APIR Code: ECL8388AU, ECL3306AU

Ellerston Global Mid Small Cap Fund

Performance Report, February 2021

Investment Objective

To outperform MSCI World Mid Cap NR (AUD) benchmark by 3% over a rolling 5 year period on a net of fees basis, with a focus on risk management and capital preservation.

Investment Strategy

The Fund's investment strategy is to construct a concentrated portfolio of global mid small securities using the Manager's distinctively contrarian high conviction, benchmark independent investment approach. The Manager believes that the trade-off between risk and potential returns is improved by implementing highest conviction ideas from a filtered universe of securities that are in a period of "price discovery" and offer the best risk/reward.

Key Information

Strategy Inception	1 March 2017
Portfolio Manager	Bill Pridham
Class A Application Price	$1.3971
Class A Net Asset Value	$1.3936
Class A Redemption Price	$1.3901
Class B Net Asset Value	$1.3119
Class B Redemption Price	$1.3086
Liquidity	Daily
No Stocks	20 - 40
Management Fee (Class A)	0.75%
Performance Fee	10%*
Buy/Sell Spread	0.25%/0.25%

*10% of the investment return over the benchmark return (MSCI World Mid Cap Index (AUD)), after recovering any underperformance in past periods

Performance Summary

Performance	1 Month	3 Months	6 Months	1 Year	3 Years (p.a.)	Since Inception (p.a.)
Class A^	1.66%	10.42%	20.13%	23.70%	16.20%	16.69%
Benchmark*	2.79%	3.22%	14.89%	10.70%	9.87%	11.22%
Alpha	-1.14%	7.20%	5.23%	13.01%	6.33%	5.47%

Performance	1 Month	3 Months	6 Months	1 Year	3 Years (p.a.)	Since Inception (p.a.)
Class B^	1.71%	11.34%	21.08%	-	-	19.37%
Benchmark*	2.79%	3.22%	14.89%	-	-	13.14%
Alpha	-1.09%	8.12%	6.19%	-	-	6.23%

^ The net return figure is calculated after fees & expenses. Past performance is not a reliable indication of future performance
* MSCI World Mid Cap Index (AUD)
Class B Inception Date is 18 August 2020

ESG in Focus

According to a Deloitte survey, corporations are beginning to consider a broader set of stakeholders which reflects not just economic performance but also societal impact. Approximately 70% of C-suite executives surveyed believe that long term business success requires the integration of Industry 4.0 technologies into their organisations.

Industry 4.0 is the marriage of physical assets and digital technology and with this data in hand, corporations are more productive, more innovative and better equipped to operate in a circular economy which according to the World Economic Forum (WEF) "promotes the elimination of waste and the continual safe use of natural resources, offers an alternative that can yield up to $4.5 trillion in economic benefits to 2030."

A recent report from the WEF shows how the power of Industry 4.0 can be harnessed to improve the way materials are managed and steer society away from antiquated take-make-waste models towards sustainable, circular solutions.

We consider the shift to circular manufacturing, which requires a connection between physical and digital assets for effective measurement and therefore management, as a nascent yet powerful megatrend which will gain more prominence over the next several years.

Portfolio Commentary

February was a key month in reminding the markets that higher growth will result in higher inflation and global bond yields kicked up as a result. The US 10yr started the month at 1.07%, and with further evidence through reporting season of a tight supply chain and associated inflationary impact on company input costs, the 10yr finished the month above 1.40% and is currently just under 1.60% at time of writing.

The market is undergoing a regime change where over the past few years lower growth and lower rates benefited large cap growth and momentum stocks while now we are transitioning to higher growth (early-stage recovery), higher rates which should see mid/small cap stocks, industrials and financials continue to be relative winners.

The Ellerston Global Mid Small Cap Fund (Class A) increased 1.7% net during the month with positive equity performance of 2.7% impacted by about 100bps from a stronger Aussie dollar. The MSCI World Mid Cap (AUD) Index increased by 2.8% over the same period.

The portfolio's top three contributors Tempur Sealy, Comerica and MIPS added 194bps to performance while Anritsu, Health and Happiness and LiveRamp detracted 141bps. The Fund had 16 portfolio companies reporting quarterly results or trading updates in February with the bulk of reporting season now complete.

Sensata finished off the year with its first quarter of revenue growth in several quarters as global auto and heavy vehicle markets appear to have bottomed after a very difficult 2020. As content per vehicle continues to increase, Sensata is outperforming its end markets and Q420 was quite stellar with almost 10% outgrowth during the quarter. Management guided to 2021 in line with market expectations despite increased spending on future growth initiatives. While shorter term holders of the stock sold it down 4.5% over the next couple of days, we used the weakness as an opportunity to accumulate a larger position.

Tempur Sealy also delivered a very strong finish to 2020 with full year revenues up 18% and EBITDA up an even more impressive 53.5%. We had been concerned about pull forward as the business did benefit from increased home spending during the year however Management expects growth to continue with 15-20% revenue and about 20% EBITDA growth slated for 2021. This will come without much of a growth contribution from Europe, as these economies are slower to recover post Covid and should benefit the business more in 2022. The Board initiated a maiden dividend and increased its buyback authority as FCF is coming in very strong.

Anritsu is one of three players globally providing testing for next generation 5G deployments and while the need for 5G and its rollout has become even more pronounced since the pandemic, activity levels have been constrained somewhat on the back of lockdowns. Management upgraded full year earnings expectations however the outcome has become more Q4 weighted which adds a layer of risk to the result. With the business trading on an undemanding earnings multiple for exposure to the long tailed secular 5G tailwind, we remain convicted holders in the business.

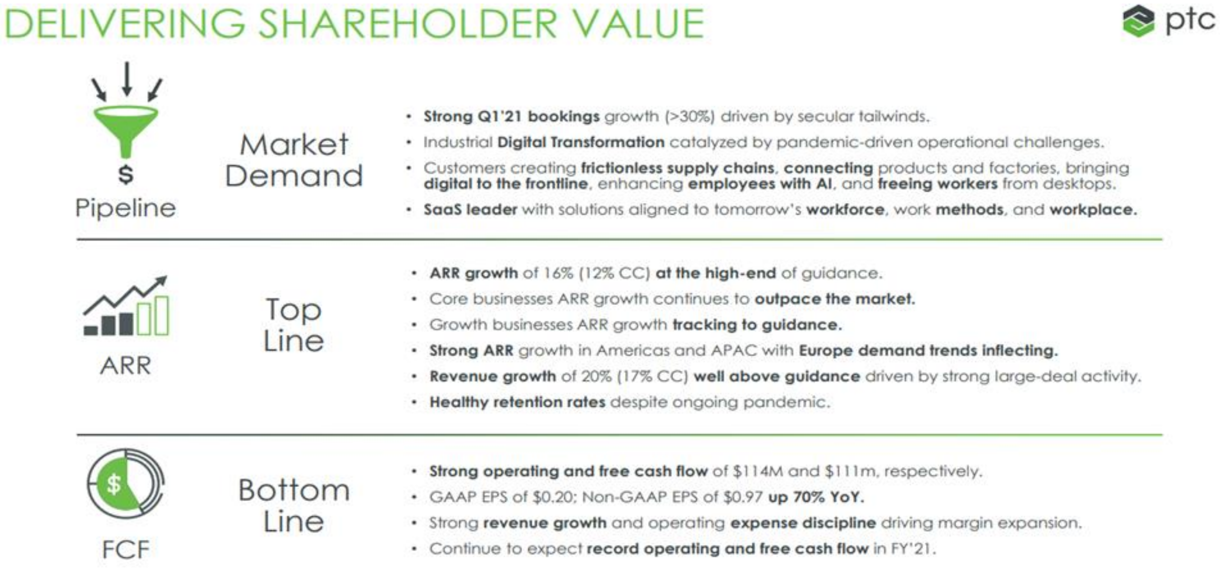
STOCK IN FOCUS: PTC Inc (PTC US, $13.8b Market Cap)

PTC is a global leader in Computer Aided Design (CAD) and Product Lifecycle Management (PLM) software products and the leader in providing solutions serving the high growth Industrial IoT and Augmented Reality (AR) markets associated with Industry 4.0. The CAD and PLM market is dominated by four global players, including PTC which has demonstrated continued market share gains as it excels in helping customers design, manufacture, operate and service products across multiple industries. While it delivers its solutions via a software stack, the underlying business is really driven by industrial activity and innovation.

PTC has three significant partnerships with industry leaders including Microsoft, Rockwell Automation and Ansys. We consider its partnership with Microsoft as the largest driver of near-term revenue contribution as PTC's ThingWorx® Industrial Innovation Platform is now available on the Microsoft Azure cloud platform as its preferred cloud platform.

The business has really transformed over the past few years as Management made the hard decision to move from a perpetual licence model to a recurring revenue subscription product offering. This had the result of constraining top line growth and margins in the early days however in FY20 the model inflected with EBIT margin increasing almost 900bps and annual recurring revenue growing double digits despite the impact of the global pandemic.

FY21 has started out well for the business with Q1 revenue and EBIT up 20.5% and almost 65% respectively prompting Management to upgrade guidance quite materially compared with its last full year expectation. Recent acquisitions including OnShape and Arena are expected to drive outsized growth as the combination represents a powerful pure-SaaS solution that's number one in technology, customers and revenue.



Source: PTC Q121 Earnings Presentation

Its core CAD and PLM business is expected to grow high-single digit to low double-digits over the coming years while the higher growth Augmented Reality group is expected to come in between 25-30% and represent close to a third of the total business in a few years. This should drive operating leverage across its "build it once, sell it many times" software stack with Management anticipating a further 700bps margin expansion over the coming years which subsequently drives 25-30% FCF growth for us as shareholders.

At the time of writing, PTC is trading at $125.50 which represents a forward PE of 28x and EV/EBITDA of 15.4x which we consider solid value for a business growing 30%+ over the next few years and roughly half the multiple as its best comparable Autodesk. As FCF continues to build on the balance sheet (excluding any further M&A) we anticipate the balance sheet to be in a net cash position in two years which provides significant capital allocation optionality for the group.

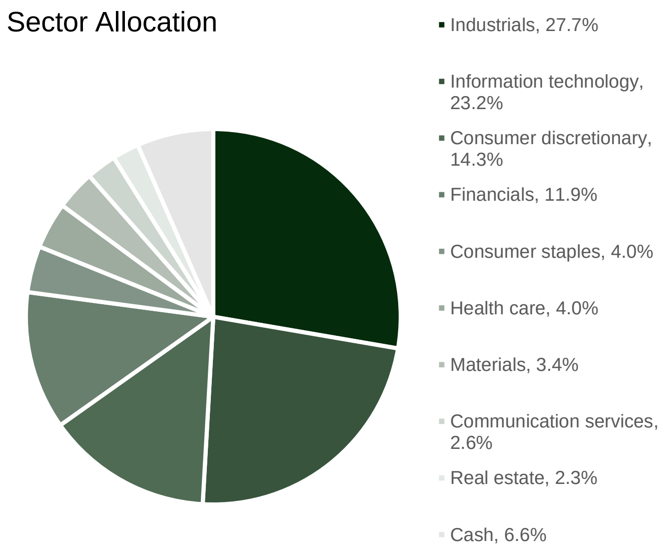
In the interest of keeping you updated on the performance and positioning of your holding in the Fund, we are hosting an investment update on Tuesday 16th March 2021 at 12pm AEDT, for which you can register here.

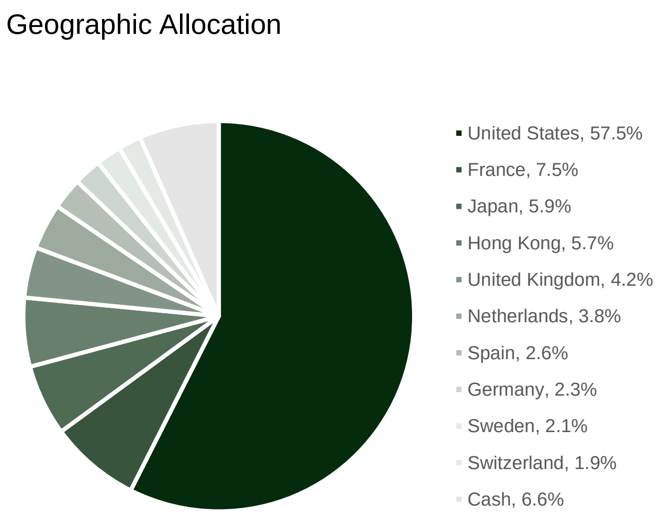
Kind regards,
Bill Pridham

Portfolio Characteristics

Holdings

Top 10 holdings	Country	Sector	%
Sensata Technologies	United States	Industrials	6.0%
PTC	United States	Information Technology	5.4%
Flex Ltd	United States	Information Technology	4.9%
Tempur Sealy International	United States	Consumer Discretionary	4.1%
Option Care Health	United States	Health Care	4.0%
Anritsu Corporation	Japan	Information Technology	4.0%
Bureau Veritas	France	Industrials	4.0%
SEB	France	Consumer Discretionary	3.5%
Techtronic Industries	Hong Kong	Industrials	3.4%
Comerica	United States	Financials	3.4%





Source: Ellerston Capital

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Find out more

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