

# Blackwattle Mid Cap Quality Fund

September 2024



## About the Fund

The Blackwattle Mid Cap Quality fund is a concentrated yet diversified portfolio of some of the highest and most improving quality companies on the ASX. We believe that high quality companies have the potential to consistently outperform over the medium term, as their competitive advantages may allow for compounding shareholder returns through market cycles.

The fund is concentrated on the team's best ideas, driven by fundamental research to establish differentiated views on the outlook of company quality, valuation and earnings. The fund is targeting long term ownership of high-quality companies to generate a consistent outperformance profile, compounding shareholder returns through market cycles.

## Blackwattle Investment Partners

Blackwattle is a new generation, highly aligned, Australian investment manager investing in quality businesses and people.

### Alignment

Shared staff ownership, zero personal trading, profit and personal salary reinvestment, and most importantly significant personal investment alongside our clients.

### Quality

We aim to buy businesses that have a forward advantage, trustworthy aligned management, priced below intrinsic value.

### Trust

We believe that honesty and transparency builds trust with our clients, stakeholders, and community.

## Key Information

<b>Fund Name</b>	Blackwattle Mid Cap Quality Fund
<b>Inception Date</b>	August 2023
<b>Typical no. of Stocks</b>	20-35
<b>Cash Limit</b>	10%
<b>Cash Distributions</b>	Semi Annually
<b>Redemptions</b>	Daily
<b>Constrained Capacity</b>	\$2.0b (or up to 25bps of the benchmark)
<b>Platforms</b>	HUB24 IDPS & Super, Netwealth IDPS
<b>Ratings</b>	Lonsec - Recommended Zenith - Approved
<b>Objective</b>	The Fund aims to outperform the S&P/ASX300 Accumulation Index - S&P/ASX20 Accumulation Index (after fees and before taxes) over the long term.

## Portfolio Managers



### Tim Riordan CFA, FRM

15+ years' investment experience. 5 years as Head of Direct Equities at Aware Super and Lead PM of the Aware Super Mid Cap Industrial Fund. Was Co-Head of Research and Portfolio Manager at Altair Asset Management.



### Michael Teran CFA

14+ years' investment experience. Associate PM of the Aware Super Mid Cap Industrial Fund. Also Long-Short Equities Analyst at Point72 Asset Management in Hong Kong. Anc Equities Analyst at Colonial First State Global Asset Management (now First Sentier Investors).

## Fund Performance<sup>1</sup>

Blackwattle Mid Cap Quality Fund Performance (net of fees) as at 30 September 2024.

As at 30 September	1 month	3 months	6 months	1 Year	2 Years	3 Years	Inception p.a. <sup>2</sup>
<b>Fund (Net)</b>	2.76%	7.70%	6.49%	29.73%	-	-	19.09%
<b>Benchmark<sup>3</sup></b>	4.05%	9.09%	4.41%	20.30%	-	-	12.89%
<b>Active Return</b>	-1.29%	-1.40%	2.08%	9.43%	-	-	6.20%

<sup>1</sup> Returns are calculated after fees have been deducted and assume distributions have been reinvested. No allowance is made for tax when calculating these figures. Past performance is not a reliable indicator of future performance. Source: Apex.

<sup>2</sup> The inception date for the Fund is 8<sup>th</sup> August 2023, returns greater than 1 year are annualised<sup>3</sup> or "calculated on an annualised basis."

<sup>3</sup> S&P/ASX300 Accumulation Index - S&P/ASX20 Accumulation Index

## Top 5 Holdings



## Market Commentary

The ASX300 ex-20 was up 4.05% in September. Global financial markets marched higher in September, with the S&P500 up 2.0%. Global equity rallied strongly on the back of easing from the 2 largest economies: US and China. The US Federal Reserve cut the Federal Funds Rate for the first time since March 2020, cutting by 0.5% to 4.75-5.0%. The following week, the PBOC cut bank reserve requirements by 0.5% and the Chinese government announced a series of stimulus packages including family allowances, subsidies for consumer goods & business equipment upgrades, funding for local governments and reducing restrictions on house purchasing. Sentiment on China had been very weak, with Chinese equity markets being one of the worst performing markets in 2024, and with the positive stimulus surprise sent Chinese markets jumping over 20% in September, to now being one of the best performing markets in 2024!

In the ASX, the Chinese stimulus surprise was the main driver, causing a significant rotation into Materials which had been consistently the worst performing sector this year. Materials was the best performing sector, rallying over 13% and driving over 80% of the ASX200's returns in September. The weakest sectors were defensive sectors such as Healthcare, Consumer Staples and Banks, as the market rotated towards more cyclical sectors given the shift towards a global easing cycle.

## Portfolio Commentary

The Blackwattle Mid Cap Quality portfolio underperformed the ASX300 ex-20 benchmark by 1.29% during the month.

### *Key Contributor – Whitehaven Coal (WHC AU)*

WHC was the largest positive contributor to performance during the month. WHC rallied 10% in September on improving China sentiment and rebounding metallurgical coal prices. WHC is an Australian coal producer with thermal coal mines in NSW and recently acquired metallurgical coal mines in QLD. We view WHC as one of the highest quality mining companies on the ASX, with strong financials and a capital disciplined management team.

Our conviction in the material long-term upside for WHC as an 'improving / enduring quality' business has allowed us to invest confidently through the recent market volatility. We expect more market volatility as China may require more stimulus to offset structural issues. However, WHC has numerous multiyear internal levers to maintain and improve the business quality beyond cyclical commodity price movements: cost reduction and production improvement in the acquired metallurgical coal mines, paydown of the deferred BHP acquisition payments, Vickery expansion & selldown, Daunia/Winchester South expansion & selldown and further disciplined capital management.

### *Key Detractor – Light & Wonder (LNW AU)*

LNW was the largest negative contributor to performance during the month, falling 18% in September. LNW received a "preliminary injunction" order from the US District Court of Nevada, stopping the commercialisation of the new and popular Dragon Train franchise globally. LNW is a global, cross-platform gaming company, and is one of 3 dominant players (with Aristocrat and IGT). LNW is dual listed in the US, having listed on the ASX in mid-2023.

LNW has been a core part of the portfolio since inception. We recognized significant upside potential from improving business quality as LNW focused on reinvesting in content creation and monetization of new content across multiple platforms. The preliminary injunction likely means LNW will lose the full court case to Aristocrat. While this is disappointing, LNW is more than a single game franchise, with Dragon Train one of many successful new games, generating less than 5% of earnings for LNW. Damages are also unlikely to be material, likely less than 1% of LNW's market cap. The market reaction appears excessive but understandable given the short-term uncertainty. We view this set back as a short-term opportunity within a multi-year 'improving quality' story for LNW, with a strong pipeline of new content and the reinvestment flywheel and scaling of the business continuing to deliver strong and improving financial metrics.

## Outlook

The portfolio underperformed a strong market in September, with LNW being the key driver of the underperformance. This is not unusual in a concentrated portfolio with large positions; however, we do not believe the LNW investment thesis is broken and expect to claw back this stock-specific underperformance with time.

A continuing theme of recent commentary is that this remains a highly uncertain economic environment. Financial markets appear polarized, with bond markets pricing significant rate cuts towards a hard-landing outcome in the US, while equity markets at all-time highs are pricing a soft-landing outcome. This mixed environment tends to be rewarding for high quality companies as earnings certainty becomes a rarer commodity. We believe our portfolio companies are well placed into this dynamic.

The Chinese stimulus announcements while positive, do not appear enough to turnaround the struggling Chinese economy and will likely require further stimulus. However, with developed market Central Banks now moving into an easing cycle (US, EU), this provides capacity for China to continue to stimulate without impacting their currency. We continue to invest in high quality miners with low costs, disciplined management and multiple internal improvement levers to navigate through commodity volatility.

There was one portfolio change in September with 1 new position added. The new position is a technology business that is on the cusp of significant financial improvement that appears underappreciated by the market. We see strong upside over the medium term for this 'early quality' business as it monetizes and scales. This is an exciting opportunity that we have seen previously with other technology businesses that we have invested in. This portfolio change is driven by our continuous tandem goals of improving the overall Quality Score of the portfolio whilst maintaining a highly attractive portfolio level risk/reward skew.

Thank you for investing alongside us, Mike & Tim.

## How to Invest

To invest click on the link [www.blackwattlepartners.com/invest/](http://www.blackwattlepartners.com/invest/) or call 02 7208 9922.

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