30 SEPTEMBER 2023

# GLOBAL SMALL CAP FUND

PARADICE
INVESTMENT MANAGEMENT

| PERFORMANCE NET (%) | 1 MONTH | 3 MONTH | 1 YEAR | 3 YEAR | 5 YEAR | 7 YEAR | 10 YEAR | SI* P.A. |
|---|---|---|---|---|---|---|---|---|
| Global Small Cap Fund | -4.76 | -0.25 | 18.17 | 7.95 | 1.19 | 4.54 | 7.04 | 9.37 |
| Benchmark[1] | -4.01 | 0.13 | 15.51 | 9.82 | 4.88 | 7.67 | 9.18 | 11.11 |
| Excess Return | -0.75 | -0.38 | 2.66 | -1.87 | -3.69 | -3.13 | -2.14 | -1.74 |

*Since Inception date (SI) – 18 January 2013

Past performance of the Fund is not a reliable indicator of future performance. The value of an investment in the Fund may rise or fall. Returns are not guaranteed by any person. Fund returns are calculated before tax, after ongoing management costs and any accrued performance fees, and assumes the reinvestment of distributions. Returns greater than 1 year are annualised.

## INVESTMENT OBJECTIVE

The Fund aims to outperform the S&P Global ex Australia and New Zealand Between USD1 Billion and USD5 Billion Net Total Return Index in AUD over a three to five year period (after management costs and before tax).

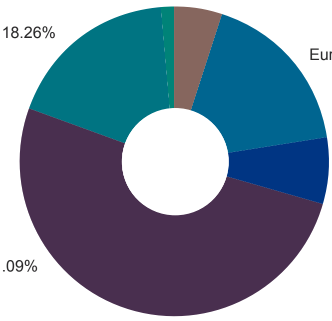
## LEAD PORTFOLIO MANAGER

Kevin Beck & Paul Mason

## KEY DETAILS

| | |
|---|---|
| Number of Holdings | 50 |
| Weighted Avg Mkt Cap (AUD M) | $5,609M |
| Active Share | 98.35% |
| Fund Size (AUD) | $122M |

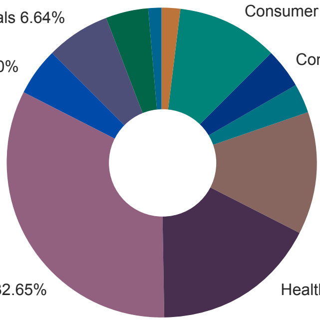
## REGION ALLOCATION




## TOP 10 POSITIONS

| TOP 10 POSITIONS | WEIGHT % |
|---|---|
| ITT, Inc. | 3.66 |
| Renewi Plc | 3.29 |
| Lear Corp. | 3.23 |
| ChampionX Corp. | 3.21 |
| Euronext NV | 3.20 |
| Onex Corp. | 3.03 |
| Globus Medical Inc. Class A | 3.03 |
| OPENLANE, Inc. | 3.02 |
| Acuity Brands, Inc. | 2.99 |
| CNO Financial Group, Inc. | 2.94 |

## SECTOR ALLOCATION




## FUND DETAILS

| | |
|---|---|
| APIR Code | ETL0365AU |
| Fund Currency | AUD |
| Distribution Frequency | Semi-Annually |
| Management Fee[2] | 1.25% p.a. |
| Performance Fee[3] | 15% p.a. |
| Buy Sell Spread | +/- 0.30% |
| Minimum Investment | $20,000 |

 [1] S&P Global ex Australia and New Zealand Between USD1 Billion and USD5 Billion (AUD) NTR Index effective from 5 November 2018. Prior to this date the benchmark was S&P Global Between USD1 Billion and 5 Billion (AUD) NTR Index effective from 1 October 2015 to 4 November 2018 inclusive and S&P Global Between USD1 Billion and 5 Billion (AUD) TR Index prior to 1 October 2015. [2] The management fee is effective 5 November 2018. Prior to this date the management fee was 1.40% p.a. [3] Applies to the investment performance achieved by the Fund (after management fees and costs) in excess of the Benchmark. Refer to PDS for more information.

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*Performance in AUD unless otherwise noted.*

## MARKET REVIEW AND PORTFOLIO PERFORMANCE

The September quarter was volatile as investors grappled with the same ongoing themes that have been lingering for what seems like two years now; stubborn inflation, high interest rates and the perennial question of "when will the economy eventually slow down?".

We find it interesting that the narrative around interest rates has taken a complete 180 degree turn in the past two years. The usual talking heads on various platforms were arguing two years ago that inflation was dead due to demographic declines, technological advancements, workplace efficiency, low-cost energy, and cheap electronic imports from Asia. Those same talking heads have now changed their tone completely saying that high inflation is here to stay due to a skills shortage, deglobalization, geopolitical tensions and expensive energy prices. The pendulum never stops in the middle.

Despite the high interest rates, we are seeing greenshoots in the M&A market globally. So far this year, we have seen two closed mergers in the portfolio and there are currently three other names in the portfolio which have had 'rumors' or have embarked upon a sale process. M&A has been an idiosyncratic driver of returns since the strategy's inception and there are many names in the portfolio which we believe are prime candidates for takeovers.

### Top Performers for the Quarter Included

**Renewi Plc (UK):** Renewi is a waste management business with a strong focus on sustainable waste solutions in the Benelux region. During the period, Renewi received a take private offer from Australian based Macquarie at a 52% premium to previous trading levels. We view Renewi as a scarce asset in the waste management sector and we have observed many take privates at higher valuations than what Macquarie is currently offering. In addition to this, we suspect that there are at least two other strategic buyers of Renewi, which may lead to some bidding tension in the coming months. We remain holders of the name.

**ChampionX Corporation (US):** ChampionX is a global energy services provider specializing in production chemicals, artificial lift technologies, and diamond cutters/bearings. The company was formed in 2020 following the merger of Apergy and Ecolab's upstream chemicals business. The upstream chemicals acquisition from Ecolab gave ChampionX a new, consumable product suite that reduced cyclicality. We have owned ChampionX since 2020 when the price of oil turned negative for the first time in history and global panic around energy demand ensued. At that time, ChampionX was trading at a discount to its legacy Apergy valuation despite the business diversification. ChampionX has been a standout performer for the Fund over our holding period. This quarter ChampionX continued this trajectory, rallying 15% due to rising oil prices, which investors anticipate will increase drilling activity globally. Despite its recent performance, ChampionX still trades at a discount to oil services peers while having a higher quality portfolio of leading market share products.

**Onex Corporation (Canada):** Onex Corp is an alternative asset manager with over US$51 billion invested across its Private Equity (PE) and Credit investment platforms. The firm manages both its own capital (US$7.8B) and fee-bearing third party capital, with zero debt on its balance sheet. During Q2, ONEX management addressed the gap between book value versus the share price and communicated their intentions to narrow the gap by selling some investments and repurchasing ONEX shares. This was taken positively by the market during Q2 and continued to see the shares re-rate during Q3. The remaining gap between the share price and book value we believe still represents strong upside in the name.

### Bottom Performers for the Quarter Included

**AMS Osram (Switzerland):** AMS Osram is a manufacturer of LEDs and sensors that feed into autos, consumer electronic devices, and other industrial/medical applications. AMS Osram was formed in 2019 via the merger of AMS and Osram. The merger diversified the business away from volatile consumer electronics, which previously represented 75% of AMS' standalone sales. We invested in AMS Osram in 2022 when the shares traded at a discount to the historical AMS valuation despite the fact that the business had diversified. This year, AMS Osram is completing a multi-year construction project for a state-of-the-art micro-LED fabrication facility, underpinned by long-term commitments from a large customer. At the same time, AMS Osram has faced a glut of its inventory in the market as customers double ordered during the supply chain crisis in '21-'22, leading to decreased customer demand this year. The lower earnings power coupled with higher capex led to a higher leverage ratio that risked breaching bank covenants. As a result, management announced a debt restructuring plan at the end of September. Part of the plan included raising equity to repay debt, sending AMS Osram shares down 35% for the quarter. We support AMS Osram's decision to raise equity as it will bolster the balance sheet and allow the company to complete the micro-LED facility, which will be a future growth driver for the company. Additionally, AMS Osram reviewed its portfolio and will be selling underperforming assets, which we believe will substantially improve future earnings power.

**Avanos Medical (US):** Avanos Medical was a bottom contributor during the quarter. Earlier this year, management unveiled a new transformation plan to improve the overall quality of the business, specifically in the Pain Management portfolio, through a series of disposals and acquisitions. This asset reshuffling has created some noise around operating performance throughout the year, including a poor earnings report for the second quarter. After the earnings release, we held a call with management to better understand the current dynamics of the business and the plan for moving forward. We came away from the meeting with higher conviction in their business optimization strategy and their ability to achieve their target earnings per share (EPS) in 2025. As 4 October 2023, the stock trades at just 10x the company's 2025 EPS target.

**Gates Industrial (US):** Gates manufactures a range of rubber and polyurethane hoses, belts and other fluid handling equipment. The shares sold off during the period on concerns surrounding the strength in automotive and general industrial end markets. Gates tends to run balance sheet leverage at roughly 3x net debt to EBITDA, which is slightly higher than most industrials which may have also been a cause of weakness as interest rates continue to rise.

## PORTFOLIO PERFORMANCE

The Fund was essentially flat for the quarter posting returns of -0.25% (net). Areas of weakness for the Fund were primarily stock selection in Europe and an underweight to Emerging Markets, which outperformed during the period. Areas of strength for the Fund were North America and the UK on the back of strong performance in Industrials.

### Portfolio Changes

During the quarter the Fund initiated two new positions and exited five. There was also one merger.

The Fund initiated a new position in a company that operates the leading investment platform in Europe, which connects financial institutions and investors. Whilst the business does not technically have a recurring subscription revenue, the revenue streams are very predictable and sticky by nature, leading to strong predictability of earnings. The company appears undervalued relative to a broad range of comparable businesses.

An additional new position for the Fund was a Japanese listed company that provides online recruitment solutions to Japanese companies seeking to recruit staff across many industries. The company's flagship website is consistently ranked #1 in satisfaction surveys. This business plays nicely into Japan's structurally tight labor market (due to demographics) as well as the constant war for talent amongst major employers.

A US retail clothing store was exited during the quarter. We commend the management team at the company on the successful turnaround of the flagship brand. Brand turnarounds are extremely challenging to execute on. We exited our position based on valuation combined with an increasingly challenging economic environment for the consumer.

A German listed trucking components business was also exited. The company is a well run business, however, recent earnings have been bolstered by supply constrained market for trucking components and high pricing for new trucks. We sold the position to zero on concerns around future earnings growth potential.

Three additional positions were exited during the period on valuation grounds to make way for new investments and manage the Fund cash position.

In addition, the merger of the Fund position in a leading player in spinal surgery, and a US medical device business closed during the quarter. As a result, our shares in the former were effectively swapped for shares in the latter. The board of US medical device business has subsequently announced an increase of their ongoing share buyback program.
We believe the combination of these two businesses, led by a well established and proven management team is a compelling investment.

## OUTLOOK

The Fund does not pretend to have a macroeconomic crystal ball; however, it must be said that this highly uncertain economic backdrop is not an ideal market for a fundamental, long-term oriented buy and hold strategy. A much more stable economic environment is ideal for our highly cash generative business to redeploy capital into growth initiatives and tuck in M&A to bolster growth. Despite the underlying strength of the economy, it seems many companies and investors are waiting for the elusive recession before making any major decisions, putting markets into a holding pattern of sorts. Our philosophy and process drives us to areas of dislocation and business that we believe are 'underearning' relative to their potential. At the moment, that is driving us towards rate sensitive sectors such as Industrials and building products, which we expect to be key drivers of return in the future.