HMC Capital

HMC Capital Partners Fund 1

QUARTERLY INVESTOR UPDATE– MARCH 2024

SUMMARY

- HMC Capital Partners Fund 1 (the "Fund") returned 21.9%[1] during the March quarter and 32.0% (annualised) since inception, closing at a NAV of $1. 5522/ unit
- Sigma Healthcare and Ingenia Communities both contributed positively to the Fund's performance, with Lendlease weighing on returns following a disappointing half year result
- The Fund has elected to undertake a small selldown of its Sigma stake to realise profits, partially rebalance the portfolio and release capital to invest in new opportunities. We retain a significant 15% stake in Sigma and have high conviction in our ongoing investment as the company progresses its proposed merger with Chemist Warehouse Group
- The Fund continues to deploy into two undisclosed investments and is actively assessing further investment opportunities in line with the Fund's strategy

Key Fund Statistics[2]

NAV	$1.5522 / unit
Entry price	$1.5569 / unit
Exit price	$1.5476 / unit
Inception Date	31 August 2022
Status	Open for investment
Management Fee	1.00% of NAV
Performance Fee	20% of returns in excess of a hurdle return of 7% per annum of NAV, subject to a high-water mark paid annually

Fund Performance – 31 March 2024[1]

Returns (Net) (%)	Fund
1 month	**9.5%**
3 months	**21.9%**
6 months	**44.8%**
12 months	**46.5%**
Since inception (annualised)	**32.0%**
Since inception (aggregate)	**55.2%**

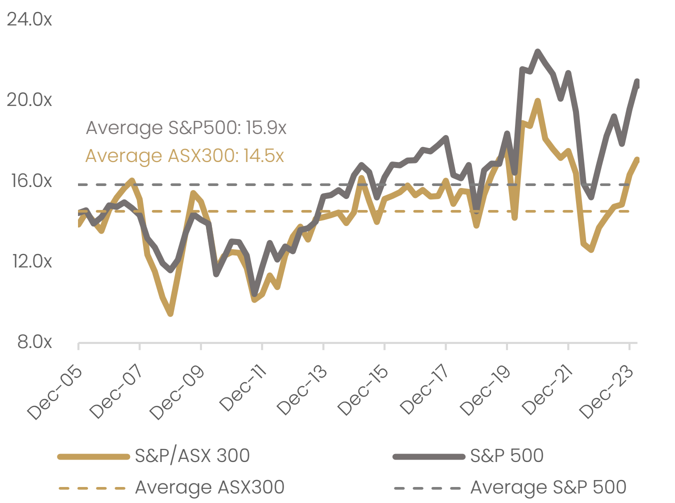
Market Commentary

Strong start to 2024 for equity markets

Global equity markets were surprisingly stronger than expected in the first quarter of 2024, building on the momentum of Q4 2023. Bullish sentiment prevailed as investors remain optimistic of rate cuts later in the year, with economic and inflation data released during the quarter continuing to support this narrative. In the US, positive earnings reports, particularly from the tech sector, drove the index higher, with the S&P 500 setting new records and closing up 10.2%, its best start to the year since 2019.

In Australia, the S&P/ASX300 Accumulation index traded up 5.4% during the quarter, with falls in materials partially offsetting strong gains in technology, real estate and consumer discretionary stocks. The strong rally has resulted in market forward multiples moving above their short- and long-term averages, with limited upgrades to market consensus earnings.

Forward P/E – S&P/ ASX 300 vs S&P 500



Source: Bloomberg (as at April 2024)

[1] All performance figures are quoted net of fees. Figures may not sum exactly due to rounding. Inception date 31 August 2022. Past performance should not be relied upon and should not be taken as an indicator of future performance.

[2] Entry and Exit prices reflect the Net Unit Value as at 31 March 2024, adjusted by the buy-sell spread (currently 0.30%).

Our view on the outlook

Interest rate cuts – a question of when not if

The RBA held interest rates steady for its third straight meeting in March, with inflation continuing to moderate but remaining above target. February CPI data released in late March showed flat headline inflation, with the trimmed mean coming in slightly under expectations.

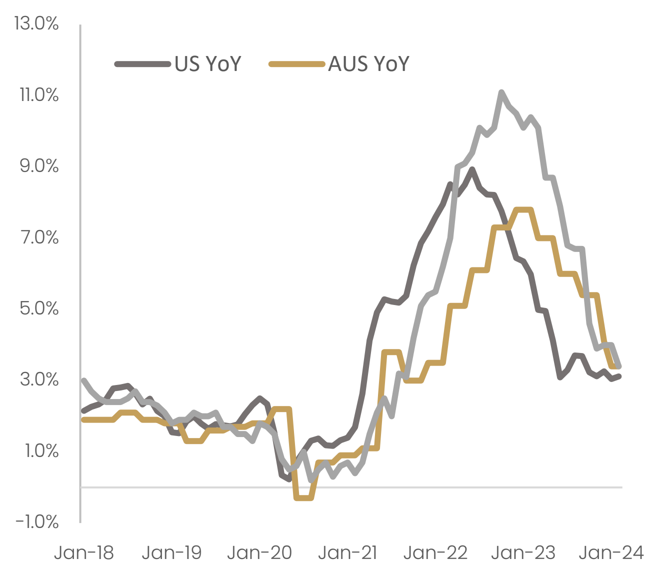
Markets have pushed out anticipated timing of a pivot to Australian interest rate cuts towards the back end of 2024, with central banks decision making remaining data dependent. While underlying GDP growth remains positive, the Reserve Bank may hold for longer, however we believe rate cuts will be moved forward if there is a sharp deterioration in economic conditions.

Investors have thus far largely shrugged off the delay to expected rate cut timing, seemingly accepting that 'higher for longer' interest rates reflect a resilient, albeit slowing economy.

Rational or irrational exuberance?

With global equity indices reaching new highs during the first quarter, valuations are looking stretched across the broader market. A lot of good news has already been priced in by investors during the past few months, and a number of technical indicators suggest the US stock market is becoming overbought. We remain alert to the risk that negative news flow regarding an economic downturn or tighter than expected monetary policy could see an end to the rally or even a market correction.

Headline inflation YoY (%)



Source: RBA, BoE, Federal Reserve

What does this mean for the Fund?

The Fund is well positioned to take advantage of pockets of volatility in equity markets or stock specific situations, with significant dry powder available to move swiftly. As we have previously stated, we view uncertainty and volatility as a significant opportunity and the current investing environment as highly conducive to the Fund's strategy.

The Fund is focused on adding value to our existing portfolio companies, tactically building our new positions in a disciplined manner, and identifying further investment opportunities to build out the portfolio.

Fund Open For Investment

The Fund remains open for investment on a monthly basis. Existing investors can top-up their investment by logging on to their Automic investor portal at www.investor.automic.com.au

Eligible investors can also opt-in to the Fund's Dividend Reinvestment Plan (DRP) via the Automic investor portal. Participation in the DRP will mean that any dividends paid by the Fund will be applied to subscribe for additional units in the Fund rather than paid in cash.

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Key investments update

Sigma Healthcare

Sigma announced full year results for the year ending 31 January 2024 during the quarter, posting a strong improvement in underlying EBIT. The company demonstrated strong operating performance and significant cost efficiencies, and we are confident the operational turnaround of the core wholesale and distribution business has been successful.

Sigma stated they remain on track and operationally prepared for commencement of delivery of the new Chemist Warehouse supply contract from 1 July 2024. Sigma also re-iterated their target of achieving a 1.5 – 2.0% EBIT margin over time.

In compliance with Sigma's continuous disclosure obligations, the full year results also included summary information regarding Chemist Warehouse Group (CWG) first half FY24 performance for the six months to 31 December 2023. CWG posted strong performance, with Profit Before Tax up 28.6% on the back of 13.5% growth in Total Network Sales.

In relation to the proposed merger between Sigma and CWG announced in December 2023, the transaction remains subject to a number of conditions including ACCC approval, and Sigma and CWG shareholder approvals. The ACCC commenced a public consultation process in early March 2024 and has set 13 June 2024 as the provisional date for announcement of its findings.

The Sigma share price continued to perform strongly through the quarter, up 28.9% to $1.295. Given the exceptional performance of the Fund's investment in Sigma, the portfolio's allocation to Sigma has grown to represent a significant proportion of the Fund's Net Asset Value. In order to partially rebalance the portfolio and recycle capital into other compelling opportunities, the Fund elected to sell down a small portion of its Sigma stake (selldown represented only ~20% of the Fund's stake) during March and early April.

The Fund continues to have very high conviction in Sigma and the proposed combination with CWG, and currently retains a significant 15% stake in Sigma.

Sigma full year results highlights

- 4.3% increase in like-for-like sales revenue
- 62.7% increase in underlying EBIT[1]
- 10.7% reduction in operating costs[2]
- On track to execute new Chemist Warehouse supply contract from 1 July 2024

Source: Sigma Healthcare ASX announcement

Notes:

1. Excluding initial merger transaction costs of $8.2m incurred to 31 January 2024
2. Reduction after absorbing $8.2m merger transaction costs

CWG half year results highlights

- Total Network Sales $4.56bn, up 13.5% vs pcp
- 9.0% LFL sales growth in Australia
- 18 stores added to global network
- $321m Statutory Profit Before Tax, up 28.6% vs pcp

Source: CWG disclosure in Sigma ASX announcement

Lendlease Group

Lendlease closed the quarter down 13.9%, underperforming the broader A-REIT index by 30%. Lendlease's first half 2024 result (released in February) was disappointing with the company downgrading FY24 earnings guidance. This was primarily driven by the continued underperformance of its operations offshore, particularly in Europe and the Americas. Importantly, the disposal of the Residential Communities business at a ~20% premium to book value has taken a highly dilutive equity raising off the table. We were pleased that the company listened to our advice (outlined in our August 2023 white paper) and pivoted from its strategy to sell a partial interest in this business to a passive capital partner.

The current share price demonstrates that the market has lost confidence in the current strategy - we estimate the share price is imputing a ~$3bn discount to account for future write-downs and losses, which we believe is far too punitive. The upcoming strategy briefing in May 2024 is a critical opportunity for Lendlease to reset and give the broader investment community a reason to own the stock.

As a proactive investor, we have had engagement with both management and the board on this front, which we believe has been constructive and positively received by the company. With the challenging macro backdrop and slowdown in transaction activity, it is evident that more decisive strategic action needs to be taken by the company, and we re-iterate our recommended strategy for Lendlease, namely:

- repatriation of capital back to Australia (and parts of Asia) where it has genuine competitive advantage and scale;
- scaling back offshore construction;
- reducing exposure to low ROE assets and long-dated projects; and
- ongoing progress on business simplification and cost efficiencies.

The status quo is clearly unacceptable, and we believe the company understands the need for more decisive action.

Ingenia Communities Group

Ingenia traded up 17.5% during the quarter after releasing half year results in line with market expectations and maintaining guidance for FY24. The business remains well positioned to benefit from powerful demographic megatrends via its land lease communities segment, with a significant captive development pipeline of communities.

New CEO John Carfi commenced on 1 April 2024, bringing significant real estate development expertise and a fresh perspective to the role. We look forward to building a constructive relationship with Mr Carfi and sharing our views on value maximising strategies for the benefit of all shareholders.

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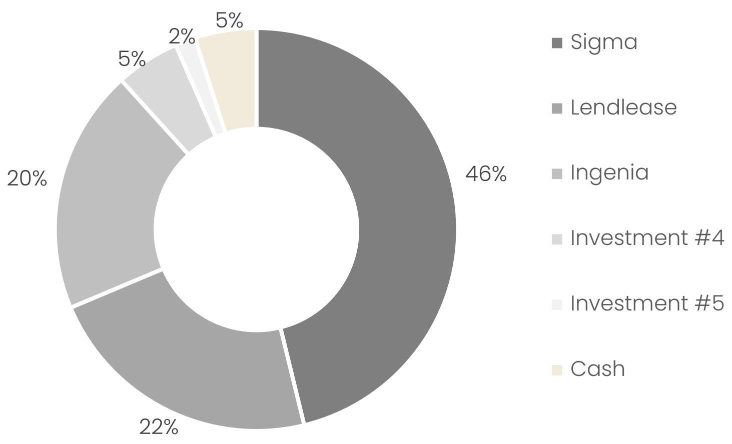
Fund Performance and Portfolio

The Fund returned 21.9% (net of fees[3]) during the quarter to 31 March 2024.

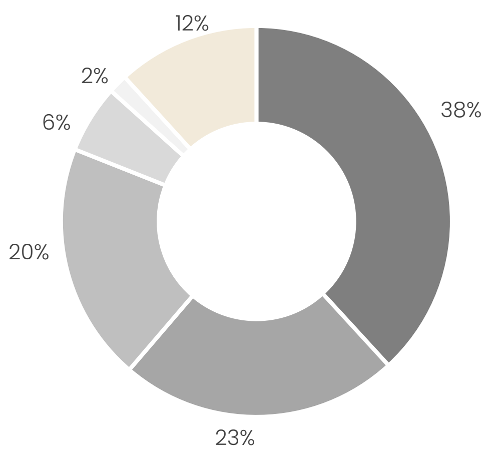
Since inception, the Fund has outperformed the S&P / ASX300 Accumulation Index by 34.3%.

We continue to see further upside in each of our investments and are deploying into two high conviction positions that are yet to be publicly disclosed. We have also identified a number of potential additional investments that are being actively reviewed by the investment team. These investments display similar characteristics to those companies we have already invested in – namely mispriced opportunities where there is value protection on the downside and the opportunity to add value through our highly engaged investment approach. We will provide further detail in due course.

Portfolio Composition as at 31 March 2024

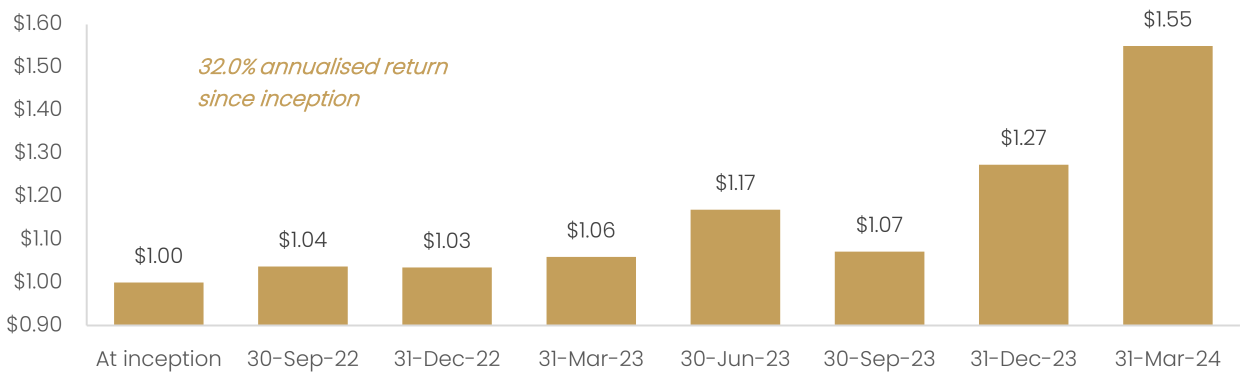


Portfolio Composition as at 4 April 2024[1]



1. Post selldown of Sigma stake to 15%

Fund Net Asset Value per unit since inception[3]



3. All performance figures are quoted net of fees, including performance fees which are accrued but unpaid as at 31 March 2024. Inception date 31 August 2022. Past performance should not be taken as an indicator of future performance.

I look forward to providing further updates on the Fund's performance and our investments as we continue to assess the evolving investment landscape, work proactively with our investee companies and selectively deploy the Fund's capital.

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