Cooper Investors Global Equities Fund (Unhedged)

QUARTERLY COMMENTARY | MARCH 2024

AFS LICENCE NUMBER 221794 ABN 26 100 409 890

"Give them bread and circuses and they will never revolt". – Juvenal (1st century Roman poet)

"Thoroughly conscious ignorance is the prelude to every real advance in science." – James Clerk Maxwell (18th century physicist)

MARKET & PORTFOLIO PERFORMANCE

The portfolio returned 11.3% in the March quarter, versus the benchmark return of 13.2%.[1]

The biggest contributors were **Interactive Brokers** (underlying strong customer account and equity balance growth), **United Rentals** (seeing re-rating along with solid rental trends in core US markets) and **TSMC** (4th quarter results beat expectations along with accelerating AI demand trends).

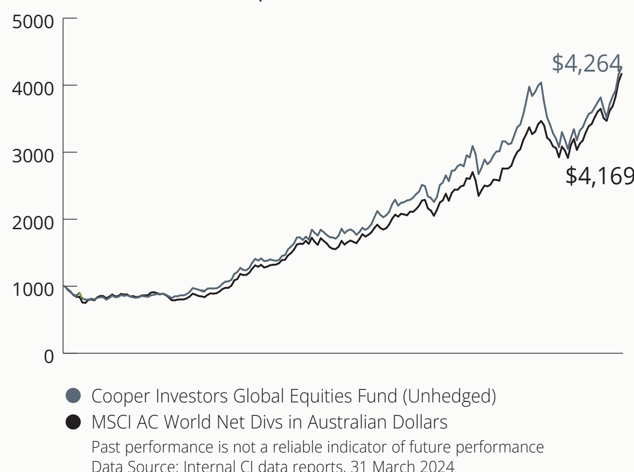
The largest detractors were **Liberty Broadband** (4th quarter broadband subscriptions growth weaker than expected), **HDFC Bank** (near-term net interest margins impacted by the consolidation of HDFC Ltd, which is largely wholesale funded) and **YUM China** (sold off in January with China market concerns though recovered later in the quarter after strong results, buyback, and store roll-out guidance).

The rally that began late October 2023 has continued into 2024. Driven by the ongoing surge in tech stocks linked to AI markets, the US is leading with the S&P500 making fresh all-time highs for the first time since the rate hiking cycle began. The S&P is up almost 25% in 6 months with most bears throwing in the towel regarding the 'recession that never came'. Our benchmark MSCI ACWI is similarly up almost 20% in 6 months, an impressive rally by most measures. We would however caution that with forecast earnings growth of 3% (over 6 months) this implies the bulk of benchmark returns have been driven by re-rating. We estimate the ACWI PE ratio is +13% over 6 months, versus the PE of our portfolio being roughly flat.

The AI theme is beginning to display hallmarks of a 'new paradigm' – parabolic growth forecasts and investment banks rushing to put out baskets of AI beneficiaries that have some link to the theme no matter how tenuous, ranging from the more obvious (semi-processor companies), to the less obvious (regulated power utilities). While market returns remain highly concentrated around these topics, there are early signs of broadening out with the S&P 500 Equal-Weighted Index outperforming its market-cap weighted equivalent by over 100bps in March.

	**Portfolio	#Benchmark	Relative
3 months	11.32%	13.16%	-1.84%
1 year	22.49%	26.49%	-4.00%
3 year*	9.45%	12.62%	-3.17%
5 year*	10.85%	12.81%	-1.96%
7 year*	12.04%	12.72%	-0.68%
10 year*	11.98%	12.54%	-0.56%
Since inception*	9.76%	9.60%	0.16%
Since inception^	326.47%	316.90%	9.57%

* Annualised
^ Cumulative (since inception on 1 September 2008).
# MSCI AC World Net Divs in Australian Dollars.
** Net of fees and expenses.
Past performance is not a reliable indicator of future performance.
Data Source: Internal CI data reports, 31 March 2024



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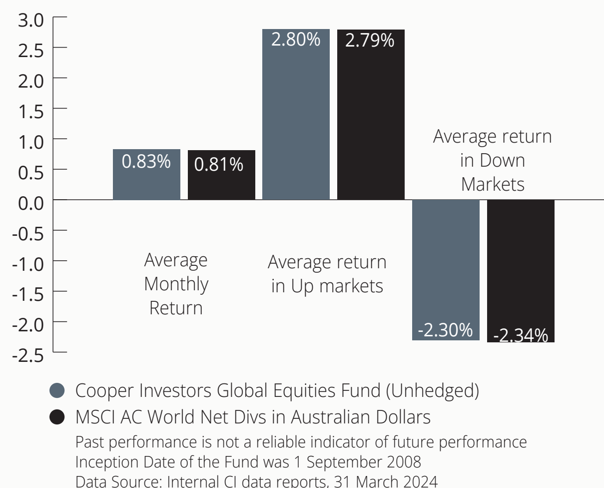
Data Source: Internal CI data reports, 31 March 2024



Past performance is not a reliable indicator of future performance
Inception Date of the Fund was 1 September 2008
Data Source: Internal CI data reports, 31 March 2024

1 Past performance is not a reliable indicator of future performance.

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Having spent time in the US during the quarter, the market's optimism is understandable. GDP growth has surprised to the upside, unemployment is low, supply chains have eased and a series of economic boomlets are happening in southern states (Texas, Georgia, Florida, Tennessee) where incoming capital investment is getting 'shovels in the ground'.

In this environment Growth (and to some extent Cyclicals) have continued to drive benchmark and portfolio returns. Defensive assets are seeing their worst period of underperformance for many years and our Stalwarts have also lagged. Ironically this could provide a window of opportunity in some great Stalwarts on a multi-year view. While the market is becalmed there remains considerable macro uncertainty this year including (but not limited to): the timing and extent of Fed Rate cuts, the US election, the US debt ceiling, the stability of the Chinese economy, the resolution of two ground wars in Europe and the Middle East, and the energy requirements of the AI build-out.

A company that welcomes uncertainty is **CME Group (CME)**, a Stalwart in which we recently reinitiated a position, having successfully invested historically. Value latency has re-emerged with the shares materially underperforming over the last five years.

As the largest derivatives exchange globally, CME offers leading liquidity pools to risk managers across multiple asset classes including equities, interest rates, FX, energy and agricultural commodities. The management culture at CME exemplifies the pragmatic, no-nonsense Midwest attitude that we admire of Chicagoans - no coincidence that the portfolio owns five Chicago-based companies today. This was reinforced in a recent meeting with newly appointed CFO Lynne Fitzpatrick. CME know what they are and what they're not, with a solid track record throughout market fads and blow-ups. The story of CEO Terry Duffy calling out Sam Bankman-Fried as 'an absolute fraud' (at the time he was lauded across the land as a visionary genius) is one recent example of their nose for risk.

We see several avenues for CME to grow earnings and cash flows today, irrespective of market volatility, as well as continuing to pay a special dividend implying a yield of ~4-5%. The business rarely changes hands as cheaply as it does today, trading at an average market multiple versus typically trading at a 30-60% premium. With this business routinely generating over 50% returns on invested capital and carrying no debt today, CME is far from an average business.

THE PORTFOLIO

The portfolio is positioned around Subsets of Value.

- **Stalwarts** (42% of the portfolio) – sturdy, strong and generally larger companies with world class privileged market and competitive positions (LSEG).
- **Growth companies** (22%) – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management (IBKR).
- **Cyclicals** (19%) – stocks showing both upside and downside leverage to the cycle with experienced and contrarian managers who allocate capital prudently (Ferguson).
- **Low risk turnarounds** (10%) – sound businesses with good management and balance sheets. (GE Healthcare).
- **Asset plays** (4%) – stocks with strong or improving balance sheets trading at discounts to net asset value or replacement value (AERCAP).
- **Bond-like equities** (3%) – stocks with secure, low-volatile dividends that can be grown and recapture inflationary effects over time (Ferrovial).

The portfolio is also diversified by Clusters of opportunity.

- **Digital Ecosystem** – Payments, SaaS, Marketplaces, Content
- **Niche Industrials** – Business Services, Manufacturers, Distributors
- **Emergent Consumer Growth** – Discounters, FMCG
- **Broker Models** – Insurance, IT, Property, Financials
- **Physical Infrastructure** – Toll Roads, Airports/Aircraft, Cable, Rail
- **Life Sciences** – Diagnostics, Testing, Consumables & Services
- **Data, Analytics & Exchanges** – Datasets, Tools and Financial Plumbing
- **Semis** – Semis and Production Equipment

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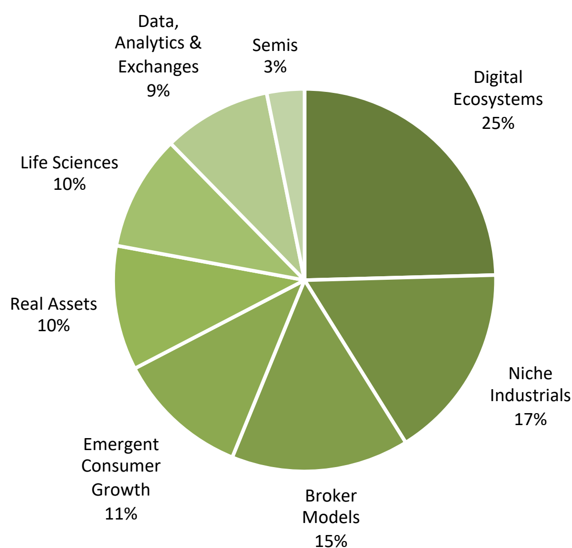
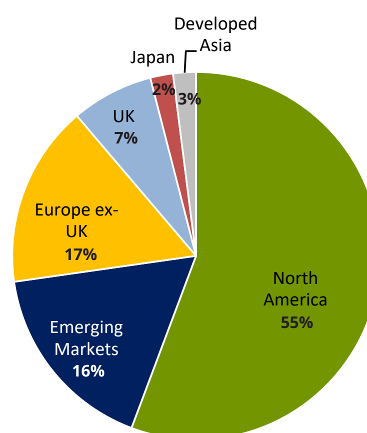
Portfolio by Cluster



Source: CI Internal Data

Geographical Exposure by Source of Revenues#



Derived on a look-through basis using underlying revenue exposure of individual Fund stocks

Source: CI Internal Data

No. of Stocks	39
Region Weights (by listing)	North America 66%
	Europe 24%
	Asia 9%
Most OW Sectors	Industrials, Financials
Most UW Sectors	IT, Energy
Cash	1%

Past performance is not a reliable indicator of future performance.
Source: CI Internal data, UBS Quant Answers, as at 31 March 2024

Portfolio Metrics – Weighted Average	
Price to Earnings [1]	20.7x
Price to Free Cash Flow [1]	21.2x
Net Debt to EBITDA [2]	1.1x
Return on Equity [2]	26.1%
Revenue Growth [2]	8.4%
Earnings Growth [2]	11.2%
Total Cash Yield [2, 3]	3.0%

1 Next twelve months forward
2 Estimated, FY1 to FY2
3 Estimated, dividends plus buybacks

One of the biggest industry crises we've observed in recent years is continuing to play out across the commercial aviation industry. After following the space for over a decade we recently invested in AerCap Holdings N.V (AER) which we see as an attractive and asymmetric Asset Play opportunity.

AER is the world's largest commercial aircraft owner and lessor. Aircraft leasing is a straightforward business and AER derives modest scale benefits from being the leading lessor globally. Over time AER has generated a return on equity in the low teens range and has compounded book value per share at ~14% p.a. from 2006 to 2023 while navigating many global crises along the way. We've been particularly impressed by CEO Aengus Kelly who has built a multi-decade track record of value creation through astute capital allocation.

This has included value accretive M&A, well-timed orders from large aircraft original equipment manufacturers (OEMs) at favourable prices (e.g. during the peak of COVID in 2020) and opportunistic share repurchases. As with any financing-type business, risk management of the balance sheet is particularly important. We note AER's management team have done an excellent job in this respect as well; liquidity is well managed and gearing levels are appropriate.

A key industry observation over the last couple of years has been the commercial aerospace sector's supply challenges. Simply put, the large airframers can't produce enough aircraft to satisfy demand. Deliveries from major OEMs in 2018 were roughly 1,600 aircraft. Five years later they mustered less than 1,300, despite a strong demand backdrop and healthy order books. The feedback through our ongoing engagement with companies across the value chain indicates no quick fix for the supply challenges.

Numerous obstacles must be overcome, including mismatched incentives across the supply chain and a shortage of skilled labour at key industry chokepoints. For example, a major

element of running aircraft is the need for scheduled servicing in the repair shop, either the airframe itself or with the engine taken off-wing for specific attention. Highlighting this on a recent call whilst discussing Maintenance, Repair and Overhaul (MRO), Aengus observed, "There is tremendous strain in the MRO network. When you have strain in a system, things rarely go well."

Technical problems with recently launched aircraft (see the news headlines around Boeing) and new generation engines are an associated outcome that only exacerbate the issues.

AER is a significant beneficiary of these dynamics as it owns an asset base in increasingly short supply. Market values for used aircraft are rising, as are lease rates. Today AER trades at roughly net book value, which we think undervalues the true value of the group. In 2023 AER sold over USD$2bn in used aircraft at an 80% premium to net book value, with aircraft sold to sophisticated buyers such as airlines and other leasing companies. This gives a good sense of the latent value on offer today for AER.

On the funding side, the portfolio fully exited Danaher during the quarter. We no longer see compelling Risk Adjusted Value Latency today with the shares rebounding 35% since the October lows and once again trading at a significant relative premium (50-60%), despite tough operating trends in the bioprocessing market. Having owned Danaher continuously for the past 14 years this is 'the end of an era' and so bears a brief tribute.

Danaher was the longest held stock in the portfolio having been initially purchased in July 2010. Investing alongside the Rales brothers has been an incredible experience. In returns generation, Danaher was a true 10-bagger; purchased at USD$25 a share and sold at ~USD$255, generating a return over the holding period of over 1,300% and an IRR of approximately 18%.

Yet its value has not merely been as a winning stock but also as a teacher, a source of idea generation, and a spin-off machine.

Danaher was the original 'Capital Allocator Champion', through which we learned about the margin-expansionary benefits of focused business systems operating with continuous improvement - Kaizens running concurrently on the lab or factory floor. We also built an understanding of how Danaher operates its M&A philosophy, a major driver of its success - what to buy, when to buy, who to buy from, how to integrate, and how much to pay. Studying this allowed us to develop Pattern Recognition of 'what good looks like' when meeting similar companies. Without Danaher, we may never have owned Domino Printing Sciences, Constellation Software, Halma, Roper, Ametek or Diploma, not to mention the spin-offs, some of which remain in the portfolio today. The business remains on our Watchlist through our continuous coverage of the Life Sciences cluster.

STOCK NEWS

Cooper Investors hold up five values as critical to how we operate our business – 1) Gratitude & Humility, 2) Intentionality, 3) Curiosity & Passion, 4) In the moment & present, and 5) Authenticity. Further details can be found on our website.

While these values influence our investment decision-making and guide our thinking through changing times, they're also what we look for in the cultures and management teams that we invest behind. A recent example worth highlighting is the Intentionality we observed at LSEG Plc (LSEG).

After the acquisition of Refinitiv (first announced in 2019) LSEG had a long execution to-do list in addition to managing a change in capital structure. Given the transformative size of the Refinitiv deal, LSEG could not pay entirely in cash and had to issue new equity as part of the consideration. This meant the selling consortium (consisting largely of Blackstone and Thomson Reuters) became the largest investor in LSEG, owning ~36% at deal completion.

A managed exit was structured such that, after a 2-year lock-up, three tranches of ~12% could be sold from January 2023, 2024, and 2025 onward. The consortium also controlled several board seats which would reduce in number as pre-agreed ownership thresholds were crossed on the way to zero. In market parlance, this situation represents an 'overhang', something markets dislike with investors wary of entering a stock story knowing a material amount of equity is due in future. This kind of overhang can linger over a stock for many years and drag on performance.

Here we have been impressed with the board's recognition of the impact on potential value creation and their Intentionality in getting it cleaned up as quickly as possible. This has been achieved through several means – accelerated direct buybacks (made possible due to strong operating cash flow generation), working with the consortium on timing of open market placings (taking advantage of periods of strong markets) and the partnership with Microsoft which involved them buying a 4% stake directly from the seller.

As the chart on the following page shows, after a recent additional placing the overhang is now close to gone almost 18 months ahead of schedule. This is an excellent outcome, especially while simultaneously reducing balance sheet debt and over-achieving on revenue growth targets.

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LSEG – Blackstone Ownership Evolution

Source: Company Disclosures, Redburn Atlantic

NORTH AMERICAN TRIP NEWS

The first quarter typically sees significant travel for the international investors at CI and this year was no exception with over 100 face-to-face meetings completed across the US (and Canada) in more than a dozen cities. Meetings covered fund holdings, peers, site tours, Watchlist stocks and potential new ideas, spanning almost all sectors of the economy.

Highlights are often the private site tours we undertake with portfolio companies, two worth discussing on this trip were with Louisiana Pacific (LP) and Eurofins Scientific (Eurofins).

LP is a business we invested in mid-2023 and represents a Low-Risk Turnaround where the proposition is a commodity-to-specialty transformation story. The company is a leading manufacturer of wood-based building materials produced from its 24 mills and finishing plants, comprising ~4bn sq. ft of Oriented Strand Board (OSB) capacity and ~2bn sq. ft of siding capacity. Historically, OSB was the core output of LP but is a commoditised product in which LP is a price-taker. Group profits and losses swung around and led to highly volatile earnings over the years for a business at the whim of the underlying OSB price.

Siding on the other hand is a genuinely differentiated product that gives LP pricing power and generates consistent incremental margins of 25-30%. Made in the same mills as OSB using engineered wood flake and embossed with a grain finish (a processing marvel we've witnessed first-hand at a mill in Upper Michigan), LP 'Smartside' is a sustainable way to wrap homes in an attractive durable substrate that is gaining popularity among small and medium builders.

CEO Brad Southern, an ex-forester that took over in 2018 having spent years in the siding business recognised the potential value in remixing the business from OSB to siding and is the architect of the strategy. This is being achieved by repurposing existing mills to increase siding capacity, innovating new high value products (e.g. pre-painted panels and lap board for the repair and remodel market) and improving brand awareness in the distribution network. LP have a significant opportunity to gain share from inferior substrates (e.g. vinyl and PVC) and, over time, displace some fibre cement from incumbents like James Hardie.

In Atlanta we visited a construction site of homes wrapped in LP siding and met with the owner of the building company who espoused the virtues of the product. It is cheaper, lighter, more durable, and easier to handle for small crews than fibre cement, which is heavy, brittle and breaks if dropped. This means less wastage and lower labour requirements on the job site, all of which saves the builder money. What's more, as it's made from real wood it looks better and allows the homebuilder to cite the carbon negative aspects of the project. The challenge for LP has been breaching the stronghold of relationships between James Hardie and the large volume builders in the US, which will take time. On this point, a recently announced nationwide supply agreement between LP and Lennar, one of the biggest homebuilders in the US, is highly encouragaing.

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In Pennsylvania we visited a key **Eurofins** site near Lancaster. This large laboratory campus principally serves the pharmaceutical industry, conducting a range of different testing services. The site was founded back in 1961 and served the local food industry before branching out into pharmaceutical services. Remarkably this one site has increased in size from a 2,500 sq ft facility in the 1960s to a 500,000 sq ft campus today. Eurofins owns land around the campus, ensuring future expansion of this site will be at low cost.

A key point of contention for Eurofins of late has been around its strategy to own more of their important sites like Lancaster globally. Having now inspected a few of these assets in person over recent years, we can clearly see both the strategic and financial merit of this decision. While it may depress cash flows in the near term, it will set the business up for lower cost growth beyond that.

The other key takeaway from our visit was the longer-term growth opportunity for Eurofins in pharmaceutical testing and related services. This is underpinned by longer term trends like the rising complexity of pharmaceuticals industry outsourcing. While COVID caused some noise for the broader industry, the digestion period is now largely complete allowing structural trends to again determine financial outcomes.

To finish with some high-level observations, we still see few signs of economic distress in the US today. While those at the bottom are struggling more, people with homes and jobs continue to spend and are managing debt servicing. A large payments company made the observation that wealthy people are once again benefitting from the wealth-effect of stock markets back to all-time highs.

One way to frame who's going ok and who isn't is to distinguish between 'Homes Owners' and 'The Rest'. Per Equifax, there are ~85mn home-owner households in the US, of which 40% are owned outright. Of the 60% with mortgages, 3 out of 4 are still on mortgage rates of less than 4%. These homeowners have enjoyed significant equity appreciation in the last few years, are employed and are spending (if not as profligately as they were).

'The Rest', typically lower income, renters, students and new migrants, are where more pain is being felt. Here there is evidence from consumer companies of value-seeking behaviours – trade-down, smaller packet sizes, white label versus premium brands. A large snack company made the observation that their pretzel brands were outperforming their popcorn brands as people can fill their stomach and feel satiated for USD$4, despite this being the less healthy option.

The strongest economic impulse continues to be felt in the South where we spent time in Atlanta. Georgia is booming with net migration and significant incoming investment in EV manufacturing (Hyundai and their supplier base), solar battery manufacturing, aerospace (Gulfstream expanding operations), and new AI-enabled data centres.

On this latter point, a step change in power demand is coming. We met a large power utility in Georgia that is now facing energy demand growth (as measured by retail Kilowatt Hour growth) forecast to grow 9% per annum, having previously grown 0-1%pa for the last 10-20 years.

AI-enabled data centres are due to account for 75% of this increase in load growth with those locations incredibly energy intense compared to standard data centres used for storage. Next-Gen AI data centres are planned or under construction in the Atlanta area that will soak up over 1,000MW (megawatts). This is roughly equivalent to the annual output of the recently commissioned Unit 3 at nearby Vogtle nuclear power plant, a troubled project which took 10 years and over USD$35bn to build.

It will be fascinating to observe how the unstoppable force of the energy hungry AI infrastructure build-out meets the immovable object of political commitment in the Western world to convert energy mix to renewables and wean grids off traditional fuel sources.

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