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Auscap Newsletter

JULY 2025

AUSCAP ASSET MANAGEMENT LIMITED

Will A Focus On Short Term Results Benefit Long Term Performance?

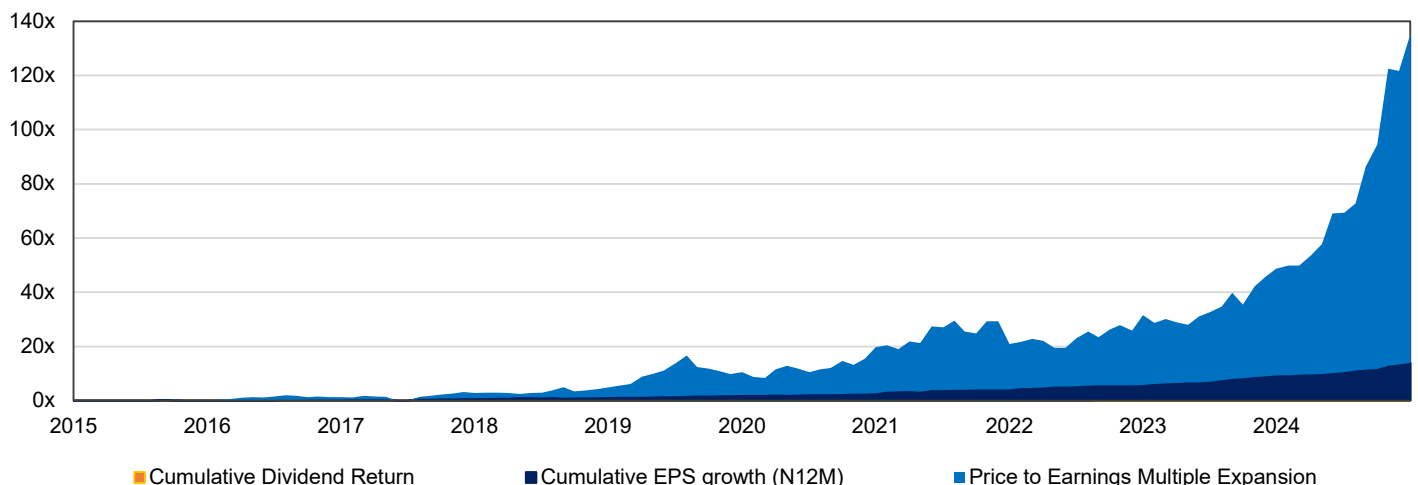
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Much is being made of the fact that the vast majority of active fund managers are overweight Commonwealth Bank of Australia (CBA). Its strong performance in recent years has led to widespread active management underperformance because it represents over 10% of the All Ordinaries Index. Should this positioning be criticised or encouraged? Is it sensible for investors to have over 10% of their domestic equities portfolios invested in a large domestic retail bank, or are fund managers acting rationally in being less exposed to this one company than the broader market?

If there is one certainty, it is that the future will not look like the past. No two sets of circumstances are the same. The companies that exist at various points are different. The reactions of governments and societies to events can vary. This makes investing challenging enough. But added to this, investment markets, if they were presented with the exact same scenario as one recently experienced, would react differently to the way they did initially, precisely because everyone would have the knowledge of how markets reacted to that event or set of circumstances previously. Some initial reactions to the COVID-19 pandemic were similar to those witnessed during the Spanish flu pandemic of the early 20th century, including the quarantine periods imposed, but because of that experience, changes in society and medical and technological developments, there were far more differences than similarities between the two periods. This is what makes investing an intellectually interesting exercise.

Markets are unpredictable. And so they do unpredictable things. Pro Medicus, a global leader in healthcare imaging software, is currently trading on more than 100x forecast FY26 revenue and more than 200x forecast FY26 earnings with a market cap that is bigger than Brambles, the global leader in pallet supply, Sigma Healthcare, the owner of the dominant pharmacy chain Chemist Warehouse or REA Group, Australia's leading property portal. It has a great product, a market leading position and lots of opportunities for growth, but so do these much larger companies that all earn more than five times as much as Pro Medicus. Why didn't the share price stop at 100x forecast earnings, or 75x, or 50x? Was it predictable that this would happen, and so as long as one was convinced of the progress of the product then one should have bought in?

Pro Medicus Total Shareholder Return Decomposition

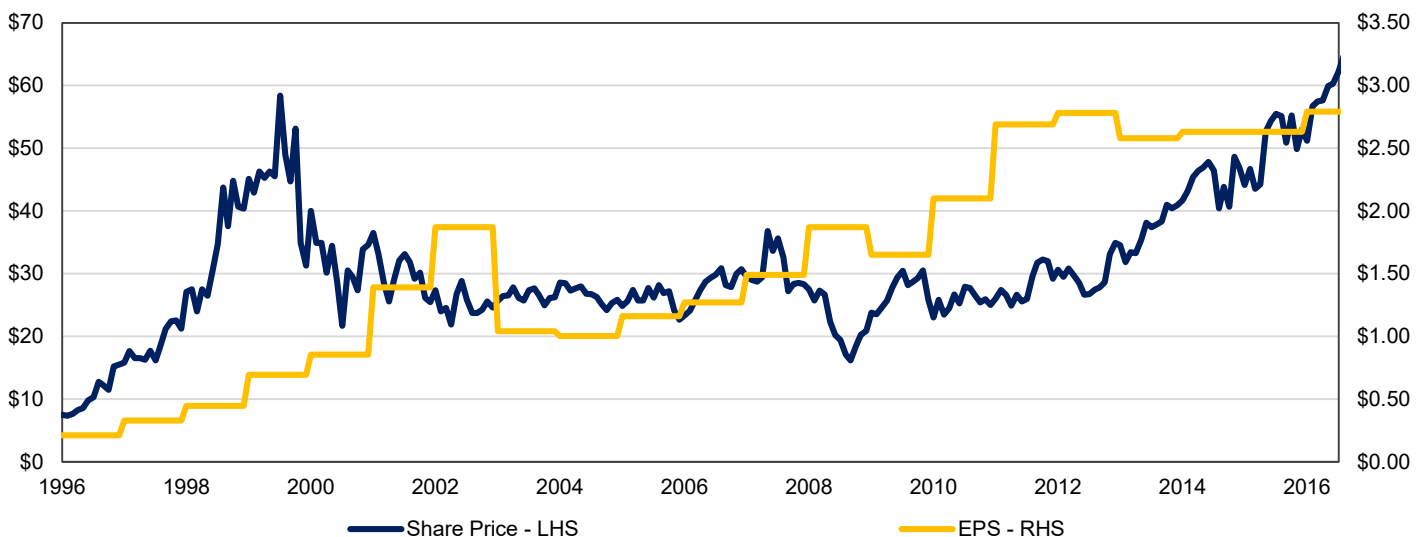


Source: FactSet, Auscap

Since 2015, Pro Medicus' forecast earnings per share (EPS) is up by an excellent 16 times, and the company has paid modest dividends. But an investment in Pro Medicus is up 132 times, meaning that multiple expansion, or paying more for each dollar of earnings, has been the difference between a \$100,000 Pro Medicus investment in 2015 today being worth \$1.6m and \$13.2m. There can be valid reasons for multiple expansion over time, such as an increase in the durability of a business moat or the demonstration of wider applicability of a product, but this level of contribution is extreme.

Will buying a business with great growth prospects on an extremely elevated price to earnings ratio always lead to an attractive shareholder return? It could, but if the ratio falls significantly in the near term, for whatever reason, it may take many years of sustained earnings growth just to breakeven. History is littered with examples where periods of extreme valuation are followed by periods of mean reversion. After the dotcom crash it took Microsoft 17 years to make a new stock high, despite remaining as the dominant global computer software company throughout this period and growing its EPS by over 285%.

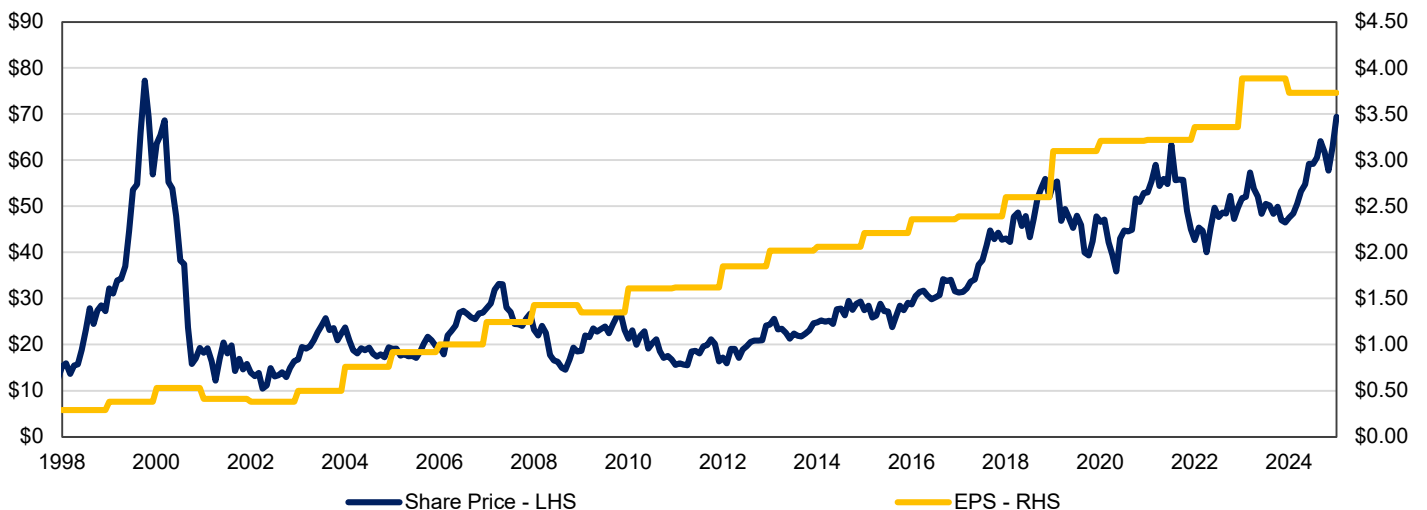
Microsoft Share Price & EPS



Source: FactSet, Auscap

Cisco, the multinational digital communications technology conglomerate based and listed in the USA, is today still not back to its peak share price that it made in 2000, some 25 years ago, despite EPS having grown over 600% during this period.

Cisco Share Price & EPS



Source: FactSet, Auscap

These companies were expected to experience strong EPS growth which led to investors rationalising elevated multiples at the time. Despite this being correct, investors who purchased near the peak were underwater on their investment for many years.

At the other end of the spectrum, who would have predicted a decade ago that the hottest stock on the ASX in FY25 would have been a domestic bank offering a low dividend yield and anaemic earnings growth, both historical and anticipated, in a competitive and largely commoditised domestic environment, while trading on the most expensive multiple of earnings that an Australian bank has traded on in the last 30 years? And yet, the same could have been said about CBA two years ago, and it has continued to perform strongly, rallying another 80%. We also suspect an objective outsider would recoil at the suggestion that more than 10% of a domestic equities portfolio should be invested in such a stock. That it has delivered such strong returns does not change the sense in having a lower exposure to the company. There are many possible paths markets can take and sensible investing involves making decisions that are likely to deliver satisfactory returns irrespective of the path that eventuates.

Our core belief is that successful long term investing is about having a sound process that will lead to solid results over time. A fixation on short term relative performance against an index risks damaging a sound investment process. The reality is that over the short term noise is highest and the performance of stocks can be driven by many factors, including those that have no relationship to company performance, such as the flow of capital. A focus on relative performance against an index also drives consideration of the constituents of the index, even though its composition is a function of what has happened historically and not what is sensible going forward. This all has the effect of taking the focus off the process and placing most emphasis on the outcome. To use a sporting analogy, this is akin to a golfer focusing on what score he or she is going to shoot, rather than playing each shot on its merits and focusing on the process of executing these individual shots. In our experience focusing on the outcome rarely works and is often counterproductive.

In our view the underweight in CBA by domestic fund managers appears sensible, assuming that in aggregate active managers are invested in businesses with better medium term prospects than CBA. To criticise the decision to be underweight such a stock is to focus on the result, rather than the process. And such conclusions can often lead to future decision-making mistakes. Short term market outcomes are often random, a function of market forces that at times have little to do with fundamentals. A focus on short term results will have the tail wagging the proverbial dog and, we are confident, lead to poorer long term outcomes.

To deal with uncertainty we continue to focus on our investment process. We aim to own a selection of market dominant, high quality businesses with good long term growth prospects, with discipline around the price we are willing to pay for and hold onto these investments. Our core belief is that the total return delivered by equities over time will be a function of the earnings they generate today plus the growth in earnings they deliver, assuming we have not materially overpaid in acquiring the asset in the first place. So our focus is on identifying these businesses and paying a fair price or better for them. This will certainly lead to *different* results from the index, with the objective of more attractive longer term returns.

Auscap High Conviction Australian Equities Fund

Fund Performance*

Period	Auscap	All Ords
June 2025	(0.2%)	1.4%
Financial Year To Date	12.4%	13.2%
Since Inception (Dec 2012)	462.2%	220.0%
Annualised Returns	14.7%	9.7%

Fund Exposures

June 2025 Average	% NAV	Index
Equities	95%	100%
Cash	5%	0%
Beta Adjusted Exposure ⁺	98%	100%
Positions	43	499

Portfolio Commentary*

The Fund returned negative 0.2% net of fees during June 2025. This compares with the All Ordinaries Accumulation Index return of 1.4%.

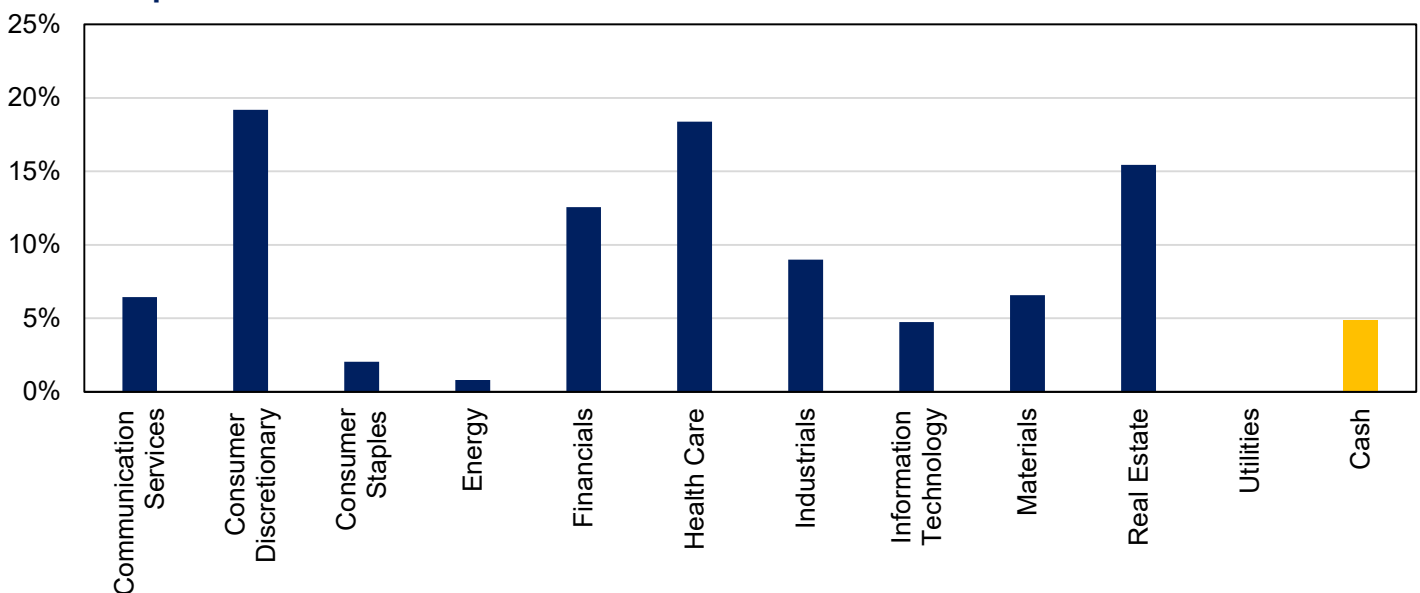
During June, the Fund’s exposure to the financials sector contributed most positively to returns, while exposure to the consumer discretionary sector was the most significant detractor.

Over the month, Macquarie Group was the largest positive contributor to performance. Nick Scali was the most significant detractor from performance.

Top 20 Investments[^]

ARB Corp	Macquarie Group
AUB Group	NIB Holdings
Breville Group	Nick Scali
CAR Group	Qube Holdings
Charter Hall Retail REIT	REA Group
CSL	Reece
Eagers Automotive	Reliance Worldwide
HomeCo Daily Needs REIT	Resmed
IDP Education	Sonic Healthcare
Life360	WiseTech Global

Sector Exposure - June 2025[#]



* Performance figures are calculated for the Monthly Class net of all fees and expenses and assuming the reinvestment of all distributions. Note, as at 1 January 2021, the Series Class was consolidated into the Monthly Class. Prior to 1 December 2024, the fund was called the Auscap Long Short Australian Equities Fund and was able to short sell and use leverage as part of its investment strategy. Past performance is not a reliable indicator of future performance.

⁺ Beta adjusted exposure adjusts the portfolio for the beta, or share price volatility, of the stocks relative to the All Ordinaries Accumulation Index.

[^] Top 20 investments in alphabetical order as at 30 June 2025.

[#] Average sector exposure during June 2025.

Auscap Ex-20 Australian Equities Fund

Fund Performance*

Period	Auscap	Index**
June 2025	(0.1%)	1.0%
Financial Year To Date	15.5%	16.4%
Since Inception (Dec 2023)	30.1%	28.6%
Annualised Returns	18.1%	17.2%

Fund Exposures

June 2025 Average	% NAV	Index
Equities	95%	100%
Cash	5%	0%
Beta Adjusted Exposure ⁺	96%	101%
Positions	55	280

Portfolio Commentary*

The Fund returned negative 0.1% net of fees during June 2025. This compares with the S&P/ASX 300 Ex S&P/ASX 20 Index return of 1.0%.

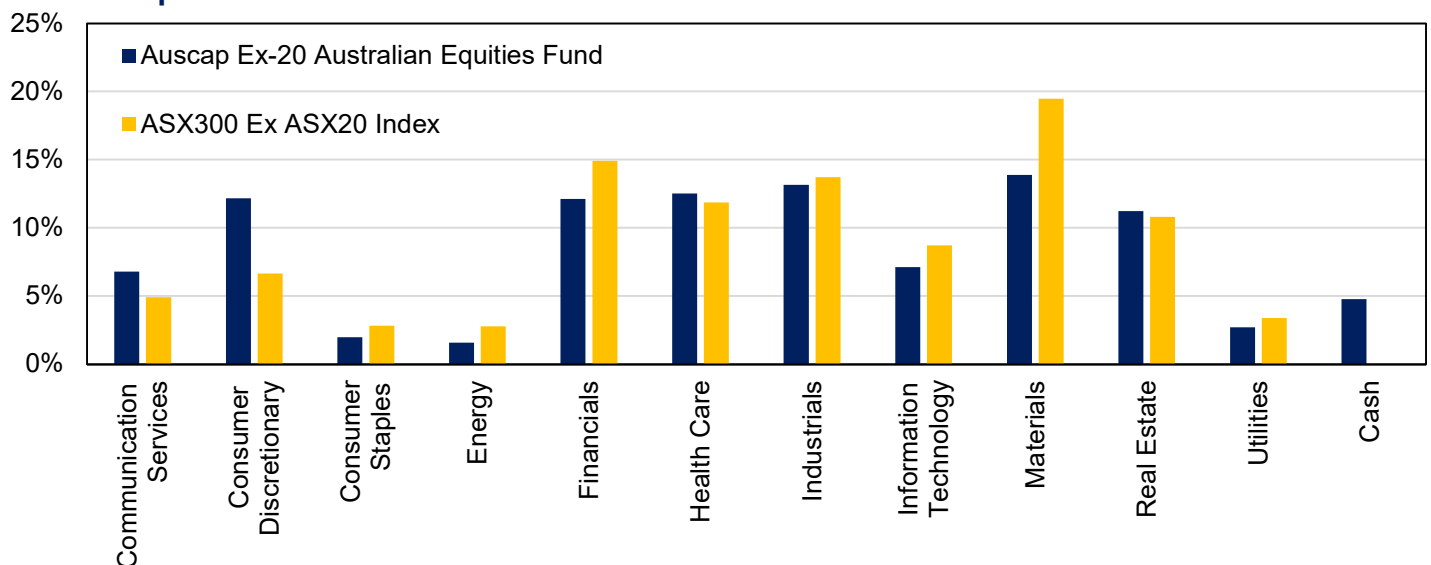
During June, the Fund's exposures to the financials and health care sectors were the largest positive contributors to returns. The Fund's exposures to the materials and consumer discretionary sectors were the largest detractors to returns.

The Fund's holding in Northern Star was the most significant detractor from performance.

Top 20 Investments[^]

ALS	NIB Holdings
Ancor	Nick Scali
AUB Group	Northern Star
CAR Group	Origin Energy
Charter Hall Retail REIT	Qube Holdings
Eagers Automotive	REA Group
Genesis Minerals	Reece
HomeCo Daily Needs REIT	Resmed
IDP Education	Sonic Healthcare
Life360	WiseTech Global

Sector Exposure - June 2025[#]



* Performance figures are calculated for the General Class net of all fees and expenses and assuming the reinvestment of all distributions. Past performance is not a reliable indicator of future performance.

** Index used is the Benchmark for the Auscap Ex-20 Australian Equities Fund, being the S&P/ASX 300 Ex S&P/ASX 20 Index.

⁺ Beta adjusted exposure adjusts the portfolio of the Fund and of the Benchmark (being the S&P/ASX 300 Ex S&P/ASX 20 Index) for the beta, or share price volatility, of the stocks relative to the All Ordinaries Accumulation Index.

[^] Top 20 investments in alphabetical order as at 30 June 2025.

[#] Average sector exposure during June 2025.

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