New Zealand Equities Fund

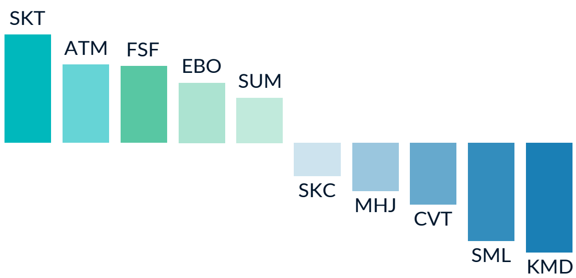
Investor Factsheet for the quarter ended 31 March 2024

	Quarter Performance	1 year	3 years*	5 years*	Since Inception*	Since Sep 2019*
Gross Fund Return**	3.79%	3.83%	2.81%	7.17%	11.22%	5.66%
S&P/NZX 50 Gross with Imputation Index***	3.13%	2.75%	-0.42%	5.03%	8.94%	3.08%
Out/under performance	**0.67%**	**1.08%**	**3.23%**	**2.14%**	**2.27%**	**2.58%**
Tracking error	n/a	2.59%	2.32%	2.53%	3.66%	2.56%
Information ratio	n/a	0.42	1.39	0.85	0.62	1.01
Sharpe ratio	n/a	-0.21	-0.03	0.41	0.80	0.45

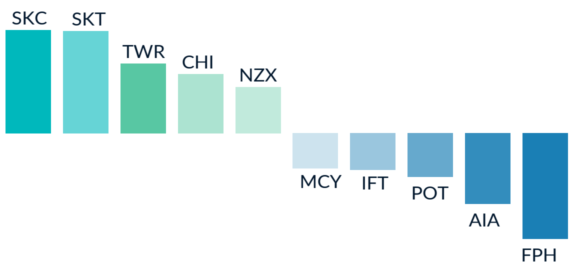
Key Fund Facts as at 31 March 2024

Fund Name	New Zealand Equities Fund	**Risk Indicator**	1 2 3 4 **5** 6 7
Inception Date	26/06/2008	**Market Index**	S&P/NZX 50 Gross with Imputation
Fund Value (NZD)	$92,136,585	**Unit Price**	$4.0593
		Annual Fund Charge (ex-GST)	1.15%

ATTRIBUTION (ROLLING 4QS TO 31 MARCH 2024)



PORTFOLIO CONVICTION (AS AT 31 MARCH 2024)



The fund in its macro context

The March quarter saw the New Zealand equity market deliver a robust 3.13% return. This was a particularly impressive performance in the face of two quite powerful headwinds.

First, the New Zealand economy delivered two consecutive quarters of negative GDP growth. The declines came in the face of strong immigration over the prior 12 months. These new arrivals into New Zealand are earning and spending, yet the economy is contracting. It is hard for companies to deliver profit growth when revenues are falling. Fixed costs are real and they take time to remove – be it by simplification, automation, or outright downsizing of a business. The February reporting season delivered the worst profit growth since the GFC (Global Financial Crisis) in 2008.

The second headwind came from an increase in interest rates. It was modest at around 0.23% on the 10-year New Zealand government bond yield. We see weakness in economic activity and that should over time lead to an easing of interest rates which will both lower interest costs and makes it easier to invest in growth projects.

Portfolio attribution

For the quarter to 31 March the New Zealand Equities Fund delivered a gross return of 3.79%, outperforming the funds' market index return of 3.13%.

On a rolling four quarters basis to 31 March, the fund delivered a gross return of 3.83%, well ahead of the funds' market index return of 2.75%.

* Annualised

** Gross Fund Returns are calculated before deduction of taxes and fund charges but after deduction of trading expenses and including imputation credits where applicable. Market index returns do not have any deductions for fund charges, trading expenses or tax.

***For periods prior to April 2018, the market index/benchmark return used is S&P/NZX50 Gross index.

Looking at annual performance, Sky TV (SKT) performed well for the fund on the back of revenue growth returning after several years of decline, improved cost management and the receipt of an indicative takeover bid – which didn't end up developing into a full offer. We still believe the market under-estimates the free cash flow the business can generate on a sustained basis. Loss of the New Zealand Rugby rights (five-yearly renewals) remains the key risk to the business.

On the other side of the ledger, our position in Kathmandu (KMD) was a drag on fund performance over the last 12 months. Our valuation, using more conservative long-term profits than management believe they can achieve, is highly supportive. However, there is an industry saying: "retail is detail". Management teams need to get a lot of things right to deliver good profits in retail, and current trends around market share need to be arrested. We have not topped up our position in KMD as the share price has fallen while we continue to gain greater understanding of the weakness in the Kathmandu brand.

Portfolio position and conviction

We see the economic backdrop in New Zealand as likely to stay weak until at least the third quarter of this year. Across the whole New Zealand landscape, management commentary around current trading was softer than we expected in the February reporting round. The weaker economic backdrop should see the RBNZ cut short term interest rates this year, in our opinion.

Each of our positions is backed by an individual valuation case. Sector weightings and exposure to single economic drivers are reviewed as part of portfolio construction to ensure we maintain diversification. In general terms, we see the market as overpaying for defensive earnings in sectors like infrastructure and telecommunications.

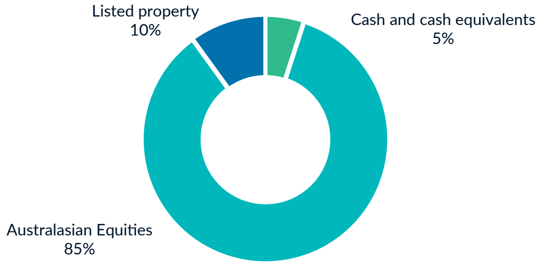
Our highest conviction positions, Sky City, SKT and general insurer Tower (TWR) have strong medium term valuation support, whilst only TWR is likely to have positive news on near term earnings. We fund these positions with large underweight or zero positions in growth stocks Fisher and Paykel Heathcare and Gentrak, along with underweight positions in growth infrastructure names such as Auckland International Airport and Port of Tauranga.

Conclusion

We see opportunity when share prices are impacted much more by near term earnings reports than medium term valuations. We believe the New Zealand Equity market is in such a phase, reinforced by a little bit of fear being priced into the cyclical sectors of the market.

Backing long term profitability in the face of profit falls is not riskless – we often find that companies offer value well before we see earnings rebound. We need to back up the valuation opportunity with confidence in the balance sheet and management team – hence the changes we have seen at Sky City and Fletcher Building invite us to understand what new management brings to those businesses.

TARGET ASSET ALLOCATION



TOP 10 FUND HOLDINGS AT QUARTER END

Security	Weight
Fisher & Paykel Healthcare Corporation Ltd	9.1%
Contact Energy Limited	7.0%
Auckland International Airport Limited	6.9%
Infratil Limited	6.4%
Spark New Zealand Limited	6.2%
Meridian Energy Limited	5.4%
SKYCITY Entertainment Group Limited	4.6%
Mainfreight Limited	4.4%
The a2 Milk Company Limited	4.0%
Ebos Group Limited	3.9%
Major holdings as % of total portfolio	**57.9%**

Investment Philosophy and Thesis

Octagon is an active investment manager. Our investment philosophy focuses on developing a repeatable process that systematically looks for short-to-medium term inefficiencies in market pricing of securities with a solid economic basis and a good management team to deliver long term, measurable alpha.

The most common and persistent market inefficiencies we find are:

- thin research coverage, especially in the New Zealand market
- excessive focus on near term earnings
- market dislocations and liquidity events
- temporary governance failures
- irrational investor behaviour

For Octagon, "value" means not overpaying for the promise of future growth by developing a fundamental understanding of a business, its financial metrics, return on invested capital and then scenario testing the investment model under different macro conditions.

Portfolio Manager

Paul Robertshawe, CA
Director, Chief Investment Officer

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