Ellerston Asia Growth Fund

Monthly Newsletter, December 2022

Investment Objective

To outperform the MSCI Asia Ex Japan (non-accumulation) (AUD) benchmark on a net of fees basis, with a focus on capital growth and downside protection.

Investment Strategy

The Fund's investment strategy is to provide access to a high quality portfolio of primarily large cap Asian Companies using the Manager's distinctively high growth, high conviction and benchmark independent investment approach.

The Manager believes that the trade-off between risk and potential returns at the portfolio level is improved by implementing highest conviction ideas from a filtered universe of securities that offer the best risk/reward.

Key Information

Strategy Inception^^	4 January 2017
Portfolio Manager	Fredy Hoh
Application Price	$0.8131
Net Asset Value	$0.8111
Redemption Price	$0.8091
Liquidity	Daily
No Stocks	34
Management Fee	1.00%
Performance Fee	15%
Buy/Sell Spread	0.25%/0.25%

PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	2 Years (p.a.)	3 Years (p.a.)	Since Inception ^^ (p.a.)
Net^	-0.95%	3.88%	-5.70%	-19.06%	-11.49%	-4.22%	3.09%
Benchmark*	-1.63%	5.22%	-3.86%	-15.89%	-8.57%	-2.30%	4.12%
Alpha	0.67%	-1.34%	-1.84%	-3.17%	-2.91%	-1.92%	-1.03%

^ The net return figure is calculated after fees & expenses. Past performance is not a reliable indication of future performance

* MSCI Asia ex Japan (non-accumulation) (AUD)

Commentary

Ellerston Asia Growth Fund (EAGF) was down 1.0% (net) in December versus the MSCI Asia ex Japan (MXASJ) Index which was down 1.6%.

December saw Asia led by China outperform developed markets (DM). The MSCI China Index was up 5.2% during the month compared to the S&P 500 and ASX 200 which were down 5.8% and 3.2% respectively as hawkish rhetoric most notably from the US Federal Reserve (Fed) drove a pullback in DM equities. Since the late October sell-off in Chinese equities, MSCI China has outperformed the S&P 500 and ASX 200 by 36% and 33% respectively. We wrote in our last newsletter that an inflection point in the outlook for Chinese equities had likely been established due to the dramatic shift by policymakers towards restoring economic growth. The likely growth divergence between China and DM in 2023 could therefore drive continued outperformance of MSCI China in the coming months.

China Reopening, Housing Support and Regulatory Easing

During the month, there were further concrete signs supporting a cyclical upturn for Chinese equities. Firstly, policymakers scrapped COVID testing requirements, contact tracing and quarantine measures for both infected residents and inbound travelers. We view these adjustments as an informal abandonment of China's draconian zero-COVID policy. This therefore paves the way for China to enjoy a reopening driven boost similar to what has played out in other countries around the world. An unintended consequence of the rolling COVID disruptions over the past 3 years is that Chinese residents have saved a significant portion of their incomes. It is estimated that up to RMB3.5trillion (~A$750bn) of excess savings could be unleashed back into the economy on goods and services. This is a powerful secular tailwind for most of our ecommerce (Alibaba, Meituan) and consumption related investments (Mengniu, Moutai, China Tourism Group). Although the near term recovery could be hampered by the sudden surge in case and mortality numbers, we believe this is already reflected in current valuations with the Hang Seng Index still trading at 10x forward PE. Earnings growth and earnings revisions meanwhile have already started turning positive particularly for the China internet companies. As such, we continue to see significant long term upside for our China investments and will be inclined to look through any near term COVID related disruptions.

Aside from the shift in COVID policy, there were also positive developments on the property and regulatory fronts. Specifically, two key takeaways from the Central Economic Work Conference held in December were the pledges by top leadership to stabilize the property sector and to support the platform economy. Encouragingly, we have seen tangible policy action to back up these commitments with the government announcing a ~RMB1tn (A$210bn) rescue package for the property sector in November. Meanwhile, regulators have restarted the approval of foreign internet games for the first time since 2021. Further helping to ease the regulatory overhang for Chinese internet companies was the audit agreement reached between China and the US which alleviates the delisting risk for ADRs.

In aggregate, a China reopening, property sector stabilisation and removal of major regulatory risks provides a more attractive backdrop for investing in China. With valuations still at depressed levels, we took the opportunity to increase our China exposure during December and will use any near term pullbacks to further add to our portfolio.

Portfolio Performance Summary

China and Korea were the largest contributors to alpha during the month. Whilst, India and Singapore were the major detractors. At a sector level, Consumer Staples and Consumer Discretionary were the biggest contributors to relative performance. Meanwhile, Healthcare and Energy were the worst performers.

At a company level, Kweichow Moutai, AIA and By-Health were the biggest contributors to relative performance during the month. All three names are key beneficiaries of a China reopening and had been unfairly sold off throughout 2022 amid COVID uncertainties.

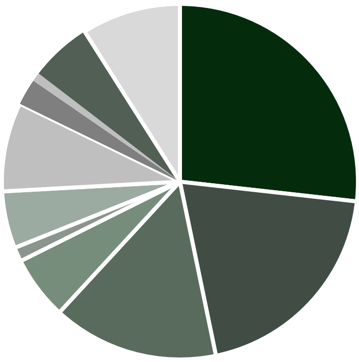
Samsung Electronics and CSPC Pharmaceuticals were the biggest drags on alpha. Samsung corrected in-line with the global sell-off in growth stocks. Fundamentally, the company is also navigating a temporary downturn in the memory market due to excess inventory. However, with peers such as Micron and SK Hynix already committing to cut capex for 2023, we believe the memory cycle is likely to bottom sometime in 1H2023. Samsung meanwhile is trading on 1.1x P/B and has KRW130tn (or A$150bn) of cash on balance sheet, which is equivalent to 35% of its market cap. We believe rational behavior from industry participants, trough valuations and a fortress balance sheet will limit further downside in the company's share price. CSPC's share price pulled back during the month as the commercialization outlook of its mRNA based COVID vaccine faded with the sudden U-turn in China's zero-COVID policy. However, our investment thesis on CSPC remains intact and we expect the stock to re-rate as the company transitions its product portfolio from generic drugs to innovative drugs. The company also recently upgraded its 2023 outlook on the back of its strong existing product portfolio and trades on an undemanding 13x forward PE with an expected earnings growth of 10-15%.

As always, if you have any questions regarding any aspect of the Fund or the portfolio, please feel free to contact us at info@ellerstoncapital.com.

Kind Regards,
Fredy Hoh

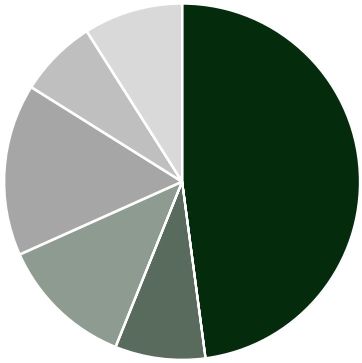
PORTFOLIO CHARACTERISTICS

SECTOR ALLOCATION



Source: Ellerston Capital.

GEOGRAPHIC ALLOCATION



Source: Ellerston Capital.

TOP 10 HOLDINGS

Company	Country	Weight
TSMC	Taiwan	8.4%
Samsung	Korea	6.5%
Tencent Holdings	China	5.8%
Reliance Industries	India	5.2%
AIA Group	Hong Kong	5.1%
DBS Group	Singapore	4.4%
Alibaba Group	China	4.2%
ICICI Bank	India	3.5%
Kweichow Moutai	China	3.2%
China Mengniu Dairy	China	3.2%

Regulatory Guide (RG240) Fund Disclosure Benchmark – Periodic Reporting (monthly)

- **Net Asset Value of the Fund and Redemption Price of Units**

Please refer to details on page one.

- **Any changes to key service providers including any change in related party status**

There have been no changes to key service providers, including any change in related party status.

- **Net returns after fees, costs and relevant taxes**

Please refer to details on page one.

- **Any material changes to the Fund's risk profile and strategy**

There have been no changes to the Fund's risk profile and strategy.

- **Any material changes related to the primary investment personnel responsible for managing the Fund**

Please refer to details on page one; there have been no changes to the primary investment personnel responsible for managing the Fund.

Contact Us

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Find out more

Should investors have any questions or queries regarding the Fund, please contact our Investor Relations team on **02 9021 7701** or **info@ellerstoncapital.com** or visit us at **ellerstoncapital.com**

All holding enquiries should be directed to our register, Automic Group on **1300 101 595** or ellerstonfunds@automicgroup.com.au

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