Spheria Opportunities Fund

ARSN 114 032 431 | APIR WHT0025AU | mFund SPM03

Performance as at 31 December 2023

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a[1]
Fund[2]	12.0%	11.2%	7.0%	5.5%	9.3%	8.9%
Benchmark[3]	7.0%	6.5%	7.8%	4.1%	9.2%	8.2%
Difference	4.9%	4.7%	-0.8%	1.5%	0.1%	0.7%

[1] Inception date is 11 July 2016. Past performance is not a reliable indicator of future performance. All p.a. returns are annualised.
[2] Spheria Opportunities Fund. Returns of the Fund are net of applicable fees, costs, and taxes.
[3] Benchmark is the S&P/ASX Mid-Small Accumulation Index.

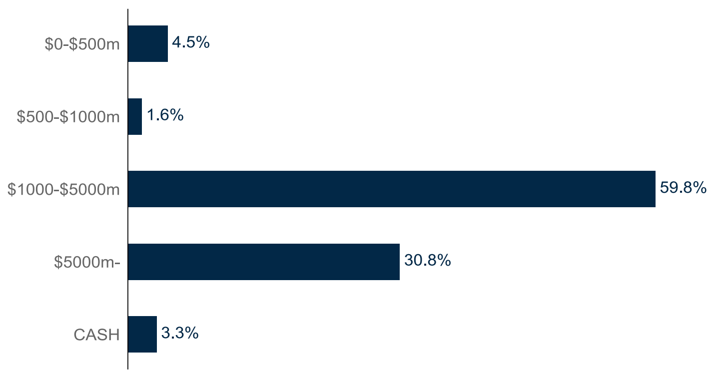
Overall Commentary

The Fund returned 12.0% (after fees) for the month of December, outperforming the S&P-ASX Mid-Small Accumulation Index by 4.9%.

Top 5 Holdings

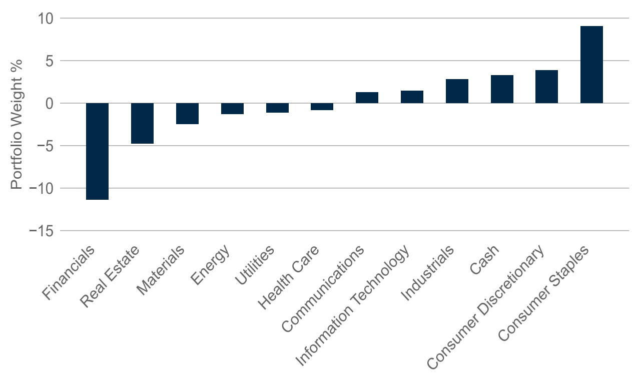
Company Name	% Portfolio
Charter Hall Group	5.4
Whitehaven Coal Limited	4.9
ALS Limited	4.9
The A2 Milk Company Limited	4.8
Link Administration Holdings Limited	4.7
Top 5	**24.7**

Market Cap Bands



Source: Spheria Asset Management

Active Sector Exposure



Source: Spheria Asset Management

Markets

December was an extraordinary month for the Fund. With corporate activity having taken a bit of a backward stance during the latter part of the year, it came back with a vengeance in December. A total of three (A2B Ltd (A2B.ASX), Link Administration Holdings (LNK.ASX) and Adbri (ABC.ASX)) of the Fund's holdings received firm bids during the month. What drove this appears to have been the confluence of several factors – firstly valuations were low in all of the names attracting bids, secondly there is now a building consensus that interest rates are likely to have peaked in the US and not far off their peak in Australia. We support this view on the basis that the remarkable events around Covid ended up being a co-ordinated super inflationary event which has since been unwound. The monetary tightening globally, higher interest rates and the re-opening of economies has seen a lot of excess liquidity drained from global economies and production bottlenecks unwind. Supply chains have largely normalised. In China we are seeing deflation – yes you read that correctly – deflation with consumer prices down 0.5% YoY and producer prices (the prices manufacturers broadly charge for goods) down 3% YoY.

Consumers are struggling in Australia with retailers reporting very tough trading environments, however, housing prices remain strong and unemployment relatively low. These are confusing signals for the RBA to interpret. Nonetheless we would expect an easing bias late in 2024 assuming domestic inflation rates continue to be downward trending – which we think likely. This backdrop should be relatively kind to small cap investors. Small caps have materially lagged large caps over the past two years (smalls^ have underperformed by 14% and micros^ by 27% vs. the ASX 100 to 31 December 2023). The December rally in small caps was mirrored by large caps meaning the underlying performance gap still remains. If the interest rate environment continues to ease, we would suspect a relatively supportive environment for small and micro caps over the next year.

Major Contributors to Performance

Over the month the largest contributors to performance were from overweight positions in Link Administration Holdings (LNK.ASX, +59%), Adbri (ABC.ASX, +47%), and Alumina (AWC.ASX, +24%).

Link Administration Holdings (LNK.ASX) share price rallied nearly 60% during the month after the company received a takeover offer from Mitsubishi UFJ Financial Group. Link shareholders will receive $2.10 plus a $0.16 cash dividend (25% franked) which represented a ~33% premium to the prior day's closing price and a ~63% premium to the 3-month volume-weighted average price. We have discussed LNK in prior commentaries as the share price had come under pressure in the last year due to legal proceedings relating to its Funds Solution (LFSL) division in the UK, as well as the surprise loss of a large client (HESTA) representing 10% of divisional revenue in June 2023 which sent the company's share price into a tailspin. We entered the name in late calendar year 2022 on valuation grounds (having never owned the company since it listed in 2015) and subsequently bought more over the last year as the share price retraced further. Whilst the bid is opportunistic, we think the significant premium offered and the risk-reward given company's relatively high gearing levels means the deal is highly attractive to shareholders. The takeover validates the significant strategic value on offer with Link Market Services (share registry and employee share plans) being the second largest player in Australia and NZ, third in the UK and second in India, whilst the Retirement & Superannuation Solutions (RSS) business is the largest administrator in the industry fund space in Australia.

Adbri (ABC.ASX) share price rose 47% in December after it received a non-binding proposal from CRH and the Barro Group to acquire 100% of the company for $3.20 per share which represented a 41% premium to the last closing price. CRH is a leading global building materials company with strong market positions in North America, Europe and growing presence in Asia and South America. As we understand CRH will be buying out minority shareholders with the Barro group retaining its 43% interest. Given CRH has only a small existing presence in the Australian market the deal is not expected to face any notable competition hurdles. ABC has been a long-term holding in the fund, but its share price has come under pressure in the last few years due to several factors including an irrational industry pricing environment, a material loss of lime volumes in respect of long-term supply agreement and balance sheet pressure from higher-than-expected capital expenditure on their Kwinana project upgrade. With these issues now largely resolved the group was looking forward to significantly improved returns for shareholders which has likely prompted the CRH/Barro consortium to pounce on the balance of the company at this point in time.

Major Detractors from Performance

The largest detractors from performance included overweight positions in Star Entertainment Group (SGR.ASX, -2%), MetCash (MTS.ASX, -4%) and ***not owning*** Neuren Pharmaceuticals (NEU.ASX, +61%).

Metcash (MTS.ASX) share price declined 4% in a rising market which means it was a source of relative underperformance during the month. Its perception as a defensive exposure due to its predominantly consumer staple nature results in a tendency for it to underperform in a rising market. The company trades at about half the multiple of its peers Coles and Woolworths due to it primarily being a wholesaler to independents in the grocery and liquor markets, and the competitive threat from the likes of Aldi, Costco, Endeavour and obviously Woolworth and Coles. In November MTS increased its ownership of the Total Tools business from 85% to 100% continuing its efforts to diversify the group from the competitive headwinds in grocery and liquor channels. The company generates strong free cash flow and trades on an EV/EBIT of only 8x FY24F.

Neuren Pharmaceuticals (NEU.ASX) – **not owned** rose 61% in December. NEU detracted from relative performance due to its weight in the index. Neuren is a biopharmaceutical company that is developing new drug therapies to treat highly debilitating neurodevelopment disorders that emerge in early childhood, with their approved drug trofinetide (sold under "Daybue") treating Retts syndrome. The strong share price performance over the month comes as the company announced positive results from its Phase 2 trial of Phelan-McDermid syndrome (rare genetic condition that causes developmental and speech delays, behavioural problems and a weakening/no ability to feel pain or sweat).

Outlook & Strategy Going Forward

Fairly evidently, we are constructive on smaller companies in 2024. Whilst it's true that – to paraphrase Buffett – you should never ask a small-cap manager if its time to buy small caps* – we still think it's about the right time to buy small caps. Just as many investors have moved capital into the relative safety of larger liquid and less economically sensitive names during a downturn, so too will they likely return to the smaller end of the market to increase returns when rates and confidence turns. We would also like to note, with sadness and gratitude the passing of Charlie Munger who died in late November just shy of his 100th birthday. Charlie was the slightly less known of the Buffett/ Munger duo but undoubtedly an equal intellectual contributor to the investment advice and wisdom that has emanated forth from Berkshire Hathaway. Many of our investment team were drawn to investing after reading some of the intelligent and humorous advice from Buffett and Munger. We are grateful for his intellectual curiosity, humility and generosity of spirit in sharing his wisdom and life outlook with us. Thank-you Charlie.

*Buffett quips that you should never ask a barber if its time for a haircut because the answer is always "yes".

^Smalls = S&P-ASX Small Ordinaries Accumulation Index & Micros = S&P/ASX Emerging Companies Index

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Platform Availability List

The Spheria Opportunities Fund is available on the below Platforms. Platforms provide with consolidated and centralised reporting (including administration, tax, and distribution) by bundling together a range of managed funds as one single product. If the fund is not available on your preferred platform, please contact us. Please check with your platform for minimum investment requirements and fees.

HUB24 (IDPS only)	mFund	mFund	Praemium
Macquarie Wrap	Netwealth (IDPS only)		

Spheria Opportunities Fund	
Benchmark	S&P/ASX Mid-Small Accumulation Index
Investment Objective	Outperform the S&P/ASX Mid-Small Accumulation Index over the medium to long term
Investing Universe	Primarily listed companies outside the top ASX 50 listed companies by market capitalisation and companies listed on the New Zealand Stock Exchange with an equivalent market capitalisation
Holdings	Generally 20-65 stocks
Distributions	Half-Yearly
Fees	0.99% p.a Management fee & 15% performance fee of the Fund's excess return versus its benchmark, net of the management fee
Cash	Up to 20% cash, typically 5% - 10%
Expected Turnover	30% - 40%
Style	Long only, risk aware
APIR	WHT0025AU
Minimum Initial Investment	$25,000

Fund Ratings

Contact Us

For more information, please contact Pinnacle Investment Management Limited on 1300 010 311 or email distribution@pinnacleinvestment.com

Disclaimer

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Link to the Product Disclosure Statement
Link to the Target Market Determination
For historic TMD's please contact Pinnacle client service Phone 1300 010 311 or Email service@pinnacleinvestment.com

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