CI AUSTRALIAN EQUTIES FUND
QUARTERLY COMMENTARY REPORT

COOPER INVESTORS

AFS LICENCE NUMBER 221794
ABN 26 100 409 890

For current performance information please refer to the Monthly Performance Report.

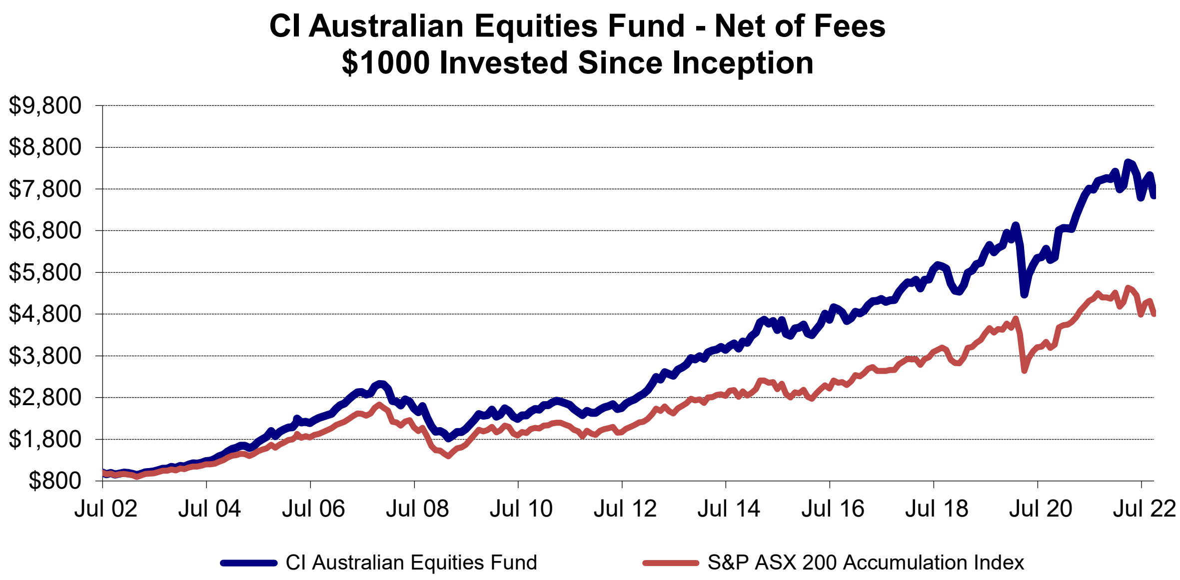
SEPTEMBER 2022

"The world which is arising is still half-buried in the ruins of the world falling into decay…and no one can know which of the old institutions…will continue to hold up their heads and which in the end will go under." **Alexis de Tocqueville**

"The worst calamity that can befall a nation is disunity." **Ahmad Kasravi**

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTH	0.88%	0.39%	0.49%
ROLLING 1 YEAR*	-3.87%	-7.69%	3.82%
ROLLING 3 YEAR*	7.02%	2.67%	4.35%
ROLLING 5 YEAR*	9.12%	6.76%	2.36%
ROLLING 7 YEAR*	9.55%	8.01%	1.54%
ROLLING 10 YEAR*	11.85%	8.41%	3.44%
SINCE INCEPTION*	11.68%	8.06%	3.62%
SINCE INCEPTION^	835.87%	380.41%	455.46%

*Annualised
^Cumulative (4 July 2002)
**Before fees and expenses
#S&P ASX 200 Accumulation Index
Past performance is not necessarily a reliable indicator of future performance



Source: National Asset Servicing

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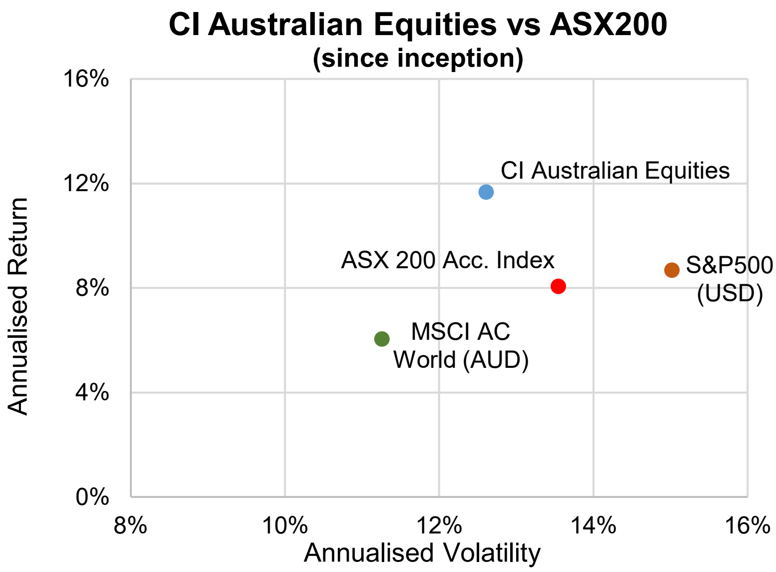

Market and Portfolio Performance

The ASX200 Accumulation Index rose marginally (+.40%) over the quarter. Stronger contributors to portfolio performance over the quarter included Oz Minerals (takeover bid from BHP), Wisetech (strong earnings result) and Qantas (rebounding as oil price retreated, passenger volumes rose and net debt reduced rapidly). The stocks whose performance over the period disappointed included TPG Telecom (end of year result weaker than market had anticipated), Orica (concerns around balance sheet given capital raising included $200m to cover working capital increase) and Ampol (falling oil price and refiner margin).

Our team travelled widely during the quarter, including visits to the US, Europe and UK. One consistent observation was the apparent disconnect between financial markets, which portend doom, and real world activity, which looks more like a boom. Airports and flights were full, despite sky-high airfares. Restaurants were packed, often requiring bookings months in advance. Streets were busy, people were buoyant. Full employment abounds – indeed almost every company has commented on the difficulty in finding appropriate staff. Markets, which are more forward-looking by nature, are of course concerned that this excess demand will further fuel inflation, leading to more monetary tightening, economic slowing and stock de-rating. Officials we spoke to are increasingly concerned about inflation too. Central banks need to act assertively to prevent a self-fulfilling wage-price spiral breaking out. This tightening of liquidity is unfolding against a backdrop of very elevated debt. The challenges are further compounded in Europe and the UK by supply-side shocks (e.g. Russia/Ukraine conflict), which are harder to address via monetary policy. The colliding spheres of sky high energy prices, rising interest rates, societal fragmentation, a rapid appreciation in the USD, close to double digit inflation and government subsidies (coming mere moments after huge pandemic related assistance) are a cocktail hitherto unseen by global markets – who for the last twenty years have seen only falling interest rates, broadly rising asset prices and the disinflationary effects of globalisation.

This cocktail of ingredients will be particularly tricky to navigate - the potential for misstep is high. Most policymakers and investors have never experienced such an environment in their careers. This situation is only exacerbated by the ability of (mis)information to flow wide and far with a speed that cannot be controlled. Interdependencies and second order impacts can be hard to judge, until it is too late. The Bank of England's recent intervention in bond markets, purportedly to prevent a solvency crisis in pension funds following a spike in Gilt yields, is a case in point. With such a divergent range of plausible outcomes, each with potentially significant impacts, it seems imprudent to stake our fortunes on bold predictions about the future. Instead, we are more focussed than ever on building a portfolio that is resilient to many different scenarios. This does not necessarily mean a defensive bias. Rather, we are keenly attuned to how risk-adjusted value latency is evolving across our various subsets of value, how such stocks and subsets might behave in different scenarios, and the interplay between them when part of a broader portfolio.

In the face of the circumstances outlined above, broad global industry trends we believe are durable and worth following include:

1. Decarbonisation and its impacts and opportunities;

2. Supply chain re-orientation by a number of large global companies – covid and the current rise in geo-political tensions have substantially upped the risk of single area (albeit cheaper) sourcing. The adjustment process will not be quick, nor will it be disinflationary;

3. The rising value of real trust (in a company or brand) in a world where trust is in short supply and easily eroded

4. Consistent with our observations on our trip to the US in March, employees are in no rush to return to the office. Investments made in state-of-the-art office space do not seem enough to drive traffic, with some of the iconic campus style offices in Silicon Valley only back to 25% utilisation. This issue will likely play out in the office property market over a number of years

The Portfolio

For the first time in a number of years, we have taken a position in **QBE** on the premise of an unfolding low-risk turnaround situation. Having promised so much for so long, only to regularly disappoint, there is an understandable market scepticism that this latest iteration can deliver. However, both our qualitative and quantitative observations lead us to believe that risks have reduced and this time is indeed different. Operating trends (e.g. pricing, investment yields) are favourable, its strategic position is improving as it exits weaker businesses and the unanimous feedback on the capability of new CEO, Andrew Horton, is very positive. There is already tangible evidence that years of restructuring are starting to pay off, with the Australia-Pacific and International businesses now consistently delivering solid margins. This leaves the North American business as the key to achieving higher and more consistent group profitability. Here we see a real intent and strategic clarity, including more management stability and aligned incentives, adjusting risk appetite/pricing more appropriately in volatile lines (e.g. catastrophe insurance), exiting/winding down businesses where QBE does not have an edge, taking out more protection (e.g. reinsurance, reserving, quota shares) and selectively pursuing growth opportunities (e.g. more scale in US mid-market). We like what we see so far.

We recently initiated a position in **James Hardie**, which we consider a high-quality cyclical with growth opportunities. James Hardie dominates the fibre cement industry, has attractive economics, a large opportunity set and strong management. However, it is also heavily exposed to US housing activity, which could come under growing pressure as interest rates continue to rise. Our approach has been to add exposure at prices where our stress testing suggests there is attractive risk-adjusted value latency. While new CEO, Aaron Erter, is a somewhat unknown quantity to Australian investors, his background in building consumer-led strategies and affable personal style suggest he is a good fit. We see clear long-term opportunity to drive greater repair and remodel (R&R) volume penetration in the Midwest and Northeast, along with margin upside from a higher value product mix. While obviously not immune to a housing downturn, volume trends will get some insulation from a growing skew to more resilient R&R activity (~65% now vs. sub-40% pre-GFC) and structurally higher mid-cycle margins given the success of the LEAN program so far.

Our investment in **Star Entertainment (SGR)** continues to underperform. The final reports from the independent reviews into SGR's suitability to operate casinos in NSW and Queensland have now been released with consistent findings: SGR is not currently suitable. SGR has subsequently been issued a "show cause" notice in NSW by the NSW Independent Casino Commission (NICC), after which they may face disciplinary action which could include termination or suspension of their casino licences, penalties, and enforceable undertakings. The Queensland government has indicated a similar notice will be issued in that state.

While a finding of unsuitability was expected, there is little doubt the content of the reports is confronting. We are extremely disappointed in the conduct of the company and management, particularly actions taken (or not taken) after similar inquiries for peer Crown Resorts had commenced and concluded. The reports have again given cause for us to review our initial rationale for investing in SGR, after reviewing when the initial allegations of misconduct were made in the media. At the time, we spoke to a wide range of industry participants that gave us comfort SGR's practices and processes were robust and industry leading. Although there was a view that certain events had occurred, our investigations failed to uncover the extent to which poor practices had permeated the entire Australian casino industry, including SGR, and we mistakenly came to the conclusion firstly that SGR behaviour had not been as flawed as that of Crown, and secondly that management had put in place practices and processes to address the problems. We therefore also misjudged previous board and management. Our process applies a higher bar to industries with elevated ESG risks, but we got this one wrong.

Looking forward, we intend to use our shareholding to support the reform of SGR. The company's 130 milestone remediation plan is a positive development and we intend use our influence to ensure it is properly executed. We believe it is in everyone's interests that reform is successful: SGR's employees, shareholders, the government and the broader community. The combination of an appropriate reform program driven by new management and the NSW government's recent amendments to the casino regulatory framework, should ensure SGR is truly a best in class casino operator. In fact, we believe the Australian casino industry should emerge from the current crises as the best regulated casino industry globally, which should ultimately attract a higher valuation for these businesses.

We do see favourable risk adjusted value latency at current share price levels. In our view, the value of SGR's property holdings largely underpin the current share price. Value latency lies in the company successfully reforming its casino operations, most likely under close scrutiny of an independent monitor and the regulator, a reversion from full reopening of operations post covid and the opening of new premises in in Queensland. Although now somewhat clouded and delayed, post SGR regulatory travails, the sale of the property would create further upside potential.

During the quarter **Orica (ORI)** announced a $650m capital raising. The raising was undertaken principally to fund the acquisition of Axis Mining Technology ($260m, or $350m if contingent payments are included), but was also needed to rebuild the balance sheet position in the face of the significant increases in working capital that the business has faced due to supply chain disruptions and elevated product pricing experienced over the last year. The advent of the war in Ukraine and the resulting trade restrictions with Russia has seen ammonia prices more than double, with related moves in ammonium nitrate pricing and ammonium nitrate product availability a major issue.

On the acquisition itself, Axis extends Orica's capability in orebody mapping. Axis is an industry leader in downhole geospatial technology, which fits with Orica's strategy in providing solutions that support mine to mill value chain optimisation. That said, the current Axis operation is focussed on exploration drilling, an area of the industry that is significantly upstream from Orica's business today. However, a significant amount of exploration drilling is done to define near mine opportunities and production related activities, activities that do sit within Orica's current mine production focussed operations. We also see the potential for the Axis technology to be utilised during the drill and blast process, which could potentially enhance real time ore body knowledge to aid optimised blast design. This would sit squarely in Orica's targeted service offering.

The capital raised in excess of the acquisition to fund working capital requirements is disappointing, although understandable in the circumstances. It evidences the disconnect between current market pricing and Orica's earnings - given the contract structure of Orica's vertically integrated supply chain, price rises will take around three years to fully flow through to earnings. It also highlights the negative free cash flow the company will deliver in the 2022 financial year. On a more positive note, it also highlights the strong industry pricing environment that exists and the strength of Orica's strategic positioning, which will underpin Orica's earnings growth over coming years. Additionally, the working capital demands which are a drain on cash flow and the balance sheet in 2022 will stabilise, as prices stabilise, and unwind over time as industry conditions stabilise and ammonia and ammonium nitrate pricing return to more normal levels.

We continue to see attractive risk adjusted value latency in Orica, with the operating environment and the industry outlook robust, combined with evidence of improved execution by Orica management. Unfortunately there will be little in the way of cash flow to show for this in the short term, however, we expect this situation to improve over the coming years.

During the quarter **Cleanaway (CWY)** raised $400mn of capital via an institutional placement and share purchase plan. The primary purpose of the raise was CWY's acquisition of a 100% interest in Global Renewables Holdings Pty Ltd (GRL) for $168 m at a 7.9x EBITDA multiple. GRL is a licensed composting facility in NSW that today processes 20% of Sydney's "Red Bin" household waste. For context, our industry analysis indicates both customer demand and government policy support for landfill diversion, resource recovery and emission reductions. One evolution of this is the separation of food organics and garden organics into "FOGO" bins which will be introduced into households across NSW by 2030. Organic waste that ends up in landfill creates greenhouse emissions and according to the Department of Climate change, Energy, Environment and Water, this accounts for 3% of Australia's total emissions. Organics compositing facilities such as GRL will play an important role in the FOGO bin transition and the associated benefits of diverting organics away from landfill.

CWY is already the exclusive contracted provider of waste to the GRL facility until 2032, underpinned by a number of council collections contracts. The acquisition of GRL advances CWY's strategy of becoming a vertically integrated waste operator who can offer these customers high circularity, low carbon solutions for waste collected via the Red Bin and eventually FOGO bins. Furthermore, diverting organic waste from the system to GRL will free up capacity at the Kemp's Creek site which can now be developed into a Construction and Demolition (C&D) site. CWY's acquisition of GRL and associated investment in facility upgrades is expected to generate a double-digit IRR. We participated in the raise on the strength of these factors

During the quarter, Justice Bromberg of the Federal Court set aside the environmental plan approval covering the drilling and completion activities in relation to **Santos' (STO)** Barossa gas project. The

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decision was based on a finding that the National Offshore Petroleum Safety and Environmental Management Authority (NOPSEMA) could not be lawfully satisfied that the plan demonstrated STO had consulted with each person it was required to under the regulations. This is despite STO engaging with both the Tiwi Land Council and the Northern Land Council, consultation consistent with previous practice. As a result, STO is required to cease drilling activities pending a favourable appeal outcome (likely to be heard in November) or the approval of a fresh Environmental Plan that STO believe could take up to 6 months. Whilst sufficient contingency within the project budget exists to cover such a delay (from both a cost and timeline perspective), the decision brings to light the heightened risk undeveloped oil and gas projects face in obtaining (and retaining in this case) environmental and other regulatory approvals relative to history.

In September, STO also announced the receipt of a binding offer from Kumul Petroleum to acquire a 5% stake in PNG LNG for an Enterprise Value of US$1.4bn subject to financing and other conditions. Kumul is Papua New Guinea’s national oil and gas company and an existing partner in the PNG LNG project holding ~17% of the project equity. The proposed purchase price is attractive and combined with a suite of latencies within the STO portfolio in addition to Barossa including Dorado, Narrabri, P’nyang, Papua LNG and Carbon Capture and Storage in the Cooper Basin, highlight the risk adjusted value latency underpinning the investment proposition.

As part of an investor trip hosted by **Lendlease (LLC)**, we met with US management and attended a number of development and construction site visits in New York and Boston. Core to our continued investment proposition in LLC is the reversion in development segment profitability in FY24 as gateway cities continue to recover from pandemic impacts. There are two key components to this, the first being a recovery in development Work In Progress (WIP) which now sits at a record $18.4bn and provides strong visibility into ~US$8bn of development completions in FY24. The second is the level of return on this development activity – and whilst on ground observations are positive, the extent of this reversion is not without risk particularly given the movements in interest rates and likely implications for commercial real estate cap rates. We continue to monitor this risk closely but remain positive around the reversion given the skew in completions in FY24 to both product not directly exposed to movements in cap rates and to where LLC’s equity holdings are high (Barangaroo apartments and Melbourne Quarter office). In addition LLC has in play build to rent projects where rental growth trends remain strong.

Early in August **OZ Minerals (OZL)** received an indicative takeover proposal from BHP at $25. The company had been trading just under $20. After assessing the proposal OZL’s board have rejected the proposal as undervaluing OZL. There are a number of potential synergies for BHP in the acquisition of OZL, in particular associated with the South Australian assets (Prominent Hill and Carrapateena), that are located near BHP’s Olympic Dam copper mine, and the nickel assets in Western Australia. That said, given the size and operating model of BHP it is unlikely that BHP will be able to operate in the agile value creating approach achieved by OZL, which would likely mean that many of the potential value creating opportunities that sit within OZL are less likely to be realised under BHP ownership. In our minds, if the takeover were to occur, the removal of the investment opportunity in a nimble copper focussed miner, with a management team that has a proven track record, would be a significant loss of future value creation potential.

Additionally, towards the end of the quarter, OZL announced final investment decision on the West Musgrave nickel/copper project in Western Australia. This decision was not unexpected as the project has been systematically progressed over recent years. The project itself is indicative of OZL’s approach. It will utilise vertical roller mills, that are not typically utilised in mining operations, that will enable high energy efficiency and enables the project to be run predominantly on renewable energy (circa 80%), with a pathway to being net zero by 2038. OZL has undertaken significant consultation with the local indigenous land owners, the Ngaanyatjarra people, with the signing of the Land Access Agreement being the key to enable the project to move forward. The project also opens up the province, which contains known mineral resources (the nearby Succoth deposit) that are not included in the initial project plan, and is a highly prospective region. This suggests further value creation potential exists within the asset and is indicative of why we would be reluctant to lose OZL as an investment opportunity.

CI Australian Equities Fund	****PORTFOLIO**	**#BENCHMARK**	**VALUE ADDED**
Financial Year Ending			
FYTD to 30 September 2022	0.9%	0.4%	0.5%
30 June 2022	-1.8%	-6.5%	4.7%
30 June 2021	28.0%	27.8%	0.2%
30 June 2020	-1.4%	-7.7%	6.3%
30 June 2019	7.8%	11.5%	-3.7%
30 June 2018	14.6%	13.0%	1.6%
30 June 2017	11.8%	14.1%	-2.3%
30 June 2016	6.9%	0.6%	6.3%
30 June 2015	13.7%	5.7%	8.0%
30 June 2014	19.8%	17.4%	2.4%
30 June 2013	31.9%	22.8%	9.1%
30 June 2012	-2.2%	-6.7%	4.5%
30 June 2011	15.6%	11.7%	3.9%
30 June 2010	12.7%	13.1%	-0.4%
30 June 2009	-18.2%	-20.1%	1.9%
30 June 2008	-12.7%	-13.4%	0.7%
30 June 2007	33.5%	28.7%	4.8%
30 June 2006	29.3%	23.9%	5.4%
30 June 2005	38.1%	26.4%	11.7%
30 June 2004	24.9%	21.6%	3.3%
30 June 2003	4.2%	-1.5%	5.7%
SINCE INCEPTION*	**11.7%**	**8.1%**	**3.6%**
SINCE INCEPTION^	**835.9%**	**380.4%**	**455.5%**

*Annualised ^Cumulative (4 July 2002) **Before fees and expenses # S&P ASX 200 Accumulation Index
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