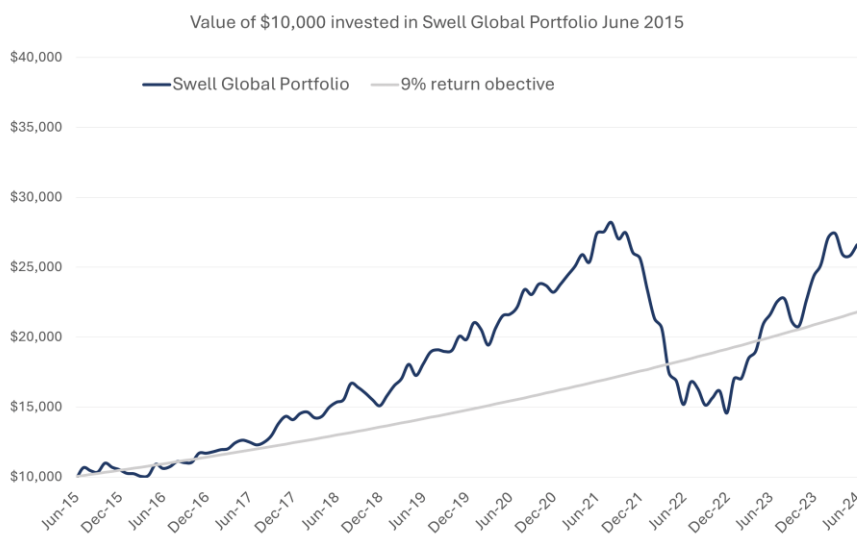


## Portfolio performance

Period	Return
6 months	9.29%
1 year	22.96%
2 years (p.a.)	32.34%
3 years (p.a.)	-0.98%
4 years (p.a.)	5.29%
5 years (p.a.)	8.03%
6 years (p.a.)	9.60%
7 years (p.a.)	11.39%
8 years (p.a.)	12.16%
9 years (p.a.)	11.68%
Inception	170.20%
Inception (p.a.)	11.68%



The Swell Global Portfolio has shown strong performance, increasing 22.96% in the twelve months to June 30 2024. This achievement aligns with the portfolio's ninth anniversary, during which it has delivered an annualised return of 11.68% after all fees, exceeding its return objective of 9%. Despite market volatility, the first half of 2024 yielded a return of 9.29%. It is noteworthy that these returns have been achieved while maintaining a significant cash reserve, positioning the portfolio to take advantage of favourable market opportunities as they arise.

## Market conditions

If you had known with certainty the Federal Reserve would raise the target federal funds rate from near zero during the Covid-19 pandemic to the 5.25% - 5.50% range it is today, you might have expected severe consequences for the economy. Instead, the economic landscape in the US presents a more nuanced picture.

While still above the Fed's 2% target, inflation is showing signs of moderation. Consumer prices fell unexpectedly in June, marking the first month to month drop in four years. This suggests the Fed's aggressive monetary tightening is having its intended effect on price stability.

The labour market, once extremely tight, is exhibiting signs of easing and the US unemployment rate has moved from a low of 3.4% to 4.1%, indicating increased slack in the job market. While the increase might seem concerning, it actually represents a more balanced labour market that could further reduce inflationary pressures.

Globally, the economic outlook remains unclear, with regions following different trajectories. The Euro zone and the UK experienced a rebound in Q2 after a softer 2023, while Australia's economy remains sluggish. This uneven recovery reflects the complex interplay of factors affecting the world economy.

But economic developments are occurring against a backdrop of major geopolitical challenges. The conflicts in Eastern Europe and the Middle East continue to impact global energy markets and supply chains. Additionally, we have seen political shifts between right- and left- leaning governments, national elections resulting in less stable governments and a rise in protectionist policies worldwide.

Despite these headwinds the US economy has exhibited remarkable resilience. Consumer spending, although cooling, remains positive and overall economic growth has not collapsed as some predicted in response to sustained interest rate increases.

### US housing market

The US housing market appears to be showing early signs of recovery, with mortgage rates beginning to ease. This is crucial for the real estate sector, which has struggled under the weight of high interest rates.

The sharp increase in borrowing costs dampened the property market, causing many potential new home buyers to delay their purchase, but recent data suggests a shift in this trend. Mortgage rates fell for three consecutive weeks in July, with the 30-year fixed rate at 6.78%, down from a peak of 7.79%, creating a more

favourable environment for home buyers which could potentially stimulate increased activity.

Despite the challenges there is growing optimism for the future of the real estate sector. Industry experts generally agree a major wave of distress is unlikely, and there is underlying strength in most asset classes, particularly the multifamily segment. This resilience, coupled with the recent easing of mortgage rates, suggests a market recovery may be on the horizon.

For investors positioned to benefit, the outlook is promising. Companies like Intercontinental Exchange (ICE) and Zillow, both closely tied to the real estate market, stand to gain from the improving property landscape. Zillow, as a leading online real estate market place, will see increased user engagement and revenue as new buyers and sellers enter the market. ICE revenue growth will come from increased mortgage origination and refinancing activity on its mortgage technology platforms.

The recovery may not be immediate, but the signs suggest it is a matter of when not if the US housing market will rebound. For investors, strategic positioning and patience could yield significant benefits as the market improves.

## AI and cloud platforms

The top three portfolio performers in the half were our cloud-focused investments which showed robust growth as businesses rush to leverage generative AI to enhance product and service offerings and improve operational efficiency. Microsoft Azure, Google Cloud and Amazon Web Services provide the infrastructure and platforms to enable businesses to develop, deploy and scale AI.

They are at the forefront of the AI revolution, offering specialised services and tools that make it easier for companies to integrate generative AI into their products and workflows. They are seeing increased usage as businesses seek to harness the power of large language models, image generation and other AI capabilities to create more intelligent, responsive and personalised user experiences.

The scalability and flexibility of cloud platforms are crucial for companies experimenting with generative AI. It allows them to access powerful computing resources on-demand without the need for significant upfront investment in hardware.

Moreover the surge in AI-driven cloud adoption is not limited to tech giants and large enterprises. We have witnessed a democratisation of AI technologies, with

small and medium-sized businesses embracing these tools to level the playing field and compete more effectively in their respective markets.

As generative AI continues to evolve and find new applications across all sectors of the economy we anticipate sustained growth in demand for cloud services. This trend reinforces confidence in our cloud investments, positioning our portfolio to capitalise on the long-term potential of the AI-cloud synergy.

## Portfolio Investments

During the half we added Kenvue Inc and Berkshire Hathaway Inc Class B stock to the Portfolio.

Kenvue was spun out of Johnson & Johnson in 2023 with leading brands including Band-Aid, Listerine, Aveeno, Tylenol and Neutrogena and is the world's largest consumer health company by sales. The name draws inspiration from two ideas, "ken" meaning knowledge and "vue" referencing insight. We acquired it at a significant discount to our calculation of its intrinsic value as it is facing a temporary slump in the health and beauty segment in North America.

Good companies will experience problems from time to time and our opportunity as long term investors is to take advantage of such dislocations. This business is not going to turn around in the next couple of quarters, but we expect its strategy to bear fruit in the coming years. In the meantime, it returns a 4.1% dividend yield, so we are being paid to wait. We are impressed by the rigour with which it develops and assesses products to ensure safety and efficacy, which is a major differentiator separating it from traditional consumer product companies.

Our analysis revealed Berkshire Hathaway was trading at a substantial discount to its intrinsic value, presenting an attractive opportunity for us as value-oriented investors. We consider the trading slump is due to short term investors fretting over life without Mr Buffett at the helm, heightened since the death of Mr Munger late last year.

However, we have great confidence in Warren Buffett's strategic positioning of the company for long term success beyond his tenure. We believe his long standing leadership succession plan will maintain his legacy of management excellence. Ajit Jain oversees insurance operations, leveraging an exceptional track record and deep industry expertise while Greg Abel brings a wealth of operational acumen to lead the service, retail and infrastructure companies and drive growth across Berkshire's diverse business portfolio.

We divested our holdings in Salesforce, Shopify and Booking Holdings as the appreciation of their share prices meant they were no longer trading at a discount to our estimate of their value. This is one of only three reasons we have to sell a stock. We will continue to monitor them and would consider buying them back at the right price. By the end of the half our cash weighting was 16.92%, giving us the opportunity to invest in quality stocks at the right price as we identify them.

Our top three investments in the half were Amazon, Alphabet and Microsoft which all benefitted from the growth of cloud computing platforms discussed earlier. Our portfolio construction strategy prioritises businesses we believe possess the capacity to thrive independently of broader macroeconomic conditions, drawing us particularly to companies positioned to capitalise on secular growth trends we anticipate will demonstrate resilience even in the face of economic headwinds.

We discuss each company below.

## Amazon

March quarter revenue reached \$143.3 billion, 13% higher than the same quarter last year, made up of \$25.0 billion from AWS, up 17%, \$86.3 billion from North America, up 12%, and \$31.9 billion from international sales, up 10%. Net income increased to \$10.4 billion, 229% higher than 1Q23, and diluted EPS reached \$0.98. AWS achieved a \$100 billion annual revenue run rate, which CEO Andy Jassy attributed to a “combination of companies renewing their infrastructure modernisation efforts and the appeal of AWS’s AI capabilities”.

The artificial general intelligence team was boosted with the appointment of David Luan and two thirds of his co-founders and colleagues from Adept, a startup working on agent based general intelligence models. Mr Luan, who will report to Rohit Prasad, SVP and Head Scientist AGI, will lead Amazon’s AGI autonomy and automations teams. He was CEO at Adept, VP Engineering at OpenAI and also worked with Google’s Brain group.

The rationalisation of Amazon’s fulfilment capacity in the US was largely completed by June 2024 with the creation of eight regional distribution centres. The regional networks have resulted in less handling, shorter delivery times and more cost effective delivery systems which in turn have driven improved retail sales and margins.

Amazon launched an AI powered shopping assistant named Rufus for US mobile customers. It is trained on the company’s product catalogue and information from

across the web including customer reviews and recommendations.

Amazon MGM Studios is partnering with YouTube sensation Jimmy Donaldson, known as MrBeast, to produce "Beast Games" featuring 1,000 contestants competing for a \$5 million prize. More than 245 million people subscribe to his YouTube channel, and applications for the games closed ahead of schedule due to overwhelming demand. The series is exclusive to Prime Video and is reported to have started filming in July with a short production season and release date before the end of the year.

Amazon's Project Kuiper low earth orbit satellite constellation global broadband network tested two prototype satellites to validate its technology and mission procedures. They recorded 100% success for all systems including custom thrusters designed to enable controlled manoeuvring. A policy of space safety and sustainability means Kuiper satellites will deorbit within a year of their mission ending. During the deorbit the thrusters execute a series of manoeuvres which gradually lower the satellite to an altitude of around 350 kms where it burns up in the earth’s atmosphere.

## Alphabet

First quarter revenue was \$80.5 billion, 15% above last year, and net income was \$23.7 billion, an increase of 57% on the same quarter last year. CEO Sundar Pichai told investors the growth validated the success of its plan to durably re-engineer its cost base. Advertising revenue rose 13% and Google Cloud revenue rose 29%. Diluted EPS was 62% higher at \$1.89. As the company continues to invest in its cloud and AI infrastructure capital expenditure will remain high. Alphabet paid its first quarterly dividend in June and the company is repurchasing \$70 billion Class A and Class C shares.

At the Google Cloud Next 2024 Google Cloud CEO Thomas Kurian demonstrated how Google's Vertex AI creates conversational agents. Its managed tools connect an AI model to enterprise applications and databases, allowing it to generate personalised answers and recommendations. By grounding the AI model with actual company data Vertex AI reduces the likelihood of hallucinations and greatly improves the reliability and effectiveness of the agent.

A month later at Google I/O 2024 CEO Sundar Pichai told developers the Gemini multimodal AI model had been integrated into all its 2 billion user products as well as being available to mobile users on Android and iOS.

Google's Deep Mind team released examples of short videos created with its Veo generative video model

using V2A, an AI model which generates audio. The videos show a synchronised soundtrack to AI generated video. V2A encodes the video with any audio prompt input provided, runs it through the model then generates audio. Deep Mind engineers believe the model is superior to existing solutions as it understands raw pixels, making text prompts optional rather than essential.

From June 2024 Waymo's rider only service in San Francisco is available to all riders in the city. It also operates over nearly 900 square km in the Phoenix-Scottsdale metropolis in Arizona, and began trials in Los Angeles last year. Waymo cars have driven more than 20 million fully autonomous miles on public roads and are delivering over 50,000 weekly paid rides. The entire Waymo fleet is the all-electric Jaguar I-PACE SUV.

## Microsoft

Third quarter revenue was \$61.9 billion, 17% higher than last year, and net income rose 20% to \$21.9 billion. Cloud revenue reached \$35.1 billion offset by \$14 billion in capital expenditure to scale AI infrastructure and meet cloud demand. CFO Amy Hood said capital expenditure would increase in the near term as AI demand continues to exceed available capacity. Nearly 60% of Fortune 500 companies are now using Copilot, and Office commercial products and cloud services revenue rose 13% from 3Q23. Diluted EPS rose 20% to \$2.94. During the quarter the company repurchased \$2.8 billion in shares and paid \$5.6 billion in dividends.

In April Microsoft and Quantinuum reported reaching a crucial milestone on the path to building a hybrid supercomputing system, achieving Level 2 resilient quantum computing with the most reliable logical qubits on record. Jason Zander, Microsoft Executive Vice President posted in a blog: "With the promise of a hybrid supercomputing system powered by these reliable logical qubits, we're paving the way for scientific and commercial breakthroughs that were once deemed impossible."

Microsoft will invest \$1.5 billion in UAE based G42 which manages subsidiary companies developing AI related technologies in diverse fields including biology,

healthcare, resources and exploration. G42 will run its AI services on Microsoft Azure and the partnership will deliver advanced AI solutions using Microsoft's infrastructure and G42's applications to global clients. They will establish data centres in Africa, the Middle East and Central Asia, providing a secure platform and services for governments and organisations in those regions. Microsoft President Brad Smith will join the G42 board. The chair of G42 is Sheikh Tahnoon bin Zayed, brother of the UAE president, and its largest investor is the country's sovereign wealth fund.

The first Copilot+ PCs in Microsoft's Surface range and from Acer, ASUS, Dell, HP, Lenovo and Samsung were released in June. The PCs run AI applications in the Windows 11 operating system and small language models including Phi Silica, custom built for the System on Chip NPUs specific to the range.

VP of Windows + Devices Pavan Davuluri revealed Microsoft will extend Windows experiences to form factors beyond the PC, and through its partnership with Meta create 3D versions of Windows and Microsoft Office. Windows and Office Volumetric apps will run on Meta's Quest devices in full 3D rather than the flat experience currently available.

## Outlook

We are witnessing a paradigm shift from an era of unprecedented low interest rates and abundant liquidity to a more constrained financial landscape which is likely to precipitate a significant recalibration of asset valuations across the board. In light of this evolving economic backdrop, our investment strategy has become even more focused on identifying companies with robust fundamentals and sustainable growth prospects.

As valuations adjust to the new interest rate regime, we believe our emphasis on fundamental strength and secular growth trends will position our portfolio to weather market volatility and potentially outperform over the long term. Although uncertainty will remain over the short-term, we encourage our investors to look through it and instead focus on the long-term opportunity.

This document has been prepared and approved by Swell Asset Management Pty Limited (ABN 16 168 141 204) Corporate Authorised Representative (CAR No. 465285) of Hughes Funds Management Pty Limited (ABN 42 167 950 236) (AFSL No. 460572). The information in this document is of a general nature only, is not personal investment advice and has been prepared without taking into account your investment objectives, financial situation or particular financial or taxation needs. Investors should read and consider the investment in full and seek advice from a financial adviser or other professional adviser before deciding to invest.

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