CI Brunswick Fund

COOPER INVESTORS

QUARTERLY COMMENTARY | MARCH 2024

AFS LICENCE NUMBER 221794 ABN 26 100 409 890

FINANCIAL YEAR	**Portfolio	#Benchmark
2024 FYTD	14.3%	13.3%
3 Year*	12.4%	9.6%
5 Year*	13.3%	9.2%
10 Year*	12.1%	8.3%
Since inception*	**15.3%**	**8.7%**
Since Inception^	**1552.0%**	**419.5%**

* Annualised
^ Cumulative (1 July 2004)
\# S&P/ASX 200 Accumulation Index
** Returns are gross of fees and expenses
Past performance is not necessarily a reliable indicator of future performance
Data Source: Internal CI data reports, 31 March 2024

"Our comforting conviction that the world makes sense rests on a secure foundation: our almost unlimited ability to ignore our ignorance." – Daniel Kahneman

QUARTERLY PORTFOLIO HIGHLIGHTS

For the March 2024 quarter, the CI Brunswick Fund returned +9.24% (gross, or before fees), which compares to the ASX200 Accumulation Index return of +5.33% over the same period.[1]

The Fund's Reversionary capital pool was the strongest contributor (+6.3%), followed by Real Assets & Income Securities (+2.16%) and Compounders (+1.0%), while cash contributed -0.22%.

Some of the Fund's outperformance in the quarter can be attributed to a reversal of the factors we spoke about in the December 2023 quarter. For example, iron ore related stocks performed poorly as the iron ore price fell from $140/T to $100/T. Given the dominance of a few large capitalisation stocks in the ASX200, this can create unnecessary noise in our relative performance over shorter periods of time.

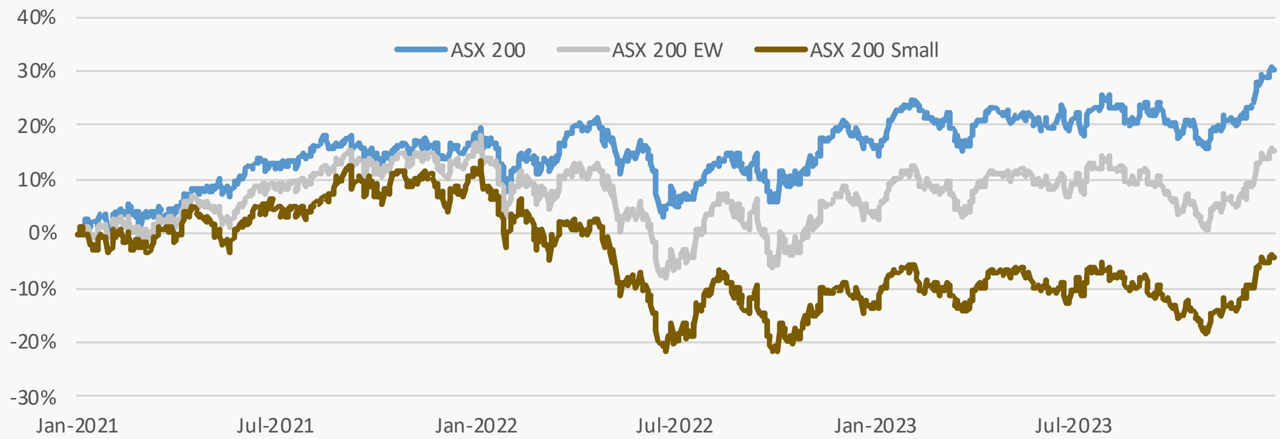
The Fund's strategy is to 1) leverage the firm's VoF stock research, 2) allocate capital to stocks with attractive VoF attributes across three pools: i) compounders, ii) reversionary stocks and iii) real asset and income securities, and 3) back what we call 'proprietorial' management teams i.e. teams with an ownership mindset.

Although the Fund is invested in some of the largest capitalisation companies in the ASX200, the Fund's strategy has tended to take it away from the large banks and resource companies in favour of stocks in the mid-cap and smaller cap parts of the market (noting there is no reason large capitalisation stocks won't be a more meaningful part of the portfolio going forward).

The last three years have favoured the very big end of the ASX200. The chart below shows the ASX200, which is a size-weighted index, compared to an equal weighted index, which reflects the average performance of ASX200 stocks. The chart also shows an index of stocks in the ASX200 that are less than $3bn in market capitalisation (which we have called "ASX smalls"). Note: the chart is for the three calendar years 2021, 2022 and 2023:

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

3 Year Performance of ASX200 (cap weighted), Equal Weighted and ASX200 smalls



Source: CI Internal data as at 31 March 2024

At a stock level, key contributors to Fund performance for the March quarter were Regis Healthcare, Sigma Healthcare and QBE Insurance. Key detractors were Lifestyle Communities (discussed further below), Ryman Healthcare (now sold) and Liberty Financial Group.

Regis Healthcare (REG) was again a strong contributor during the quarter. The company reported a solid operating result with improving occupancy (+250bps), earnings trends and an increasing opportunity set for value accretive M&A.

The Aged Care Taskforce recommendations were also released in March, which in our view demonstrated far greater understanding that industry returns need to improve materially to drive the incremental supply of beds needed to meet expected growth in demand. The taskforce estimated an average of 9,000 new residents per year for the next 20 years versus the current build rate of 1,200 over FY22/23. The Taskforce also advocated for increased user pays and user choice for accommodation services and daily living activities. While there is a higher probability of implementation than prior recommendations given the Taskforce was chaired by the Minister for Aged Care, there is some uncertainty on what the Government will ultimately implement and/or legislate. However, there were two particularly important recommendations in our view which are worth highlighting.

The first was the recommendation that operators retain a portion of Refundable Accommodation Deposits ("RADs") to "make an immediate improvement to sector financial sustainability". Given Regis' significant RAD exposure and the report referencing up to 3% per annum retention, this is a meaningful value latency if enacted in our view of >$1.50 per share (on our initial estimates).

The second was the recommendation that providers should, at a minimum, not be losing money for the provision of daily living services (meals, laundry, cleaning etc) versus the current funding where providers are estimated to lose $4 per resident per day[2] providing these basic services which residents have paid for their entire lives. They also recommended that there should be increased flexibility for residents to pay more to receive higher quality services, in which we would argue Regis should disproportionately benefit by virtue of its scale and more affluent resident base.

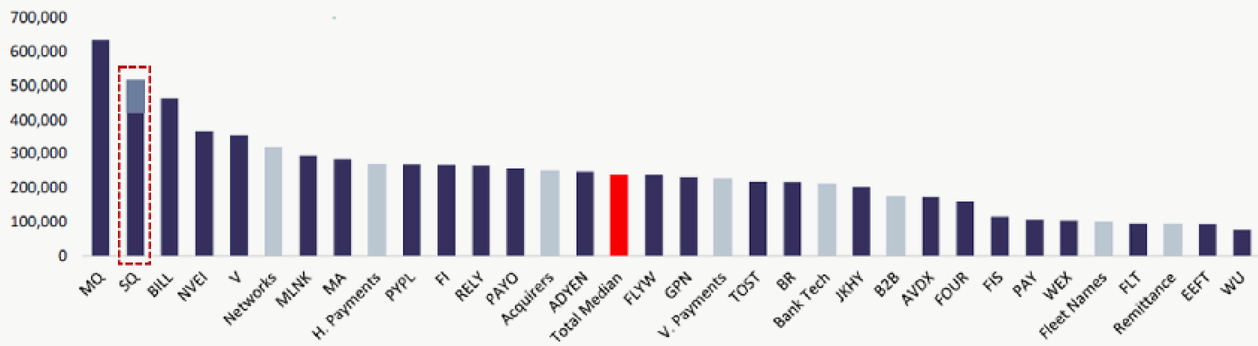
In our September 2023 quarterly, we detailed our investment proposition at length. A key tenet is that there has been a prolonged capital strike in the industry as operator returns are insufficient to drive capital investment. Encouragingly, the Taskforce report acknowledged this numerous times, with different wording of "sustainability" referenced 36 times in the 64 page document.

2 Source: Department of Health and Aged Care, 2023

From an investing stand-point, Regis retains attractive risk-adjusted value latency despite its recent share price outperformance. Some of the reasons we believe we are still early in the up-cycle include:

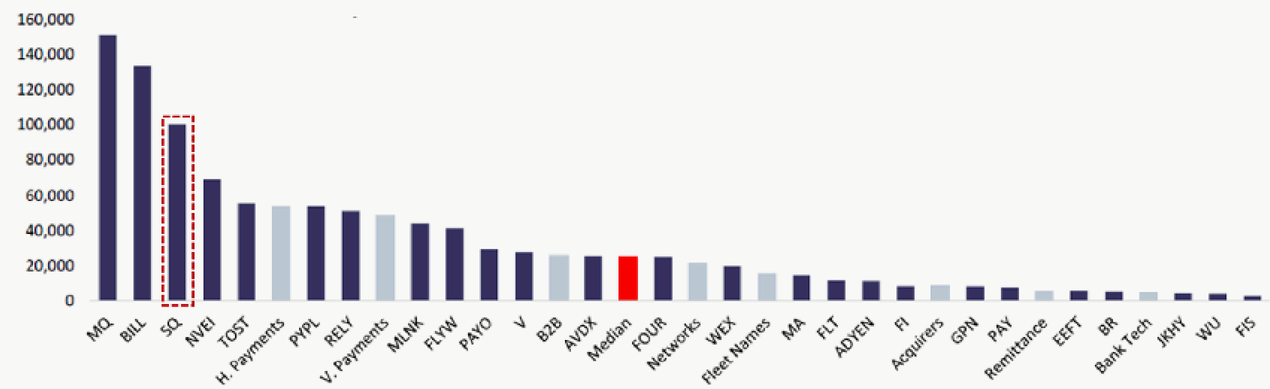
- industry returns still need to improve significantly to see a sustained increase in build rates
- once it gets towards that level of incentive returns, there is then a long time lag between deciding to build a new facility and opening that facility (~3-4 years)
- in the interim, incremental occupancy is likely to drive relatively high incremental margins (despite mandated care minutes), and as facilities approach maximum occupancy there is likely to be upward pressure on room rates (pricing power)
- cash flows are likely to be strong reflecting their working capital position and RAD flows, which provides balance sheet capacity for value accretive bolt-on M&A
- Regis is particularly well placed to benefit from increased user pays given its exposure to more affluent suburbs.

Block (SQ) FY23 Adjusted OPEX per Employee



Source: Company Documents, Wolfe Research

Block (SQ) FY23 SBC per Average Employee



Source: Company Documents, Wolfe Research

During the quarter, we initiated a position in Block (SQ) which we classify as a Compounder (Growth) and sits within the Family and Founder category of management teams. Block is best known to Australians as the acquirer of Afterpay, although we note that Buy Now Pay Later ("BNPL") contributes a small portion of the group's current revenue and earnings. Block's business is characterised by two ecosystems (1) Square, a payments and point-of-sale (POS) service, and (2) Cash App, a peer-to-peer app in the US with over 55 million monthly active users that has now evolved into a neobank.

Jack Dorsey (Block's founder and current CEO) is a tech entrepreneur who previously co-founded Twitter. Consistent with many technology companies, Block's cost base increased significantly over the last four years and became bloated. From 2019-23, Block's employee headcount increased more than three times from 3,800 to 13,000. In addition, industry benchmarking highlights that Block's salary and cost per headcount is one of the highest amongst peers. During this period, Block also became unfocused from a product perspective, with the velocity of product development slowing considerably as management were distracted by low value-adding projects such as cryptocurrency. This ultimately led to Square ceding share to vertically focused competitors and low employee morale.

Dorsey's track record in building businesses at Twitter and Block highlights that when he is focused, he can be as good as the best tech CEOs. In the last six months, Dorsey has taken radical steps in resetting Block's culture and cost base, including:

1) taking back Square's leadership from Alyssa Henry
2) prioritising profitability and cash flow by committing to achieving the "Rule of 40" by 2026 (the rule of 40 states that tech companies should aim to achieve a growth rate plus a profit margin of 40%, eg 20% growth rate + 20% margin, or some other combination)
3) accelerating layoffs of 10% of Block's workforce with a new headcount cap of 12,000 until "the growth of the business has meaningfully outpaced the growth of the company" with the goal of creating lean, agile teams with less bureaucracy.

Our VoF proposition for Block is based on the value latency we see emerging from a long "hubris to humility" cycle we are observing management driving a hard cultural reset and intense refocusing on profitability, productivity, cost discipline and execution. Realisation of these value latencies will effectively come from achieving more with less:

1) continued cost improvement from headcount reduction, centralisation of shared resources and opportunities in procurement
2) a reacceleration in revenue growth in both Square and Cash App, driven by improved product development velocity
3) completing the integration of Cash App and Afterpay, which will accelerate commerce initiatives and assist in "closing the loop" between the Square and Cash App ecosystems
4) customer adoption of Cash App as the primary banking relationship as its functionality, product offerings and relevance continues to evolve
5) optionality from an excellent and continually improving balance sheet.

During the quarter we exited our position in **Boral (BLD)**, having built the position over the prior 12 months. We highly rate Boral's CEO Vik Bansal, following his time at Cleanaway and saw a similar turnaround opportunity at Boral after more than a decade of mismanagement. Our VoF proposition for Boral was based on:

1) a cultural and operating model reset by one of the best industrial CEOs in Australia
2) turnaround execution and cadence being underestimated by the market
3) the quality and earnings power of Boral's quarry assets being underappreciated
4) improving industry dynamics and structure
5) further latency from a strong balance sheet and a transition in the group's approach to monetising its property portfolio.

While our investment in Boral generated an attractive return over a short time period, we were disappointed to sell the stock so soon. We believe Seven Group's $6.25 bid materially undervalued the trajectory and future potential of Boral under Vik. Our decision to divest the position was due to the limited upside in the foreseeable future driven by the complexities of Seven Group's "best and final" offer and stated intention to delist the business if the 90.5% acquisition threshold was not met.

Opportunities such as Boral are a good illustration of the Fund's strategy. Boral is a leader in the building materials space with a mid-sized market capitalisation. However, its more limited free float (due to Seven Group's large holding) meant it was difficult for many funds of size to build a position in the stock. It is an example of why we want to keep the Brunswick Fund capacity constrained.

OBSERVATIONS FROM THE ROAD

Several of CI's global team visited the US during the March quarter, which included meetings related to two of our portfolio holdings – **Louisiana Pacific (LPX)** and **Ferguson (FERG)**.

The team visited one of Ferguson's large warehouse/distribution centres in the Chicago area, illustrating the ongoing investment Ferguson has made in its supply chain. This investment has allowed Ferguson to get more inventory closer to the customer in both the plumbing distribution and HVAC (heating, ventilation, and air-conditioning) markets which should continue to support Ferguson's ongoing market share gains.

The team also met with an installer of LPX product who described why he had shifted to using LPX's engineered siding product SmartsideR from James Hardie's 'HardieR Plank'. There is an opportunity for LPX to grow its share of the siding market via market share gains as engineered wood and fibre cement continue to take share from vinyl. In addition, there is a large opportunity to increase LPX's exposure to the Repair and Remodelling ('R&R') market via improving their distribution capabilities.

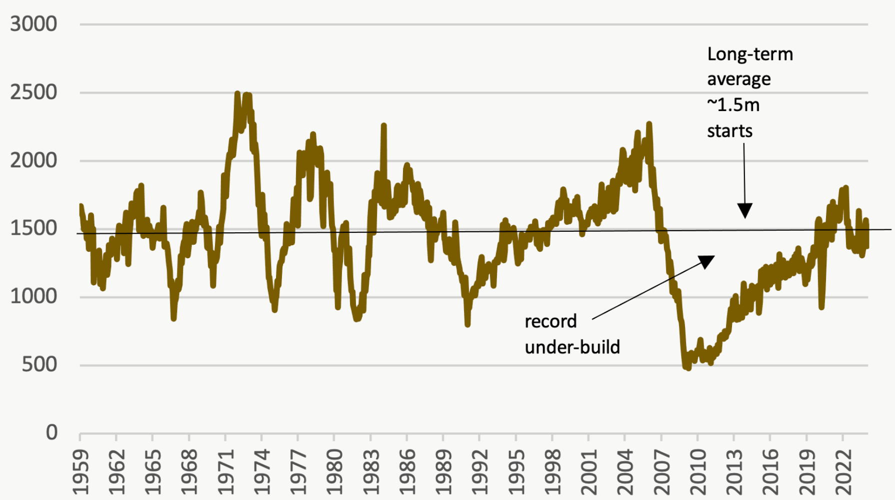
As we outlined in the prior quarterly, our VoF proposition for LPX is underpinned by:

1) the ability to convert more Oriented Strand Board (OSB) mills to siding mills (each dollar invested creates >$1.50 of value on our estimates)
2) an increase the proportion of sidings volumes to "Expert Finish" which generates ~2x the gross margin
3) opportunity to convert a very large OSB mill (Wawa), which they recently purchased out of bankruptcy, into a new siding mill.

Finally, the VoF propositions for both FERG and LPX continue to be underpinned by a supportive 'top-down' setting, namely the historically significant underbuild of housing in the US, which we believe will take many years to recover:

Interestingly, Australia is undergoing its own housing cycle, which has impacted some portfolio companies such as **Lifestyle Communities (LIC)**. LIC raised capital at its 1H24 result following a softer than expected result. In particular LIC has seen a delay to the number of homes settled, despite its sales remaining fairly robust.

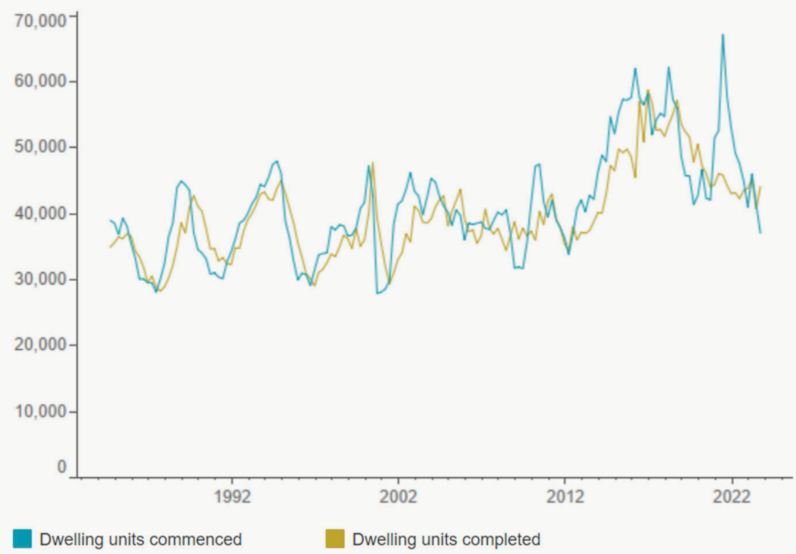
US Housing Starts – 12 month rolling



Source: Federal Reserve Economic Data

This largely reflects market conditions, with the backdrop for housing completions/commencements now at a low point (the chart below includes houses and apartments/other dwellings quarterly data):

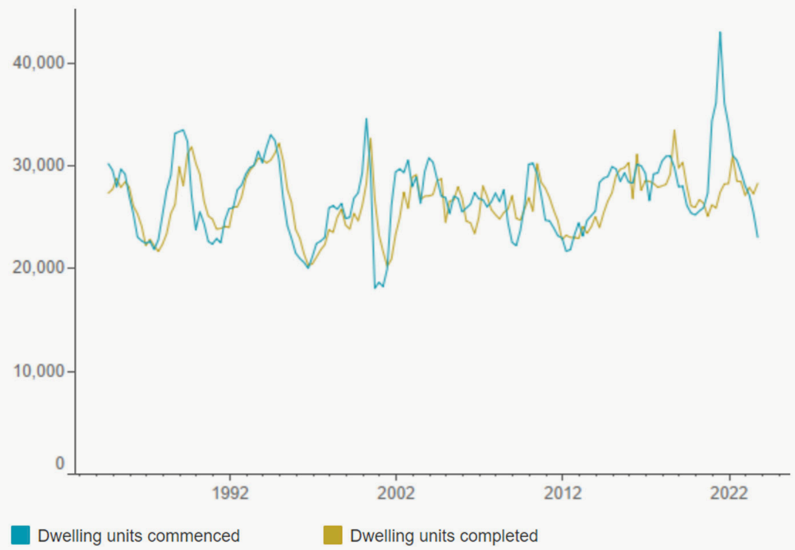
Dwelling units commenced and completed (number), total sectors, total (type of building), 2003 Q3 to 2023 Q3
Australia



Source: Australian Institute of Health and Welfare

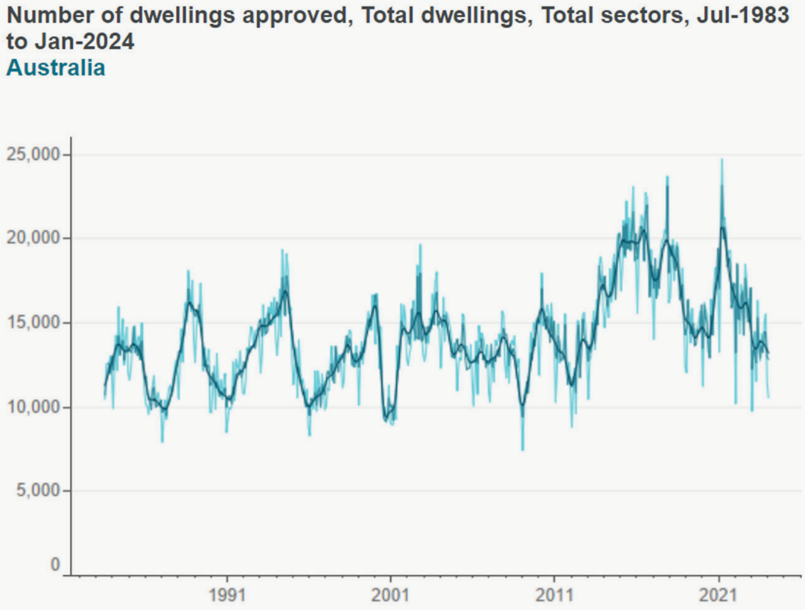
The cyclical low point looks even more extreme if we purely look at houses:

Dwelling units commenced and completed (number), total sectors, houses, 2003 Q3 to 2023 Q3
Australia



Source: Australian Institute of Health and Welfare

However, there is no sign yet, based on approvals (houses plus apartments), that we have reached a trough:



Source: Australian Institute of Health and Welfare

The challenge for Australia is that demand for housing continues to grow strongly. Australia's housing stock is around 10.8m. This needs to grow by around 200k per annum (50k quarterly) just to keep up with population growth, assuming similar levels of housing formation (and also accounting for rebuilds and other replacements).

PORTFOLIO POSITIONING

The most significant changes to the portfolio over the last six months have been in the Compounders pool, where more opportunities have presented of late (to be discussed in further detail in our July annual letter).

In terms of industry, the Fund balances diversity with a focus on clusters like 'aged accommodation', and an overall relatively defensive positioning. The Fund remains very different to the benchmark ASX200.

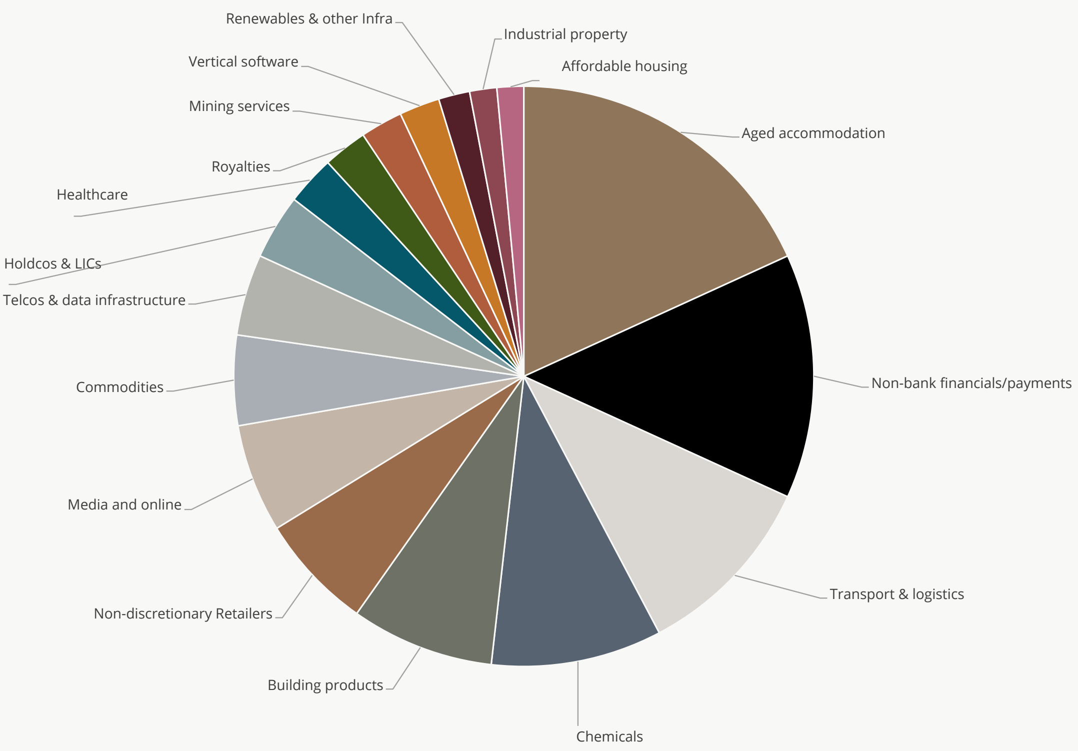
CI Brunswick Fund

COOPER INVESTORS

QUARTERLY COMMENTARY | MARCH 2024

AFS LICENCE NUMBER 221794 ABN 26 100 409 890

Brunswick Fund by Industry



Source: NAB Asset Servicing, CI data

A number of clusters remain of interest in terms of current and future opportunities:

- ageing demographics and community
- affordable housing and other residential exposures where demand and rental growth is strong
- infrastructure and property leveraged to data, renewables and industrial/online
- companies benefiting from the US housing cycle
- attractively valued 'platform' companies that generate high incremental returns on capital as they grow
- companies benefiting from increased spend on domestic infrastructure, for mining, road, rail and other major projects
- 'picks and shovels' companies servicing the mining sector set to benefit from demand for future facing commodities
- assets in the ground that are valued well below replacement cost, earning low to mid-cycle returns on capital at present, that will benefit from an improved supply/demand dynamic
- non-bank financial companies benefiting from a normalisation of interest rates
- small and mid-cap companies more leveraged to the next profit cycle

CI Brunswick Fund

COOPER INVESTORS

QUARTERLY COMMENTARY | MARCH 2024

AFS LICENCE NUMBER 221794 ABN 26 100 409 890

MARKET OBSERVATIONS

Despite a reasonably strong year for equity markets, the ASX200 trades at an average multiple of 16.5x:

PE ratio of ASX200

Source: Factset Data, Cooper Investors analysis

Consensus is expecting a near term recovery in earnings (which is still modest by historical standards at ~3%), which is perhaps the bigger risk to stock markets should the economy falter under current interest rate settings.