Ltd	Consumer Staples

SECTOR BREAKDOWN

Consumer Discretionary	11.1%
Consumer Staples	6.7%
Financials	24.9%
Health Care	16%
Industrials	4.1%
Materials	13.1%
Real Estate	2.3%
Communication Services	7.2%
Utilities	3.4%
Cash	11.2%

CAPITALISATION BREAKDOWN

ASX 1-50	52.4%
ASX 51-100	13.7%
ASX 101-300	10.8%
All Ordinaries	5.2%
Non ASX	6.7%
Cash	11.2%

CUSTOM SECTOR BREAKDOWN

Defensive	49.1%
Financials	19.8%
Consumer Discretionary	10.1%
Resources	9.8%
Cash	11.2%

A STRONG DECEMBER DELIVERS SOLID DOUBLE DIGIT RETURNS FOR CALENDAR 2023 – AHEAD OF CASH PLUS 6% BENCHMARK

COMMENTARY

The Fund generated an encouraging +5.1% return in December. By way of comparison, the (annual) return of the RBA cash rate plus 6% equated to approximately +0.8% for the month, whilst the Australian stock market increased by +7.4% over the month. For the 12 months ended December 2023, the Fund generated a return of +11.3%, exceeding the benchmark of RBA cash rate plus 6% return of +9.8% whilst the Australian stock market returned +13.0% over the same period.

We are pleased to be able to report a solid double digit return for the Fund over the calendar year, in excess of the Fund's benchmark. Just as pleasing has been the behaviour of the Fund throughout the year – participating in periods of market strength, proving more resilient in the weaker months, and importantly generating its return for the year at a lower level of volatility than the market. Despite a rising interest rate environment, we remain confident in the strategy which since inception has delivered a superior outcome for our investors (+8.6% after all fees and charges) than the market (+6.9%), and the cash plus 6% benchmark return of 8.4% over the same period.

Relative to the market's performance, we identify two primary factors for the modest performance gap in the calendar year – the Fund's ongoing "underweight" position in the Resources space and its relative "overweight" position in Resmed. Energy and Materials comprise approximately 29% of the ASX 200 and rose circa 15% in the 12 months to December 23, contributing over 400 bps to the market's 13% total return. The Fund's exposure to these sectors has approximated 9% over the same period, attributable to its relatively smaller holding in BHP and separate position in Evolution Mining. We continue to resist using our investors' funds to manage our business risk of underperformance by taking on large market weight related positions in companies that have very difficult to predict future cash flows.

The largest notable stock detractor in the period was a decline in value of our holding in Resmed. Share price weakness, which started in August and continued through to October, was driven by two primary factors. Firstly, a lack of operating leverage in the FY23 results, where strong top-line growth failed to translate fully to profit growth – a dynamic that disappointed us but, understanding the dynamics, we remain confident in our longer-term cash flow projections. The second factor relates to the broader adoption of a drug (GLP-1 RA) for the treatment of obesity, which is recognised as a significant contributor to sleep apnoea. We believe the threat this poses to ResMed's potential target market has been significantly overestimated due to a number of factors including cost of treatment, various side effects, and significant weight regain following withdrawal from the drug. Given what we viewed as solid underlying fundamentals and an overreaction to GLP-1, we added significantly to our RMD holdings on the weakness during the period and are encouraged by the 20%+ recovery in the shares from their October lows.

On the positive side, the Fund benefited from a combination of i) strong performances from long term core portfolio holdings, such as Super Retail Group, SG Fleet, Aristocrat, and Accent Group; ii) reward for its conviction with previous underperformers such as Ryman Healthcare and Evolution Mining; and iii) a number of new contributors in the calendar year, notably James Hardie Group and CSR. At a sector level, Discretionary Retail (SUL, AX1, JBH) was once again the largest positive contributor for the Fund over the calendar year, with solid contributions also from Financials (NAB, CBA, MQG, ANZ), Health Insurers (MPL, NHF) and Materials (BHP, EVN).

Super Retail Group was once again the largest positive contributor in the period. Certainly, the consumer remaining stronger for longer has been a key element to its ongoing share price performance, however, we believe fundamental improvements made to the business prior to and during the COVID period have significantly added to the quality of the underlying business. These improvements have manifested themselves in additional growth channels, as well as increased resilience of existing channels, the ability to retain a higher portion of the gross margin gains through COVID, more efficient cost of doing business, stronger operating cash flows, and greater cash returns to shareholders. Whilst valuation is beginning to look more appropriate, we think operational momentum remains strong and believe it is well placed to manage the increasingly difficult spending environment facing households in early 2024.

James Hardie was another meaningful contributor for the year. We accumulated a position during 2022, attracted by their market-leading product, highly efficient manufacturing operation, and superior distribution network, all coupled with an undemanding valuation. Some initial turbulence for the new management team following the sharp increase in U.S. mortgage rates during 2022 provided an opportunity to build our position, and the team demonstrated remarkable stewardship in 2023 – adeptly controlling fixed costs and enhancing operating margins amidst falling volumes. This strong performance restored market confidence in the resilience of the business and led to a favourable re-rating that exceeded our expectations, so we were pleased to take profits and exit our position entirely.

The thematic around a structural shortage of housing – a key element of the James Hardie investment thesis – has become just as great an issue in Australia as it was in the United States. Through CSR, we now have exposure to a portfolio of leading building products in Australia, as well as a vast property portfolio, that we have been able to accumulate at what we believe are attractive valuation levels.

Finally, core holdings in large cap defensive names Telstra and CSL both contributed positively to performance, although were not amongst the leading contributors in the period. Telstra's earnings momentum remains solid, in particular, the core mobile division and the inflation linked recurring NBN income stream (combined c85% of total valuation). However, the decision by management not to monetise part of the infrastructure business disappointed elements of the investor base, whilst rising bond rates domestically and abroad put downward pressure on sector valuations. CSL experienced similar headwinds in the period to Resmed – although has more quickly recovered much of the initial sell down given positive comparisons with global peers and an arguably lower potential exposure to GLP-1 drug cohort. We continue to have high levels of confidence in both investments and following a more subdued contribution in 2023, believe their large, predominately stable cash flows are well positioned to driveperformance in the medium term.

In terms of positioning going forward, despite the economy remaining stronger for longer than many had anticipated we continue to retain a level of caution in our outlook for 2024. We have worked hard to improve the liquidity of the Fund and retained a focus on well managed defensive cash generators. Cash levels continue to remain healthy at c11% providing us with stability and downside protection, a decent positive return given elevated cash rates, and the capacity to invest when we assess the time is right. At December 31 the Fund had no active put options in the portfolio, and whilst they remain an option for downside protection, we view our cash holdings as playing a more meaningful defensive role in the near term. During the course of 2023, the cost of put option protection was a net negative contributor to Fund performance (the cost of insurance).

Over the past 18 months, we have observed the negative impact of the higher cost of money on valuations of long duration assets. The resulting shift in the market environment, from one driven by virtually free money and near zero discount rates, to a more normal level of interest rates today has in our view resulted in more rational valuations overall. More specifically, we believe the relative valuation appeal has shifted from business models that generate a significant portion of their profits/cash flows in the future, back towards those that are generating profits/cash flows today. Such a dynamic is better aligned with our strategy and positioning, and we look forward to the underlying cash flows of our investments asserting themselves on valuations in the near term.

We continue to invest with a view that interest rates will remain elevated for the foreseeable future. Our view is based on the premise that inflation, whilst off its peak, is likely to remain elevated throughout 2024. Whilst some of the imported inflationary forces of 2022 have waned, domestically driven forces remain very much at play (high levels of employment/wage growth, elevated migration, services inflation, and an ongoing lagged recovery of cost pressures from 2023). As such, it is difficult for us to see downside to the RBA cash rate so long as our inflation outlook is 4% or above.

As we enter 2024, we have observed a wide range in outlook commentary – from those who believe the worst is now behind us, to those that believe the pain is only just beginning. Despite an elevated level of uncertainty in markets, we remain as focused as ever on our primary objectives of capital preservation and generating a reasonable real return for our investors. We continue to believe this is best served by a disciplined approach and consistent investment methodology. A variety of good businesses run by honest and competent management teams at the right price will create a well-diversified portfolio of ever-growing cash earnings streams.

FEATURES

APIR CODE	PCL0005AU
REDEMPTION PRICE	A$ 1.8046
FEES *	Management Fee: 1.025% Performance Fee: 10.25%
MINIMUM INITIAL INVESTMENT	A$10,000
FUM AT MONTH END	A$ 623.54m
STRATEGY INCEPTION DATE	1 July 2008
BENCHMARK	The RBA Cash Rate Target plus Australian equity risk premium.

FUND MANAGERS

Rhett Kessler
CIO and Senior Fund Manager

Anton du Preez
Deputy CIO and Fund Manager

1. Net performance figures are shown after all fees and expenses, and assume reinvestment of distributions. The benchmark of cash rate plus 6% p.a. is included in the chart as it relates to the Fund's investment objective and performance fee. The Fund may invest up to 100% of its assets in equity securities. The greater risk of investing in equities is reflected in the addition of a margin above the cash rate. No allowance has been made for buy/sell spreads. Please refer to the PDS for information regarding risks. Past performance is not a reliable indicator of future performance, the value of investments can go up and down.
2. Inception 1st July 2008.
3. Annualised standard deviation since inception.
4. Relative to ASX All Ordinaries Index. Using daily returns.
*(including GST, net of RITC) of the increase in net asset value subject to the RBA Cash Rate & High Water Mark. For further information regarding fees please see the PDS available on our website.

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