

Ellerston Asia Growth Fund (Hedge Fund)

Monthly Newsletter, October 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 Asian Companies using the Manager's distinctive high conviction and benchmark independent investment approach. The Manager identifies those Asian Companies by filtering the investment universe to identify those that are likely to offer an attractive risk/reward profile.

The strategy leverages the Manager's broader experience investing in global markets to identify companies with superior growth characteristics, sustainable earnings and quality management.

Key Information

Portfolio Manager	Fredy Hoh
Application Price	\$6.0066
Net Asset Value	\$5.9916
Redemption Price	\$5.9766
Current Total NAV	\$43,915,183
Liquidity	Daily
No Stocks	31
Buy/Sell Spread ¹	0.25% on application 0.25% on redemption
Distribution Frequency	Half Yearly (i.e. June & December)
Management Fee ²	0.75% p.a.
Performance Fee ³	10%

1. Applicable only to investors buying and selling directly with the Manager.
2. The Manager is waiving the management fee for the first year following quotation of units on the ASX.
3. Of the investment return above the benchmark, after recovering any underperformance in past periods.

Performance Summary

Performance	1 Month	3 Months	FYTD	1 Year	Since Inception ^{^^} (p.a.)
Net [^]	-1.22%	-6.21%	-2.73%	-	-2.41%
Benchmark*	-2.05%	-7.23%	-3.15%	-	-3.80%
Alpha	0.83%	1.02%	0.42%	-	1.39%

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

^{^^} The Inception Date is 01/06/2023. The Ellerston Asia Growth Fund (Hedge Fund) was formerly known as the Ellerston Asia Growth Fund, with a strategy inception date of 04/01/2017. The performance was reset following a restructure of the fund into an exchange traded managed fund which took effect on 01/06/2023. Performance is cumulative since inception.

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

The Ellerston Asia Growth Fund (Hedge Fund) (EAFZ) was down -1.22% (net) in October versus the MSCI Asia ex Japan (non-accumulation) (AUD) (MXASJ) Index which was down -2.05%.

Market Commentary

Global markets were negatively impacted during October by the resurgence of the Israel/Palestine conflict and US bond yields rising above 5% for the first time since 2007. These two events put further upside pressure on the US dollar, which rose to near 12-month highs during the month. Historically, a stronger USD has been negative for flows into Emerging Markets and indeed this was again a headwind throughout October. All Asian indices, with the exception of Malaysia (+1.3%) were down during the month, with Korea (-7.6%), Thailand (-6.1%) and Philippines (-5.5%) the major underperformers.

MSCI China was also down -4.4% in October on the back of mixed economic data and news flow. Although September quarter GDP growth of +4.9% surprised to the upside, the latest PMI reading (50.6) and the potential default of high profile developer Country Garden drove further investor selling. The Government took further measures during the month to stabilise both the economy and capital markets. Firstly, it raised its 2023 budget deficit target from 3.0% to 3.8% of GDP. This is the first time China has raised its budget deficit since 2000 and signifies the Government's intention to boost the economy into year end. Secondly, China's sovereign wealth fund announced the purchase of domestic equities throughout October in order to support the market. This was the first time the 'national team' has publicly stepped into the local equities market since 2015. Another positive over the past month has been the de-escalation in US/China tensions with Presidents Xi and Biden agreeing to meet at the Asia-Pacific Economic Cooperation Summit in November.

We continue to see the prospects of further positive stimulus, a more stable geopolitical environment, improving economic data and earnings and historically cheap valuations as providing an attractive risk-reward backdrop for investing. As such, we maintain our overweight position in China/HK.

Elsewhere around the region, the Korean market was the worst performer in Asia in October led by selling in electric vehicle supply chain names on demand slowdown and overcapacity concerns. Our exposure to Korea is primarily through semiconductor supply chain companies such as Samsung Electronics and SK Hynix, both of which contributed positively to alpha during the month. We however, have a small position in battery maker Samsung SDI, and this detracted from relative performance during the month.

On the Ground Views – China

Over the past few newsletters, we have discussed the key themes that shape the way that EAFZ is constructed, namely – Technological Disruption, The Rise of the Asian Consumer and Capital Market Liberalisation.

This month, we change pace a little by highlighting some on the ground insights from a recent trip to China by our Senior Investment Analyst, Dejia Li. His main conclusion from the visit was that on the ground economic activity remains solid despite the still cautious sentiment. Consumers are cash rich, but do not have the 'animal spirits' to spend aggressively and are therefore more selective with their purchases. Dejia highlights four other interesting observations:

- **Strong services related demand:** Similar to what we've witnessed with other countries, services related demand is strong as people place a greater emphasis on their lifestyle post COVID. Tourist sites were extremely busy, whilst restaurants, bars, cafes and bubble tea shops were full. The strong travel demand confirms our investment thesis for Trip.com and Samsonite.
- **Value for money is the new consumer trend:** Consumers are becoming more budget conscious with value for money products gaining popularity. Domestic brands have caught up, with their products offering similar quality and features but priced considerably lower than international peers. Xiaomi, which is one of our portfolio companies, is a great example of how value for money innovative products can potentially do better in the current consumer environment.
- **Changing offline landscape:** Online channels are going from strength to strength at the expense of offline channels. Traditional offline stores (e.g. supermarkets, brick-and-mortar stores, travel agents) are exiting the market and being replaced by either online competitors or other offline stores that can offer a better consumer experience. Our portfolio companies such as Trip.com are well positioned for this trend.
- **Live streaming platforms are the new super app:** Companies such as Douyin have become increasingly powerful and disruptive. People use them to shop, order food, message friends and family, search for information and for entertainment. As such, they present a structural challenge to the incumbent internet giants. Consumer companies in turn have needed to adjust their channel strategy in order to stay relevant with their customers, but usually at a lower ROE. This trend supports our decision to not own Meituan and JD.com and our underweight position in Tencent. Other portfolio companies that could be impacted by this trend, such as Mengniu and By-Health, have established omni-channel presences, which helps to alleviate disruption risk.

Overall, the trip helped to dispel concerns that China is still in an economic doldrum. It reinforced our view that there are pockets of opportunities that exist in China, particularly in companies that are more service, and travel orientated or produce innovative and affordable products.

Portfolio Performance Summary

Taiwan and South Korea were the largest contributors by country to alpha during the month, whilst China/HK and our underweight in Malaysia were the relative drags. At a sector level, Information Technology and Communication Services were the biggest contributors to relative performance. Meanwhile, Consumer Discretionary and Real Estate were the worst performers.

At a company level, **Mediatek**, **Netease** and **AIA** were the biggest contributors to relative performance during the month adding a combined 79bps to alpha. Meanwhile **China Overseas Property Holdings**, **Samsung SDI** and **Li Ning** detracted 93bps to relative performance.

Mediatek is a leading fabless semiconductor company that specialises in smartphone system on chips (SoC) for Android device vendors. The company reported better than expected 3Q23 earnings and 4Q23 guidance during the month. Management also cited 'healthy' inventory levels and a bottom in the smartphone cycle.

Netease is one of the largest mobile and PC game content producers in the world. The Netease share price was boosted during the month by broker upgrades ahead of the company's 3Q23 result in November. High frequency data indicates that recently released titles such as Justice Mobile, Racing Master and Dunk City Dynasty have performed well, and this has raised expectations going into the earnings result.

AIA the largest independent Pan-Asia life insurer. AIA's share price had been sold off prior to October on China related growth concerns. The company, however, saw some renewed interest during the month given expectations of better than expected 3Q23 results. Indeed, in early November, AIA reported robust numbers with value of new business growing 34%yoy, including +20%yoy in China.

China Overseas Property Holdings (COPH) is the property management company of China Overseas Holdings, one of the country's largest state-owned property developers. During the month, COPH announced an acquisition of a supervision and consultancy business from its sister company China State Construction. The transaction was conducted at an expensive 19x P/E, which represented a premium to COPH's trading multiple of 14x. The transaction also raised questions around the strategic merits of a property services company owning a consultancy business. In our view, this event created corporate governance concerns that previously did not exist. Given the potential prospects of further related party transactions, we decided to exit our position in COPH during the month.

Samsung SDI is a leading producer of rechargeable batteries for products such as smartphones, power tools, electric vehicles (EV) and energy storage. Samsung SDI's share price was sold off during the month on concerns over slowing EV demand. This was despite the company reporting 3Q23 earnings that were in-line with market expectations. Encouragingly, the company recorded improving EV battery profitability and management guided to the potential for further sequential improvements in 4Q23. Samsung SDI also announced during the month that it had signed an EV supply contract with Hyundai Motors. The company is clearly executing well on its EV strategy, but weak industry demand and sentiment is negatively impacting the share price. We, however, see the transition of the entire auto industry to EVs as a structural story backed by supportive Government policies and any slowdown in demand as temporary.

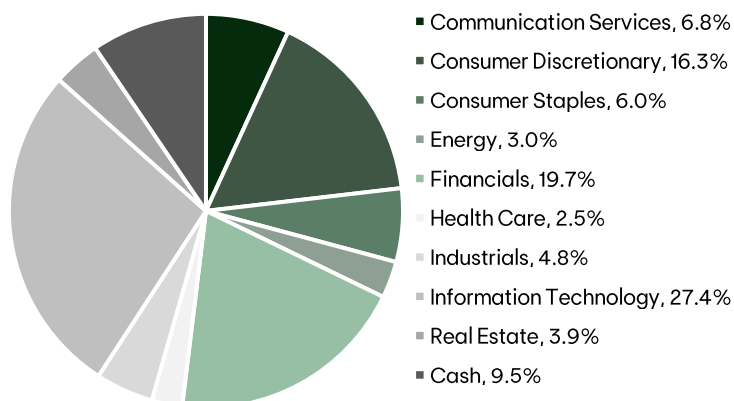
Li Ning is the second largest Chinese sportswear company. The company's share price was impacted by a surprise profit warning where 2023 revenues and operating margins were both downgraded. On the trading update call, management acknowledged there was a channel inventory issue they have not been able to get control of. We view the task of clearing inventory in a more discerning consumption environment in China as a challenging one. As such, near term earnings visibility for Li Ning has deteriorated significantly. Furthermore, this event has not only raised serious questions over the company's overall inventory management process, but it has also dented our assessment of management credibility/competence. Given management quality is a key factor into our investment thesis, we made the decision to exit our position in Li Ning during the month.

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

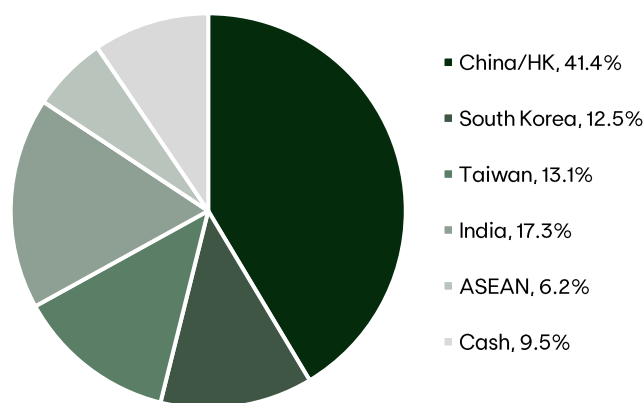
Portfolio Characteristics

Sector allocation



Source: Ellerston Capital.

Geographic allocation



Source: Ellerston Capital.

Top 10 Holdings

Company	Country	Sector	Weight
Taiwan Semiconductor Manufacturing Company Limited	9.8%	Taiwan	Information Technology
Samsung Electronics Co., Ltd.	7.6%	Korea	Information Technology
Alibaba Group Holding Limited	4.2%	China	Consumer Discretionary
NetEase, Inc.	3.8%	China	Communication Services
AIA Group Limited	3.5%	Hong Kong	Financials
HDFC Bank Ltd.	3.5%	India	Financials
SK hynix Inc.	3.5%	Korea	Information Technology
PT Bank Mandiri (Persero) Tbk.	3.3%	Indonesia	Financials
MediaTek Inc.	3.3%	Taiwan	Information Technology
Trip.com Group Limited	3.2%	China	Consumer Discretionary

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

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

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