

AIRLIE AUSTRALIAN SHARE FUND UPDATE - Q4 2024

Emma Fisher discusses key drivers and insights from the recent quarter and how the portfolio was positioned to navigate the market. Emma also highlights the best performers for the fund and outlines opportunities the team continues to monitor as we move into 2025.

The Australian share market has had an interesting year, with the standout story being the surge in bank share prices. The Airlie Australian Share Fund, however, is underweight in banks, which has been a costly position. How are you maintaining your conviction in this stance?

The rise in the share prices of the big four Australian banks has been the top news story of the year, with an average increase of 33%. However, we believe this headwind is temporary, as the rally has been driven by interest rates rather than fundamentals, which have actually worsened. The commoditisation of mortgages and the shift to mortgage brokers have led to a price frenzy, deteriorating the banks' returns despite their rising share prices.

For example, Commonwealth Bank, the best in terms of quality, has a return on equity of 13% but is trading at 26 times earnings, an unprecedented level for any bank globally. Our portfolio includes businesses with much better returns and cheaper valuations, reinforcing our conviction in our positioning. Our investment process favours companies with strong financial strength, solid balance sheets, high-quality business structures, good management teams, and attractive valuations. Most banks currently fail to meet these criteria, especially with new management teams at three of the four major banks.

The focus for 2025 is to move beyond the current issues with Australian bank valuations and continue to follow our disciplined investment process.

Mineral Resources has been a hot topic this quarter due to the allegations against Chris Ellison. Could you explain how you're addressing these issues and what actions you've taken regarding your position in the stock?

In response to the governance crisis at Mineral Resources, we significantly reduced our position. We recognise that Chris Ellison has been a phenomenal value creator for the company, with numerous successful deals. However, the ongoing pattern of governance issues, including the alleged offshore tax evasion scheme, makes his position untenable in our view. On the facts that we know today, the board's decision to give him 12 to 18 months to find a successor seems balanced, considering the company's current debt levels and the need to ramp up production at Onslow project.

The ramping of Onslow, a large iron ore asset, is critical for the business and the share price in the near term. However, the complexities of the project, including the use of transshipping and the historical challenges of mine ramps, pose significant risks. Perfect execution is required for the share price to perform well, which we believe is unlikely.

Despite the reduced position, we remain open minded, there are scenarios in which we would re-enter the business if we felt that the devaluation accounted for all of these risks but for now, we continue to monitor the situation closely. But as it stands today, we have substantially reduced our position.

Sigma has been one of the top performers for the fund this quarter, especially after the State approved its merger with Chemist Warehouse. Given its strong performance, how are you currently evaluating this position?

Sigma had an impressive quarter, returning 82%. This surge was driven by ACCC approval of its merger with Chemist Warehouse. Despite its high valuation, we see Sigma as a fantastic long-term investment, ideal for

holding over the next 10 to 20 years due to its strong earnings compounding potential.

The company has proven its profitability and success through its store expansion strategy. With nearly 500 stores in Australia, there is still significant growth potential, especially if the store density in other states matches that of Victoria. Sigma has also seen success in New Zealand and Ireland, with plans to double its store count in these regions. The potential for further international expansion, possibly using Ireland as a launching pad into Europe or the UK, adds to its attractiveness.

Overall, Sigma's ability to improve store economics as it grows, combined with its strategic expansion plans, makes it a compelling long-term investment. The company is expected to continue its strong performance, much like other successful retailers that have shown consistent growth over time.

Have you made any other changes to the portfolio towards the end of the year?

In December, the ASX fell by 3%, largely due to the U.S. Federal Reserve's revised dot plot forecast, which indicated fewer rate cuts next year. This caused market volatility, but we saw it as an opportunity. For instance,

BlueScope's share price dropped by 15% despite no change in its fundamentals, so we added to our position. Similarly, James Hardie's volatility throughout the year provided attractive valuation points, allowing us to strengthen our core position.

We also made adjustments to other holdings. We trimmed our position in ResMed, which had performed exceptionally well, and reallocated some of that investment to CSL. CSL's core plasma business is showing strong demand, and we expect significant gross margin expansion and earnings growth in the coming years. Additionally, we increased our position in News Corp following their announcement to sell Foxtel. This move simplified News Corp's business and strengthened its core assets, making it a more attractive investment.

Overall, while there were no major changes, we took advantage of market volatility to optimise our portfolio and position ourselves for future growth.

Watch the video [here](#).

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