

Ellerston Asia Growth Fund

Monthly Newsletter, March 2023

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-Jan-17
Portfolio Manager	Fredy Hoh
Application Price	\$0.8446
Net Asset Value	\$0.8425
Redemption Price	\$0.8404
Liquidity	Daily
No Stocks	36
Management Fee	1.00% p.a.
Performance Fee	15%
Buy/Sell Spread	0.25% on application 0.25% on redemption
Distribution Frequency	Half Yearly (i.e. June & December)

** Of the investment return above the benchmark, after recovering any underperformance in past periods

Performance Summary

Performance(%)	1 Month	3 Months	6 Months	1 Year	3 Years (p.a.)	5 Years (p.a.)	Since Inception (p.a.)*
Net^	3.25	3.95	7.98	-4.70	-1.02	0.04	3.61
Benchmark*	4.00	5.39	10.90	-0.24	1.68	0.60	4.83
Alpha	-0.76	-1.44	-2.91	-4.46	-2.71	-0.56	-1.22

^ 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 up 3.25% (net) in March versus the MSCI Asia ex Japan (MXASJ) Index which was up 4.0%.

March was a volatile month for global equity markets with the banking turmoil in the US and Europe weighing on returns early in the month, followed by a strong rebound after measures to stabilise the financial sector were announced.

Banking turmoil in the US and Europe

The collapse of Silicon Valley Bank, Silvergate Capital and Signature Bank in early March sent shockwaves through financial markets and led to concerns of an imminent financial crisis. US authorities however have acted swiftly to address near contagion risk and restore confidence in the sector through additional liquidity via the Bank Term Funding Program and the potential extension of deposit guarantees. Furthermore, there were idiosyncratic reasons behind the failure of all three banks, most notably the concentration towards riskier areas such as venture capital and crypto currency. This, together with duration mismatches between assets (i.e. held to maturity instruments) and liabilities (i.e. uninsured deposits) that were exposed by the sharp rise in interest rates over the past 12 months, created unique challenges for these smaller 'niche' banks. As such, we do not view these bank failures as another Lehman Brothers moment and believe systematic risks are well contained.

Further compounding stresses in the global banking system was the collapse of Credit Suisse, which had reportedly run into liquidity issues. Again, contagion risk was quickly addressed when UBS agreed to acquire Credit Suisse, albeit at a steep discount.

Although concerns around the banking sector have eased in recent days, the potential implications from these events on credit conditions and economic growth have yet to fully play out. As such, we believe banking system risks for developed markets are likely to remain an overhang in the coming months. Asia is relatively better placed due to differences in banking regulations and monetary policies. Furthermore, Asian banks have smaller investment books than their US peers and are much better capitalised than during previous financial crisis.

This relative difference further strengthens the case for Asian equities led by China to outperform in 2023. Within Asia, we prefer companies with strong balance sheets and free cash flow generation such as TSMC, Kweichow Moutai and China internet companies. These businesses are unlikely to be impacted by distress in the banking system as they require little external financing.

Asia as a relative safe haven

We have previously written about the case for Asian equities outperformance driven by less restrictive monetary policies, China's reopening and positive spill over benefits for the region and more attractive risk/reward. Within Asia, China and India are our two largest country exposures. This positioning is underpinned by strong relative growth prospects, with China (+5.2%YoY) and India (+5.9%YoY) likely to account for half of global GDP growth in 2023 according to the IMF.

On China specifically, the economic recovery since reopening remains positive particularly for the services sector (March PMI of 57.8). There have also been green shoots for the property sector, with residential property sales returning to positive growth throughout March. This is particularly important given the property sector accounted for ~50% of local government revenues and ~70% of household wealth. Meanwhile, other measures such as loan growth and retail sales have also shown an improving trend in recent months. These improvements are likely to be sustained given the policy setting environment continues to be supportive. Indeed during March, the People's Bank of China cut the reserve requirement ratio for banks by 25bps in order to inject more liquidity into the economy. Furthermore, a key takeaway from the 'Two Sessions' in March was the positive comments from top government officials around growth, the private sector and property. This suggests further incremental easing measures are likely in the coming months, which will help to deliver the 'around 5%' GDP growth target for 2023. Equity valuations remain attractive with the MSCI China trading on 10.6x forward PE.

We continue to take a diversified approach to investing in China with a preference for high quality companies that are either supported by government policies or operating in policy neutral sectors. We also own companies that are regulated by the Government but remain strategically important such as the Chinese internet names.

Portfolio Performance Summary

Taiwan and Indonesia were the largest contributors to alpha during the month. Whilst, China and Singapore were the largest detractors. At a sector level, Financials and Consumer Discretionary were the biggest contributors to relative performance. Meanwhile, Consumer Staples and Communication Services were the worst performers.

At a company level, Alibaba, Bank of Mandiri and Samsung Electronics were the biggest contributors to relative performance during the month. The Alibaba share price was boosted by the announcement that the company will be split into 6 separate business units which could pave the way for individual IPOs in the coming years. We view the restructure positively given it will help to unlock embedded value within the company. The expected improvements in operating performances of each independent business unit from more focused management teams and removal of business friction should eliminate the 'conglomerate discount' that has historically existed for the company. Indeed, Alibaba continues to trade on 8.5x (ex cash) forward PE, which looks attractive against earnings growth of ~15% CAGR over the next 3 years. Bank of Mandiri meanwhile saw inflows ahead of its proposed stock split. Finally, the Samsung Electronics share price bounced as its competitor Micron reaffirmed previously announced capex and production cuts. This together with tentative signs of a bottoming in TV and PC demand could help to stabilize memory prices in the coming quarter.

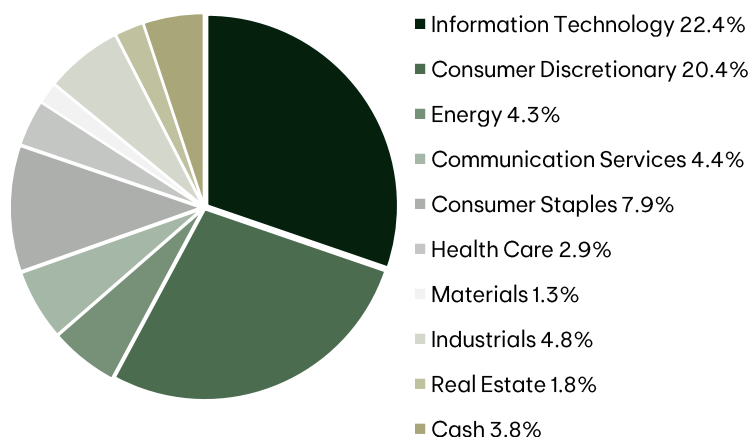
Mengniu Dairy and DBS were the biggest drags on alpha. Mengniu was sold off during the month after management provided softer than expected revenue guidance for 2023. We believe expectations of 'teens' revenue growth and 30-50bps of margin expansion could prove conservative. Meanwhile, the company trades on an undemanding 15x forward PE. The DBS share price was negatively impacted by the banking sector turmoil that played out during the month. We note however that DBS has no direct exposure to the troubled banks and the company has healthy liquidity coverage (>145%) and capital ratios (CET 1 of 14.6%).

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

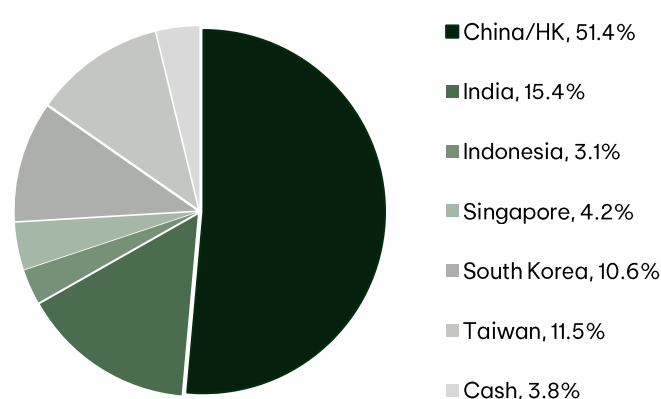
Portfolio Characteristics

Sector allocation



Source: Ellerston Capital.

Geographic allocation



Source: Ellerston Capital.

TOP 10 HOLDINGS

Company	Country	Sector	Weight
Taiwan Semiconductor Manufacturing Co., Ltd.	Taiwan	Information Technology	9.6%
Samsung Electronics Co., Ltd.	South Korea	Information Technology	7.5%
Alibaba Group Holding Limited	China	Consumer Discretionary	5.8%
AIA Group Limited	Hong Kong	Financials	4.7%
Tencent Holdings Ltd.	China	Communication Services	4.4%
Reliance Industries Limited	India	Energy	4.3%
DBS Group Holdings Ltd	Singapore	Financials	4.2%
HDFC Bank Limited	India	Financials	3.7%
Kweichow Moutai Co., Ltd.	China	Consumer Discretionary	3.4%
PT Bank Mandiri (Persero) Tbk	Indonesia	Financials	3.1%

Source: Ellerston Capital.

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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