Ellerston Global Mid Small Cap Fund

Ellerston Capital

Monthly Report as at 31 July 2024

APIR Code: ECL3306AU, ECL8388AU | ARSN 609 725 868

Concentrated portfolio of global mid small cap securities, built through a contrarian, high conviction, and benchmark independent approach.

Targets companies which the Portfolio Manager feels are in a period of "price discovery" and which offer an attractive risk/reward dynamic.

Aims to outperform the benchmark with a focus on risk management and capital growth.

Performance Summary - Class A

Performance	1 Month	3 Months	1 Year	3 Years (p.a.)	5 Years (p.a.)	Since Inception (p.a.)^^
Net^	6.06%	6.45%	4.19%	0.70%	9.37%	10.68%
Benchmark*	7.01%	5.40%	14.73%	5.59%	9.34%	10.44%
Alpha	-0.95%	1.05%	-10.54%	-4.89%	0.03%	0.24%

Performance Summary – Class B

Performance	1 Month	3 Months	1 Year	3 Years (p.a.)	Since Inception (p.a.)^^
Net^	6.07%	6.41%	4.14%	0.94%	8.38%
Benchmark*	7.01%	5.40%	14.73%	5.59%	11.48%
Alpha	-0.94%	1.01%	-10.59%	-4.65%	-3.10%

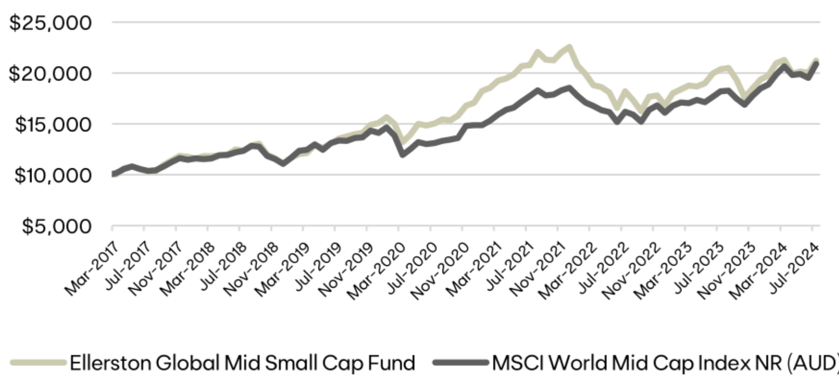
*^ The net return figure is calculated after fees & expenses, assuming all distributions are reinvested. Past performance is not a reliable indication of future performance. * MSCI World Mid Cap Index NR (AUD). ^^Class A inception is 28 February 2017. Class B inception is 18 August 2020.*

Key Information

Portfolio Manager(s)	Bill Pridham
Investment Objective	To outperform the benchmark by 3% over a 5-year rolling period.
Benchmark	MSCI World Mid Cap Index NR (AUD)
Liquidity	Daily
Target Number of Holdings	20-40
Number of Holdings at Month End	36
Minimum Investment	Initial investment - $25,000 Additional investment - $10,000
Distribution Frequency	Half-Yearly (where available)
Management Fee	0.75% p.a.
Performance Fee[1]	10.00%
Buy/Sell Spread	0.25% / 0.25%
Class A Unit Prices & Fund Size	Application – $1.4950 Net Asset Value – $1.4913 Redemption – $1.4876 Fund Size – $42,896,532
Class B Unit Prices & Fund Size	Net Asset Value – $1.2639 Redemption – $1.2607 Fund Size – $48,977,689

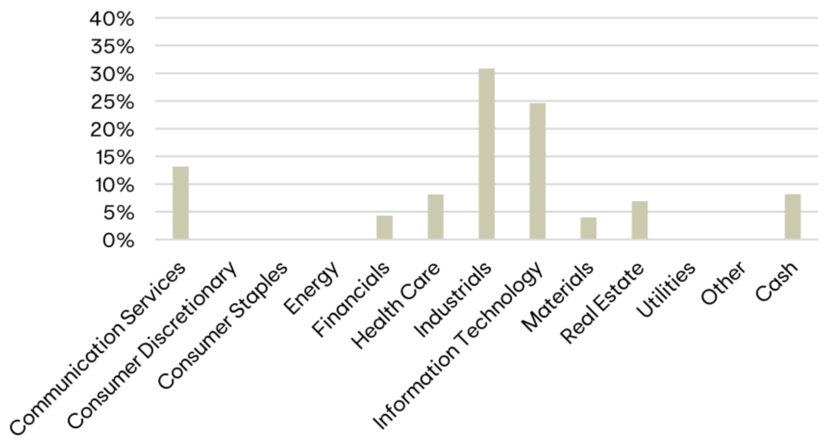
[1]Of the investment return above the benchmark, after recovering any underperformance in past periods.

Growth of $10,000 Investment



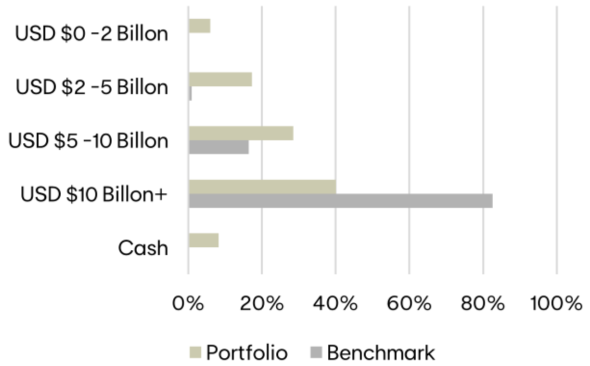
Source: Ellerston Capital.
Performance shown are for Class A Units and net of fees, assuming all distributions are reinvested.
Past performance is not a reliable indication of future performance.

Sector Allocation



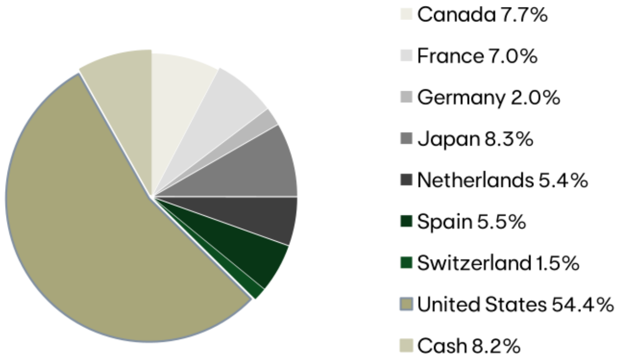
Source: Ellerston Capital.

Market Capitalisation Exposure



Source: Ellerston Capital.

Regional Exposure



Source: Ellerston Capital.

Top Holdings

Company	Sector	Country	Portfolio Weight
GFL Environmental Inc	Industrials	United States	6.5%
Cellnex Telecom S.A.	Communication Services	Spain	5.5%
GXO Logistics Inc	Industrials	United States	4.3%
Bureau Veritas SA	Industrials	France	3.7%
QXO, Inc.	Information Technology	United States	3.6%
Option Care Health Inc	Health Care	United States	3.3%
Chart Industries, Inc.	Industrials	United States	3.3%
AerCap Holdings NV	Industrials	United States	3.0%
WillScot Holdings Corporation Class A	Industrials	United States	2.9%
Acadia Healthcare Company, Inc.	Health Care	United States	2.8%

Source: Ellerston Capital.

MARKET COMMENTARY

July produced a large divergence in returns amongst different equity sectors, characterised by a rotation out of much-loved mega-caps (MSFT, NVDA, AAPL, GOOG, AMZN) and AI related names and into smaller cap companies.

The main driver of this was confirmatory signs of disinflation, with US June CPI falling 0.1% MoM, compared to expectations for a slight increase. This sharp drop in inflation, coupled with disappointing revisions to prior month employment data, brought forward the market's expectations for multiple interest rate cuts from the US Federal Reserve.

The fixed income market is now pricing in a rate cut in September, and two more before the end of the year. Live inflation data point to a continued decline in inflation through July and August, giving some credence to near term rate cuts.

Source: Truflation

Reflecting this rotation, the Russell 2000 rallied 10.2% in July, compared to the NASDAQ falling -1.6%. For context, this was the biggest relative outperformance of the Russell since the 2000 Dot-com bubble, nearly a quarter century ago.

Whether this trend continues, and equity returns further broaden out beyond a handful of mega-caps, remains an open-ended question. However, we would note that positioning and valuations in small caps relative to large caps remains at extreme levels, even despite the recent moves. Hence a continuation of the current environment, characterised by disinflation and reasonable nominal economic growth, could be supportive of small caps outperforming their larger peers.

Beyond the inflation headlines which have dominated market moves, the current 2Q24 reporting season, which is mostly complete, points to an underlying economy in reasonable shape. US GDP growth remains healthy (+2.8% 2Q) and roughly two-thirds of reporting companies have beaten consensus estimates.

However, of note is the US consumer, which appears to be running at two speeds. American Express and Mastercard have pointed to a reasonable overall picture of consumer spending, though some cracks are appearing, with many bellwether companies such as LVMH, McDonalds, Amazon, Starbucks and Diageo pointing to weakening sales and more discerning spend. Given the price increases pushed through by many of these companies over the last 3 years, it raises the question of whether price cuts may be required to stimulate demand in the months ahead.

REGIONAL DISCUSSION

In July, the S&P 500 achieved a return of 1.22% driven by positive economic data such as better-than-expected GDP growth. The Russell 2000, representing small-cap stocks, surged by 10.2%, bolstered by strong earnings reports and the anticipation of interest rate cuts. Additionally, the June CPI data showed a continued deceleration in inflation, which further fuelled expectations of a potential easing in monetary policy.

European markets experienced mixed performance in July. The MSCI Euro index was flat, reflecting the balance between strong corporate earnings and persistent economic concerns. French and Spanish markets saw positive performances, as did Germany. The main market concerns remain on persistent inflationary pressures and ongoing geopolitical tensions.

In July, Japan's stock market experienced a modest decline with high volatility. The Nikkei 225 index dropped by 1.21%, reflecting mixed investor sentiment amid uncertainties in key export markets. The currency market also experienced significant fluctuations, with a sharp appreciation of the yen. On 31 July, the Bank of Japan (BOJ) raised its policy rate to 0.25% from 0.0%-0.10%, which further supported the yen strength.

SECTOR DISCUSSION

The Information Technology sector experienced mixed performance during July. Large-cap tech stocks saw declines, influenced by market volatility and shifts in investor sentiment. Meanwhile, small-cap IT stocks had varied results, with some benefiting from niche market opportunities and innovation. Despite supply chain disruptions and cybersecurity threats, advancements in AI and significant progress in semiconductor production continued to drive innovation and growth.

The Industrials sector experienced positive performance. Key contributors included robust construction activity, with significant job growth reported globally, particularly in the commercial aerospace and utilities infrastructure sectors. Additionally, increased investments in smart manufacturing technologies and sustainability initiatives further bolstered the sector.

The global Communication Services sector saw varied performance in July. While the sector continued to benefit from advancements in AI and digital connectivity, particularly in digital advertising, economic uncertainties and regional disparities presented headwinds. Overall, the sector displayed resilience driven by technological advancements and strategic investments.

PORTFOLIO COMMENTARY

The Ellerston Global Mid Small Cap Fund (Fund) increased 6.06% net during the month compared to the MSCI World Mid Cap (AUD) Index which was up by 7.01% over the same period. The weaker Aussie dollar was a nice tailwind to returns due to the unhedged nature of the portfolio.

The portfolio's top three contributors QXO, Bureau Veritas and Webster Financial added 196bps to performance while Pinterest, Montrose Environmental and Vivendi detracted 159 bps during the month.

QXO Inc (+1.00%): The next vehicle of Brad Jacobs (architect of XPO) has recently raised >$5bn from sophisticated investors, following a $1 billion equity investment ($900m from Jacobs personally) in June. QXO plans to become a tech-forward leader in the $800 billion building products distribution industry. The company is targeting tens of billions of dollars in annual revenue over the next decade through accretive acquisitions and organic growth.

Bureau Veritas (+0.50%): is a world leader in inspection, certification, and laboratory testing services supporting customers in 140 countries to address challenges in quality, health and safety, environmental protection, and sustainability. The company released its first half-year financial report of 2024 with strong growth. Full year organic growth was upgraded to high-single digit as second quarter metrics actually accelerated from the start of the year. With an incredibly strong balance sheet and cash flow profile, we should see an acceleration of accretive tuck in M&A over the coming months.

Webster Financial (+0.46%): is a leading commercial bank in the Northeast of the U.S. that provides a wide range of digital and traditional financial solutions across commercial banking, consumer banking and healthcare financial services. The company reported its second-quarter results on 23rd July, which came in slightly below market expectations. Regardless, the market remains positive about the bank increasing reserves and potentially benefitting from rate cuts.

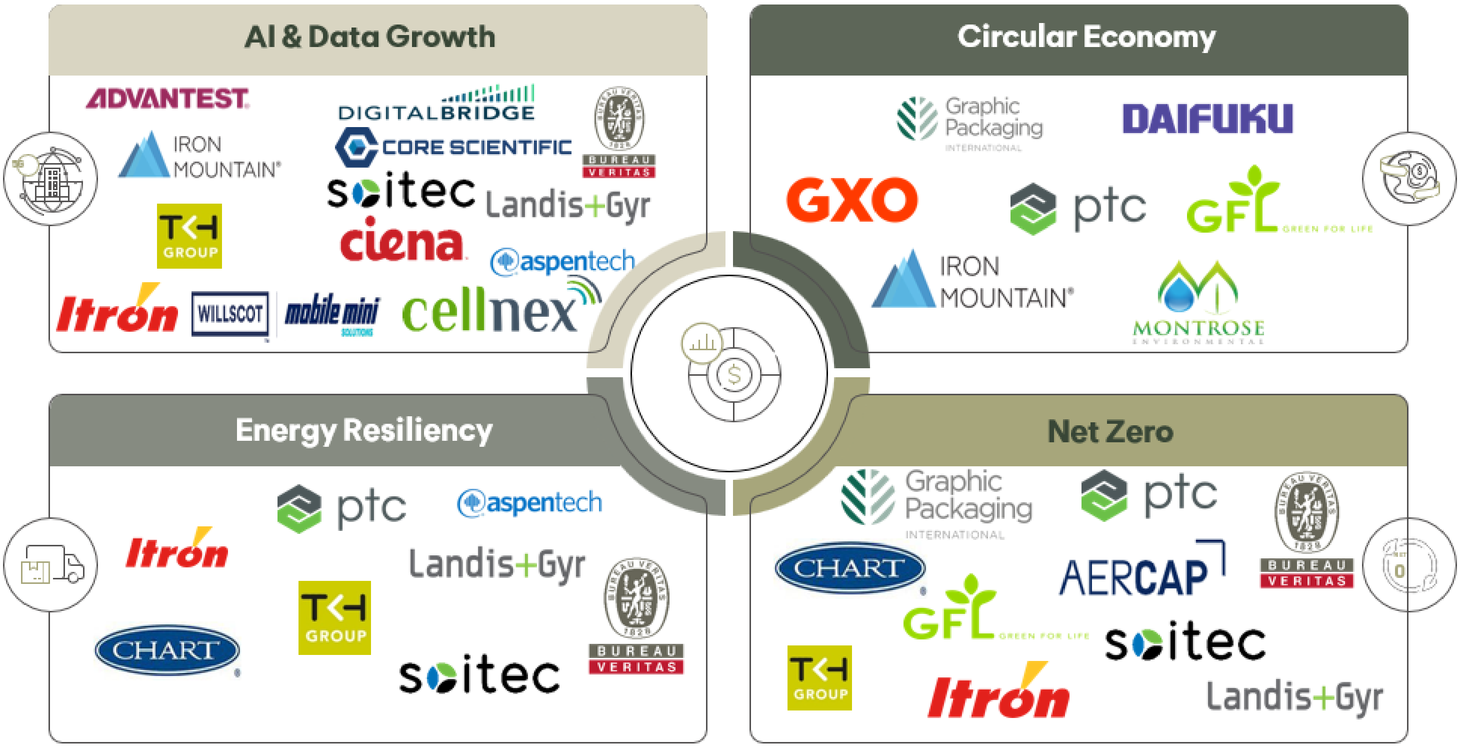
Pinterest (-0.71%): is a visual search and discovery platform where people find inspiration, curate ideas, and shop products. Launched in 2010, Pinterest has over half a billion monthly active users worldwide. The company reported its second-quarter results on 30th July with solid growth but warned of generating lower revenue than expected for the current quarter. Pinterest is running the risk of being usurped by the much larger platforms such as Meta and Tik Tok and despite the much different user experience, digital advertisers will follow the eyeballs and subsequent return on ad spend.

Montrose Environmental (-0.71%): is a leading environmental solutions company delivers comprehensive air measurement and laboratory services for regulatory compliance, emergency response, permitting, engineering, and remediation. The company acquired Spirit Environmental, LLC., a leading provider of air permitting and compliance services in July. The company also reaffirmed a positive outlook following U.S. regulatory catalysts. The stock has been weak due to concerns around new legislation potentially impacting Environmental Protection Agency (EPA) directives however in its recent result, the company materially outperformed expectations along with strong commentary around the strong growth outlook for the business.

Vivendi SE (-0.17%): is a world-class content, media and communications group, active in businesses including the creation and distribution of cinema and audiovisual content, book publishing for the public and educational markets, global communications, as well as magazine and video games. Vivendi is a new position in the portfolio and was impacted by a poor earnings announcement out of one of its large holdings, Universal Music. Despite this, the value of the underlying assets is much higher than the current share price and Management is looking to split the company to unlock shareholder value.

During the month we trimmed positions in Itron, Iron Mountain, Landis+Gyr and Webster to take advantage of price movements which moved closer to fair value. We exited positions in Flex and LiveRamp during the month. Flex has had an incredibly strong price performance over the past several months, increasing >36% and slightly exceeding our view of fair value. One of its comparable companies (Jabil) reported very weak results in late June and when coupled with full valuation, we deemed the risk/reward as unattractive. Our investment in LiveRamp was predicated on the thesis that Google would move to deprecate cookies (these are used to follow your movements on the internet for advertising) which would place LiveRamp in a prime competitive position. This thesis changed when Google announced it would not be deprecating cookies and we decided to exit the position as the profile of the business had changed. Conversely, we initiated positions in Aercap Holdings and Vivendi Group. Aercap is the world's largest owner of commercial aircraft and leader in aviation leasing. The business will benefit from the structural shortage of aircraft driving up lease rates as well as strong aftermarket pricing for older aircraft, both of which will drive up shareholder value. Vivendi owns a portfolio of media assets which are not being valued appropriately given the conglomerate nature of the holding structure. Vivendi is expected to unlock significant value with the splitting of these assets into separate entities which should benefit us as shareholders.

We continue to have differentiated exposure to some pretty powerful long term thematics which should drive long term compounding benefits to us all as investors. These include AI and the growth in data as Industrial IoT and large language networks such as ChatGPT and next generation applications drive data demand, companies that enable our push to a circular economy, beneficiaries of deglobalisation as well as those helping to improve the resilience of our energy grids as the world looks to electrify and companies which are levered to the multi trillion-dollar spending required for our "Road to Net Zero".



Source: Ellerston Capital

These businesses as well as idiosyncratic opportunities in the Fund should provide solid absolute and relative returns over the long term as secular and structural business drivers help mitigate earnings risk in times of economic uncertainty.

As always, we thank you for your continued support and look forward to providing further updates in the future.

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.**

There have been no changes to the primary investment personnel responsible for managing the Fund.

Contact Us

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Find out more:

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

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