Blackwattle Global Quality Fund

Blackwattle Investment Partners

December 2024

About the Fund

The Blackwattle Global Quality Fund is a high conviction long only fund that aims to provide exposure to the highest quality companies in the world, trading at attractive valuations. The fund adopts an 'All-weather Quality' approach for investing.

Our approach recognises a company's persistent competitive edge and the durability of earnings power allowing for the compounding of capital over the business cycle.

Risk is managed through portfolio and stock exposure limits and process discipline.

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

Fund Name	Blackwattle Global Quality Fund
APIR	ETL1392AU
Inception Date	May 2024
Typical no. of Stocks	20-35
Cash Limit	10%
Cash Distributions	Semi Annually
Redemptions	Daily
Buy Sell Spread	0.25% upon entry 0.25% upon exit
Fees	Management 0.90% | Performance 12.5%
Objective	The Fund aims to outperform the MSCI AC Net World (after fees and before taxes) over the long term. To deliver performance of 8-12% p.a over the long-term.

Investment Team

Sunny Bangia

18+ years' investment experience. Previously Co-Founder and Portfolio Manager of Antipodes Partners, and Co-Portfolio Manager of Antipodes Global funds and lead Portfolio Manager of Antipodes Asia Fund.

Edward Li

8+ years' investment experience. Previously Investment Analyst at Antipodes Partners (Global Strategies). Investment Associate at Colinton Capital Partners and Investment Banking Analyst at Macquarie Capital

Nicholas Tan

13+ years' investment experience. Previously Senior Investment Analyst at Antipodes Partners (Global and Emerging Markets) and at Platinum Asset Management

Fund Performance[1]

Blackwattle Global Quality Fund Performance (net of fees) as of 31 December 2024.

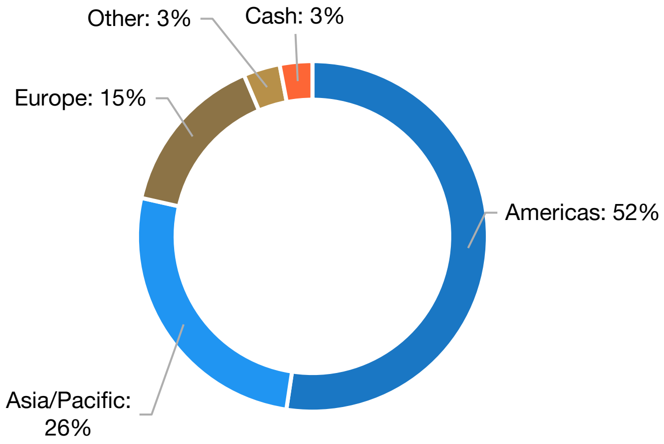
	1 month	3 months	6 months	1 Year	2 Years	3 Years	Inception p.a[2]
Fund (Net)	2.34%	13.27%	14.78%	-	-	-	21.69%
Benchmark[3]	2.73%	10.94%	13.86%	-	-	-	18.08%
Active Return	-0.39%	2.33%	0.92%	-	-	-	3.61%

[1] 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.
[2] The inception date for the Fund is 2 May 2024
[3] MSCI AC Net World (AUD)
*Inclusive of Goods and Services Tax (GST) and net of any Reduced Input Tax Credits (RITC).

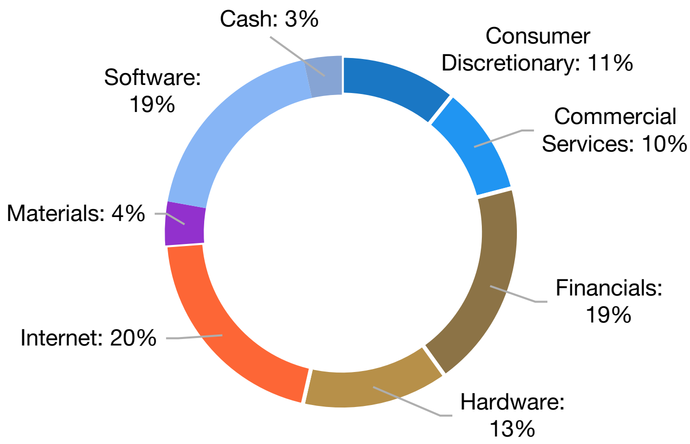
Top 5 Holdings

amazon MSCI Microsoft mastercard FICO

Geographic Revenue Exposure



Sector Exposure



Portfolio Commentary

The Blackwattle Global Quality portfolio underperformed the MSCI AC World Index (AUD) by -0.39% during the month.

Key Contributor –Amazon

Amazon had a positive month following its recent earnings call, with attention drawn to the growing adoption of its Trainium chip. Trainium is Amazon's inhouse GPU chip which competes with Nvidia. During the call, management noted higher than expected demand, stating they had to "go back to our manufacturing partners a couple of times now to produce a lot more Trainium than we anticipated." This was consistent with comments made from certain suppliers in the semiconductor supply chain.

At Invent 2024, Amazon's annual cloud conference, the company introduced its next generation Trainium chip, called Trainium2. While Trainium2 delivers slightly lower performance compared to Nvidia's H200, Trainium2's lower pricing allows for a 30-40% better price performance ratio. Trainium2 provides Amazon's customers more choice of GPUs across the price-performance spectrum, which is a key differentiator against other cloud service providers.

Amazon also announced their next generation Trainium3 which is expected to launch later in 2025. Trainium3 is expected to further increase compute performance by twice compared to Trainium2.

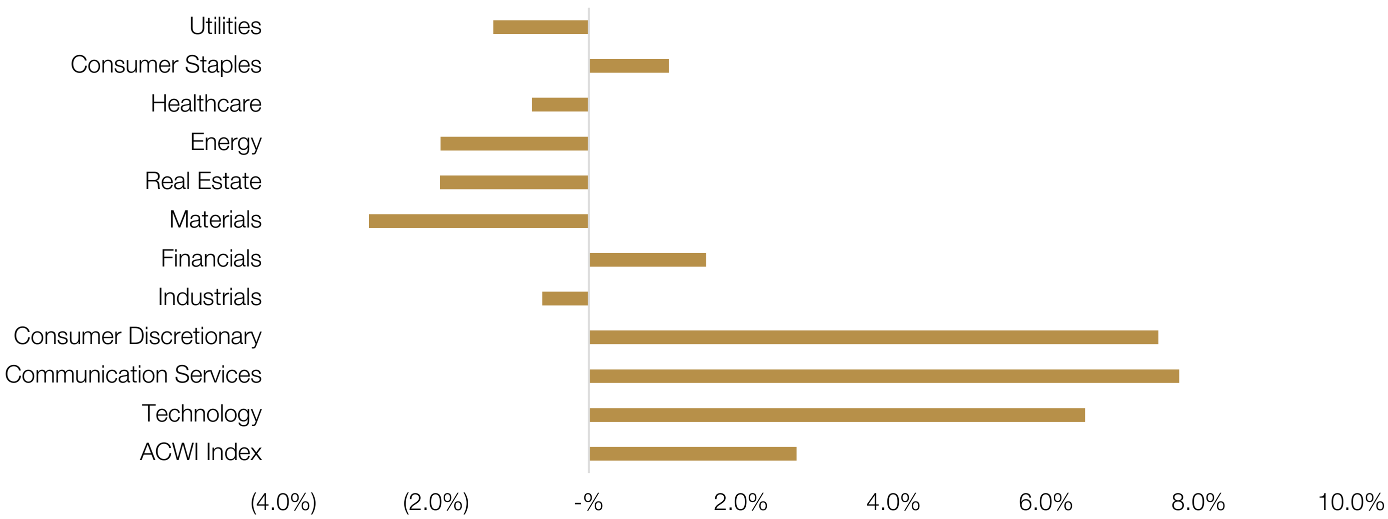
Key Detractor – Fair Isaac

FICO contributed negatively to the relative performance of the fund as the share price had a period of consolidation after an extraordinarily strong run over the course of 2024. As US interest rates rose both in treasury yields and mortgage rates, led to lower confidence in the recovery of the US housing market and mortgage originations. While FICO does benefit from the eventual recovery in mortgage volumes the larger value driver for the business remains that it is raising the price per FICO score which has remained flat for twenty years.

Market Commentary

In December 2024, the MSCI AC World Index (AUD) rose by +2.73%, driven primarily by strength in Technology & Consumer Discretionary. In contrast, Materials, Energy, and Real Estate detracted. The gains were supported by market optimism around policy clarity following the U.S election. Additionally, robust economic data showing signs of resilience in global growth.

MSCI ACWI December returns (AUD) (%)



December closed out the year with a focus on central bank policy, global economic growth concerns, and the early impact of fiscal measures from the newly inaugurated U.S. administration. Equity markets showed resilience despite lingering uncertainty over geopolitical tensions and mixed economic data, as investor sentiment benefited from a seasonally strong December rally and optimism about 2025.

In the U.S., markets stabilized following November's volatility as investors digested the first details of the incoming administration's economic agenda. Proposals for corporate tax cuts and infrastructure spending sparked gains in industrial and financial sectors, while technology stocks regained footing after clarity on trade and regulatory policies. The Federal Reserve lowered rates by 25 basis points during its December meeting, citing ongoing economic resilience and an improving labour market, but maintained a cautious tone regarding inflation, signalling a measured approach in 2025.

European equities ended the year on a positive note, although challenges remained. The ECB held rates steady, reiterating its commitment to supporting growth while expressing concerns about weaker-than-expected inflation. Improved trade prospects with the U.S. under a more predictable administration provided a modest tailwind, particularly for export-heavy economies like Germany. However, political uncertainty in the Eurozone persisted, with upcoming elections in key member states likely to shape the region's economic outlook.

In China, a combination of fiscal stimulus and targeted monetary easing fuelled optimism about the economy's trajectory into 2025. Retail sales data exceeded expectations, reflecting stronger domestic demand during the holiday season. However, property market weaknesses and the continued unwinding of excessive corporate leverage remained concerns. Market participants are watching closely for further policy clarity at January's National People's Congress, where additional measures may be unveiled.

Emerging markets experienced divergent performance. Commodity-exporting nations benefited from higher energy and industrial metal prices, while countries with significant external debt faced pressure from tighter global financial conditions. Despite challenges, emerging markets overall saw net capital inflows in December, a positive signal for their resilience heading into the new year.

December's themes underscored the delicate balancing act central banks face between fostering growth and controlling inflation, while fiscal policies are increasingly taking centre stage. As markets transition into 2025, investors will be closely monitoring the impact of U.S. fiscal initiatives, ECB policy adjustments, and China's continued reform agenda. The interplay of these factors, alongside geopolitical developments, will shape the trajectory for global markets in the year ahead.

Feature stock – Microsoft

Microsoft is the largest software vendor in the world by revenue. It operates multiple business segments including software, hardware and cloud services. Microsoft is a market leader in most of the industries it operates in:

- Microsoft's Office suite (Word, Excel, PowerPoint, Outlook, Teams, etc.) is the largest and most widely used SaaS application globally, with over 400 million paid business users and over 80 million paid consumer users
- Microsoft is the largest database software provider globally with Microsoft SQL and Azure SQL database offerings
- Azure generated over $60b revenue and is the second largest cloud service provider following Amazon
- Microsoft is the largest cybersecurity software vendor globally, generating over $15b revenue
- Windows is still the most dominant PC operating system

Competitive Advantage

Microsoft's key advantage is being able to leverage its dominant position in one market to gain market share in another

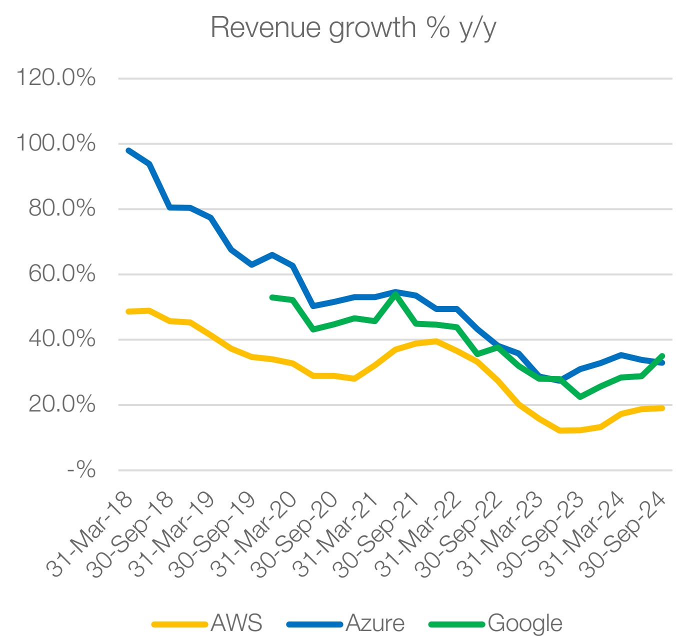
For instance, Microsoft has a dominant position in on-premises database market with Microsoft SQL Server. When customers transition their on-premises data centers to the cloud, the path of least resistance is to move to Microsoft's Azure cloud as customers are able to retain their existing software stack. This is the key value proposition of Azure over Amazon's AWS cloud service. It is for this reason that Microsoft is expected to surpass AWS as the largest cloud service provider by 2030.

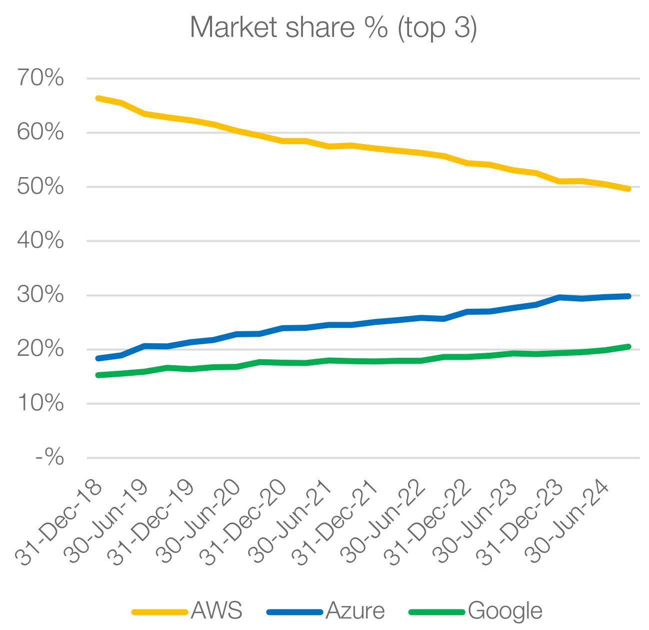
One of the key value propositions to Microsoft Dynamics 365 enterprise resource planning (ERP) and customer relationship management (CRM) software is its familiarity of its user interface and native integration with Microsoft's Office suite (Word, Excel, PowerPoint, Outlook, Teams, etc.). Microsoft's dominant position in Dynamics 365 and Office 365 also allows it to easily cross sell its cybersecurity software solutions.

Runway For Growth

Despite its large revenue base, Microsoft still has a long runway for growth. Azure cloud services and Office 365 represent over half of Microsoft's total revenue.

Azure is the second largest cloud service provider generating over $60b revenue in the last twelve months. Today, total cloud penetration of enterprise workloads is approximately at 23%. That is, more than 3/4 of enterprise workloads still remain on-premises within company data centers. Cloud penetration increases approximately 3-4% p.a., which provides strong visibility into its runway for growth. Even at this scale, Azure grew 33% in the last quarter and management expects Azure's growth to accelerate in the first half of calendar year 2025.





Office 365 is used by over 400 million enterprise employees and generates almost $70b revenue. Microsoft's AI software solution called Microsoft 365 Copilot represents a significant revenue growth opportunity to Office 365. Copilot is currently priced at $30/user/month. This compares to Office 365's average revenue per user per month of approximately $10/user/month. This means that Microsoft 365 Copilot represents a potential 3x revenue uplift opportunity. Just a third penetration of its user base could lead to a further $70b in revenue.

Copilot thus far has seen mixed user reviews. Some users criticize the AI for getting things wrong, i.e. "hallucinations". However, there is a concept called the "first version trap" popularized by Andy Grove in his book "Only the Paranoid Survive":

"When you think about it, first versions of most things usually are [disappointing]. Lisa, the first commercial computer with a graphical user interface and the predecessor of the Mac, did not receive good acceptance. Neither did the first version of Windows, which was considered an inferior product for years—DOS with a pretty face, as many called it. Yet graphical user interfaces in general, and Windows in particular, have become "10X" forces shaping the industry. My point is that you can't judge the significance of strategic inflection points by the quality of the first version"

Just as computer graphics and software became better as Moore's Law continued to progress, we should expect Copilot and AI performance to become better as large language model (LLM) scaling laws continue to progress. As AI becomes 'smarter', the AI applications will become better, and we should expect greater adoption of Microsoft Copilot among Office 365 users.

Vertical integration

There is ongoing debate as to where most of the profit capture will be in the value chain for AI software. Currently, frontier large language models (LLMs) are increasingly commoditized, with the price of using such models falling rapidly. The price of Nvidia GPUs powering AI applications is also falling on cloud service providers. Some software companies have experienced a positive re-rating on their stock as they launch their AI software solutions.

No matter where the profit capture lies in the stack, Microsoft is well positioned to capture that value as it is the only fully integrated player with a scaled offering at each layer of the stack.

Chips and hardware	Microsoft NVIDIA	• Inhouse AI chips e.g. MAIA 100 AI accelerator • Major supplier of Nvidia GPUs on Azure
Cloud computing	Microsoft	• Currently over $10b annualized revenue in AI cloud computing
AI models	Microsoft OpenAI	• Investment in best-in-class OpenAI models
AI middleware tooling applications	Microsoft	• Extensive tools such as Microsoft Fabric and Microsoft Copilot Studio
AI end user applications	Microsoft	• Microsoft Copilot priced at $30/user/mth
End users	Microsoft	• Over 400m existing commercial Office 365 users

- Microsoft is the largest buyer of Nvidia GPUs, as well as designs its own competing GPU called MAIA 100
- Microsoft currently generates over $10b annualized revenue in AI cloud services on Azure
- Microsoft invested $1b (2019) and $10b (2022) into OpenAI for approximately 49% ownership stake. Today, OpenAI is valued at $157b
- Azure has one of the most extensive AI application development platform called Microsoft Fabric and Microsoft Copilot Studio
- Microsoft has launched some of the most widely used AI solutions today including GitHub Copilot, Microsoft Copilot and Dynamics 365 Copilot, and ChatGPT via OpenAI
- Microsoft has some of the largest user bases to surface AI products
  - Over 400m Office 365 commercial users
  - Over 80m Microsoft 365 consumer users
  - Over 100m developers on GitHub
  - Over 1.5b Windows users
  - Over 44,000 Dynamics 365 customers, with over 20 million users
  - Over 100m daily active users on Bing

How to Invest

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

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