Australian Equities Fund

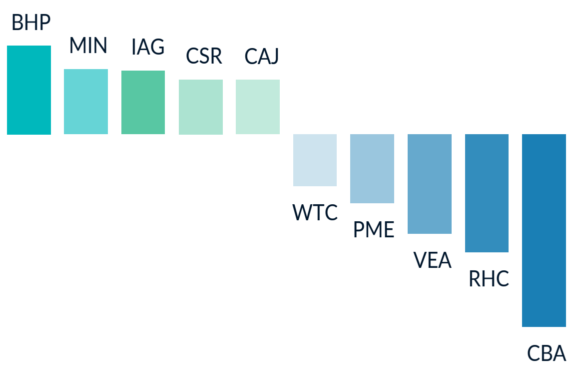
Investor Factsheet for the quarter ended 31 December 2024

	Quarter Performance	1 year	3 years*	5 years*	Since Inception*	Since Nov 2019*
Gross Fund Return**	-0.89%	13.32%	9.71%	10.43%	5.40%	9.66%
S&P/ASX Accumulation 200 Index (50% Hedged)***	-0.11%	13.32%	8.66%	9.09%	6.23%	8.35%
Out/under performance	**-0.78%**	**0.00%**	**1.06%**	**1.34%**	**-0.83%**	**1.31%**
Tracking error	n/a	1.74%	2.00%	2.44%	5.70%	2.42%
Information ratio	n/a	0.00	0.53	0.55	-0.15	0.54
Sharpe ratio	n/a	0.89	0.41	0.48	0.16	0.44

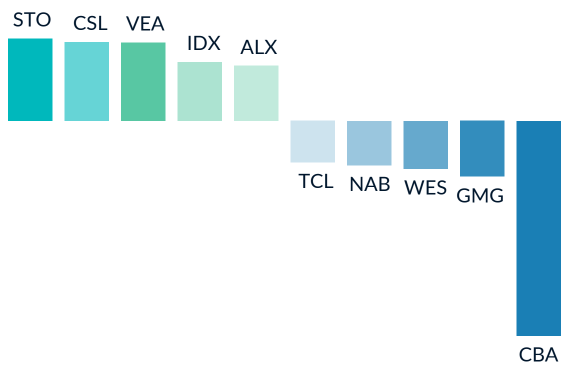
Key Fund Facts as at 31 December 2024

Fund Name	Australian Equities Fund	**Risk Indicator**	1 2 3 4 5 6 7
Inception Date	26/06/2008	**Market Index**	S&P/ASX Accumulation 200 Index (50% Hedged)
Fund Value (NZD)	$99,034,486	**Unit Price**	$ 1.9284

ATTRIBUTION (ROLLING 4QS TO 31 DECEMBER 2024)



PORTFOLIO CONVICTION (AS AT 31 DECEMBER 2024)



The fund in its macro context

Australian equities declined by -0.8% in the December quarter, modestly outperforming the MSCI All Countries World Index (ACWI), but underperforming the New Zealand equity market.

Weaker equities during the December quarter were triggered by a more cautious stance from the US Federal Reserve (the Fed) on the extent of its easing cycle; rising long-term bond yields; and risks to inflation and global growth stemming from US trade and domestic policy under the incoming Trump administration.

Australian macroeconomic data remained mixed during the quarter, but key fundamentals have not materially changed:

- **Inflation:** Easing at a modest pace, with the trimmed mean at 3.2% in November.
- **Consumption and Investment:** Household consumption and business investment continue to grow below trend, constrained by higher interest rates.
- **Labour Market:** Relatively tight, with unemployment edging lower to 3.9%.
- **Government:** Increased public spending is helping to sustain mildly positive economic growth.

* 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 an unhedged variant of the S&P/ASX Accumulation 200 Index in New Zealand dollars.

This macroeconomic setup points to a soft landing for the Australian economy. We don't expect a dramatic decline in corporate profits nor a material expansion in margins. Cost pressures remain and opportunities to raise prices are limited with softer household consumption and business investment activity. Valuation multiples in the equity market are quite high relative to history, with some large sectors, namely the banks, clearly over-extended relative to their fundamentals.

Portfolio Attribution

For the quarter ending 31 December, the Australian Equities Fund delivered a gross return of -0.89%, underperforming the fund's market index return of -0.11%.

For the four quarters to 31 December, the fund delivered a gross return of 13.32%, matching the fund's market index return of 13.32%.

Our underweight position in BHP contributed positively, as its shares underperformed due to falling iron ore prices and negative sentiment around the Chinese economy. The failed Anglo American acquisition further raised concerns about the company's growth prospects and capital allocation. Following this material sell-off, we closed our underweight position as valuation now appears closer to fair value given its industry leading production assets.

Our long-held overweight position in insurer IAG was another top contributor for the four quarters to 31 December. Strong operational momentum, supported by a benign claims environment in 2024 after the flooding events of 2022 and 2023, drove the stock's performance. IAG also benefited from premium pricing gains, as claims and cost inflation lagged policy price increases. Lower reinsurance costs further boosted operating margins. Recent global catastrophes (e.g., the Los Angeles fires) may provide scope for additional premium hikes. While revenue growth may moderate, we expect positive real price gains to continue boosting profits.

Our overweight position in Ramsay Healthcare (RHC) detracted from performance as the company has experienced structurally lower profit margins post-pandemic. Reduced doctor visits and referrals led to fewer surgeries, resulting in lower capacity utilisation and significant operating deleverage as the high fixed cost base took a toll.

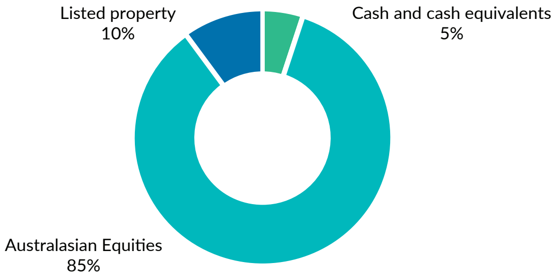
RHC's inability to raise prices in line with sharply increasing operating and wage costs has compounded the pressure on margins. Health insurers and government tariff structures have exerted substantial bargaining power, limiting cost recovery. With around a third of private hospitals in Australia now loss-making, the industry is calling for emergency government funding and higher indexation from insurers. Given these structural challenges, we have reduced our position.

Our overweight position in Viva Energy (VEA) also detracted from performance. While the company delivered stable operating performance half on half, earnings were heavily driven by the more volatile refinery business, with weaker results in core petrol and convenience retail. Tobacco sales, a significant retail product, were particularly impacted by the growth of the illicit tobacco market as consumers sought cheaper alternatives. Additionally, VEA flagged a weaker outlook for near-term refining margins in its August results, which is expected to weigh on profitability in FY25.

TOP 10 FUND HOLDINGS AT QUARTER END

Security	Weight
BHP Group Limited	7.6%
CSL Limited	7.1%
Commonwealth Bank of Australia Limited	6.4%
Westpac Banking Corporation	4.6%
National Australia Bank Limited	3.8%
Australia and New Zealand Banking Group Ltd	3.1%
Macquarie Group Limited	3.1%
Telstra Group	2.6%
Rio Tinto Limited	2.5%
Santos Limited	2.5%
Major holdings as % of total portfolio	**43.4%**

TARGET ASSET ALLOCATION



Portfolio Conviction

Our conviction positions in the energy sector began delivering strong returns in late 2024, which have continued into early January 2025. Santos and Karoon remain favoured due to their strong free cash flow and dividend profiles at current oil prices. Despite recent share price gains, valuations remain reasonable. We are comfortable maintaining these overweight positions but will consider selling into further gains if implied oil prices rise significantly.

As noted earlier, VEA underperformed in 2024; however, our long-term thesis remains intact. Earnings upside is expected from On the Run (OTR) store rollouts and improved synergy guidance for the Express and OTR businesses. With improving earnings and a low valuation starting point, we see potential for attractive returns in the coming years.

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
- 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.

Healthcare is another favoured sector, with CSL and Integral Diagnostics (IDX) our preferred picks. IDX's merger with Capitol Health offers potential cost savings across procurement and current overhead duplication. Imaging volumes are recovering, and cost pressures are abating, which should support improved operating margins.

CSL's positive outlook is driven by gains in plasma collection. Donor fees and costs, which had peaked in 2022, are now significantly lower, and the rollout of the REIKA system is expected to improve collection efficiency by reducing donor time by approximately 25%. These improvements should materially lift profitability over the medium term.

Conclusion

The key market catalyst in the final quarter of 2024 was the return of Donald Trump as US president. This development has increased global interest rates and strengthened the USD, creating mixed outcomes for riskier assets. As the Trump administration's trade and economic policies take shape, further volatility in equity markets is expected.

Weak economic growth in China has weighed heavily on hard commodity markets and major ASX-listed miners in 2024, with iron ore and copper prices falling materially. We anticipate new stimulus measures from China in response to any tariffs introduced by the Trump administration.

The magnitude and focus of these measures will be a key driver for ASX returns, given its significant resources sector exposure. After the 2024 sell-off, we closed our underweight position in the sector because valuations now seem closer to fair value. Many of these companies deliver healthy longer-term cash flows even with conservative commodity prices assumed.

Entering 2025, Australian inflation is trending towards the Reserve Bank of Australia's (RBA) target, with recent monthly CPI data indicating an outcome below RBA forecasts for the December quarter. In recent weeks a number of analysts have responded by bringing forward their expectations for the first RBA rate cut to the February meeting (from May), indeed the market now prices this at around a 2/3 probability. Falling interest rates would set the scene for improved performance across rate sensitive segments of the market, particularly those out of favour last year, in 2025.

Portfolio Manager

Jason Lindsay, CA
Head of Equities

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