Quarterly report

Munro Concentrated Global Growth Fund

MCGG.ASX

March 2024

Munro Concentrated Global Growth Fund & MCGG.ASX

March 2024 – Quarterly report

MCGGF Fund quarter return
24.8%

MSCI quarter return
14.0%

MCGG.ASX Fund quarter return
24.7%

MSCI quarter return
14.0%

QUARTERLY HIGHLIGHTS

- The Munro Concentrated Global Growth Fund returned 24.8% for the March quarter. MCGG.ASX returned 24.7% over the same period.
- Global markets rallied during the quarter, driven by strong company earnings and guidance above market expectations. Returns broadened away from the narrow leadership of the "Magnificent Seven" towards a wider distribution of gains across different sectors and stocks. Following the Federal Reserve's signalling, the market continued to expect rate cuts this year, which contributed to the bullish sentiment.
- The Funds' performance was driven by strong earnings from a broad range of holdings and AoI's. Top contributors for the quarter included Nvidia and TSMC from our High Performance Computing AoI, Constellation Energy from our Climate AoI and Rheinmetall from our Security AoI.

MUNRO MEDIA

Livewire Listed Series: Nick Griffin's formula for double digit returns (plus 13 stocks Munro is backing for the long-term)
18 March 2024
Read the article here

Area of Interest video: Innovative Health
29 March 2024
Watch the video here

CONTENTS

QUARTERLY COMMENTARY

Fund commentary

The Munro Concentrated Global Growth Fund returned 24.8% for the March quarter (MCGG.ASX 24.7%) while the MSCI World (Ex-Australia) index returned 14.0% over the same period.

Global markets rallied during the quarter, driven by strong company earnings and guidance above market expectations. Returns broadened away from the narrow leadership of the “Magnificent Seven” towards a wider distribution of gains across different sectors and stocks. Following the Federal Reserve’s signals, markets continued to expect rate cuts this year, which contributed to the bullish sentiment.

From a Fund perspective, Artificial intelligence (AI) was a dominant theme, stock winners came from multiple different AoI’s that were tied to this theme. High Performance Computing was the standout, with Nvidia and TSMC being the largest contributors to this AoI. The Climate AoI also contributed to performance, with holdings Constellation Energy and Nextracker benefiting from the increased energy requirement to power new AI data centres. Meta Platforms within the Internet Disruption AoI also saw accelerating revenues as improved recommendation algorithms resulted in increased time spent on the platform. Other holdings that also performed particularly well were Security AoI company Rheinmetall and our leading Innovative Health AoI company Eli Lilly.

Market Outlook

Global markets made a strong start to the year, continuing the good momentum coming out of 2023. There is reason to continue to be optimistic throughout 2024 and beyond.

The US Federal Reserve has indicated that the interest rate tightening cycle is over, and whether there are two, three or no rate cuts this year, we believe it doesn't matter. What matters is that the hard work of taming inflation is largely done, and central banks can cut rates from here if needed. In fact, central banks now see themselves in the strongest position they have been in a decade, having seemingly normalised interest rates without collapsing the economy. Consequently, we expect them to be prudent in managing their 500 basis points of economic 'ammunition', ultimately putting themselves in a good position to manage a long and sustained period of future economic growth.

With the interest rate tightening cycle behind us, equities can return to doing what they do best: following their earnings growth. The earnings growth of companies tied to strong secular growth themes has continued to be robust and, in many cases, has started to see acceleration. Over the last quarter, this was most prevalent in how quickly the world is moving to adopt AI. While clearly, we have seen strong moves from stocks tied to the AI theme over the past 12 months, we believe we are still at the very early stages of its evolution with multiple data points to suggest that the adoption of generative AI will create similar large scale winners that the adoption of the internet and mobile internet did in previous cycles. Below we highlight a few key areas where we have invested and some data points that increase our conviction.

Hardware and software. As we have discussed in previous reports (September 2023 MCGGF quarterly report), we see the hardware layer as the picks and shovels in the gold rush and should initially see the strongest earnings growth tied to AI. This has proved to be the case with the staggering acceleration in earnings growth from AI semiconductor champion Nvidia (refer to stock story on page 6) and its supply chain. We believe that their growth looks sustainable with capex budgets from public cloud providers such as Amazon Web Services and Microsoft Azure having increased significantly and are likely to continue to rise into 2025 as they invest in enough computing power to be able to host all the future Generative AI applications that will be hitting the market. Microsoft Azure, for example, is expected to invest $50bn in capex this year, with some analysts suggesting this number could rise to $60bn next year, which is up from less than $30bn just two years ago. These companies are investing so heavily that they clearly see the demand coming down the pipeline. Microsoft Azure pointed to 6% of Azure growth coming from AI services in the last quarter, up from 3% in the prior quarter. Much of this growth will come from AI inferencing, that is, the running of AI applications.

These are large numbers when you consider that Microsoft's Office 365 Copilot has seen relative slow take-up to date. Many other applications have only just become generally available and have not seen enterprise adoption yet. The number of companies we have met with many different industries that are rolling out Generative AI products for their customers in the 2nd half of 2024 and into 2025 continues to grow exponentially. While not all these applications will be successful, or work as advertised on day one, it is now clear to us, that the use cases are plentiful and the opportunity for additional revenue growth from these applications is high.

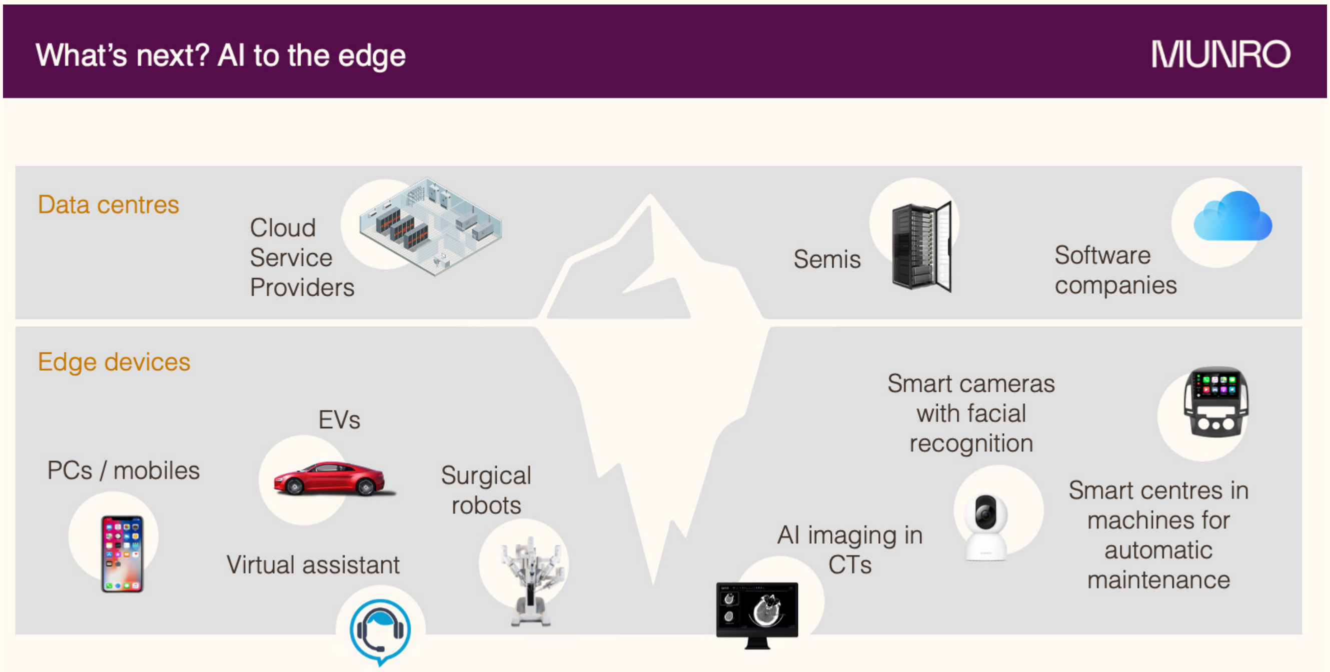
Productivity. Another area of strength that is quietly emerging from the use of Generative AI is productivity enhancements. AirBnB commented that its employees, especially developers, could easily be 30% more productive using tools like GitHub's Copilot in the short to medium term. Privately-held Klarna, the Swedish buy-now-pay-later provider, implemented an AI assistant that now handles the workload equivalent to 700 full-time staff members. These developments could lead to margins expanding more quickly than expected, which we have seen from the likes of Synopsys and Microsoft, or a faster cadence of innovation leading to higher top-line growth.

Power demand. Within the Climate AoI, we are finding many opportunities both in renewable energy and energy efficiency plays that have seen a big uptick in demand for their products and services as the world gears up for the increased power consumption that will come from the adoption of AI. Constellation Energy, the independent power producer that owns and operates the largest nuclear fleet in the US, is one such stock that looks particularly attractive to us. Existing nuclear power plants are the US's largest source of base load renewable power and are uniquely positioned to supply the expanding data centre footprint. A small US nuclear generator company recently signed a contract with Amazon to power a new 960MW data centre at a significant $30/MWh premium (~67%) to the prevailing power price. This highlighted the potential upside in earnings for Constellation Energy as they look to sign long-term contracts with data centre customers to provide carbon-free, baseload generation.

QUARTERLY COMMENTARY

Market Outlook

AI to the Edge. Finally, it is worth highlighting that this should be just the beginning. Soon we expect to see AI driving growth in all our Area's of Interest. Innovative Heath looks like an obvious beneficiary as medical specialities like CT scans and radiology add AI software to cancer detection, surgical robots add AI software to improve patient outcomes, and large pharmaceutical firms use AI models to accelerate drug discovery. Elsewhere large industrial companies will use AI to build more complete digital twins, helping improve productive efficiency while also identifying problems well before construction begins. Security companies will use AI to improve video surveillance and threat detection, while many of our consumer companies will use it to improve throughput at a drive-through, better product design and inventory management. Practically every company in the world will look at this technology to see if it can improve how they operate and the experience they provide their customers. Those companies that do not, risk potentially being disrupted by the ones that do, virtually ensuring a wave of investment in the space that will last well beyond just this year.



While most of our outlook here is dominated by AI, we only highlight it as it's moving quickly. In the medium term, we believe we are at the beginning of a sustained favourable period for growth investing. While AI is dominating the headlines right now, we do expect the economic recovery to begin later in 2024, and we expect to broaden our portfolio as the year goes on. We anticipate innovations in healthcare, efforts to decarbonise the planet and changes in consumer preferences will continue to fuel structural earnings growth independent of the adoption of AI. We see this as an opportunity to lean into our process, identify the areas of structural growth, identify the winners across large and small caps and set our funds up for strong returns in the years ahead.

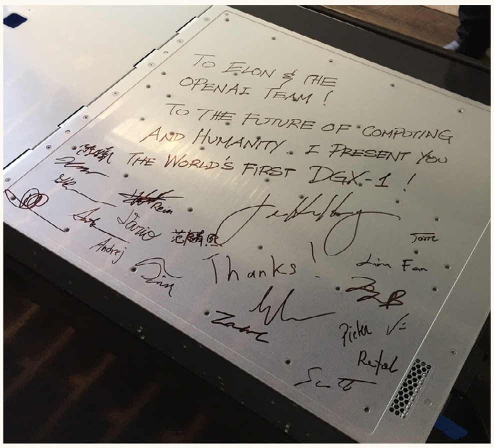
AREA OF INTEREST: **High Performance Computing**
MARKET CAP: **USD $2.3 tn**

Nvidia added 564 bps to Fund performance for the quarter.

Nvidia continued its strong run of performance for the Fund in the March quarter as the key beneficiary of the adoption of generative AI. Performance was driven by another set of exceptional results in February and the company's developer conference GTC in March. Both the results and the event pointed to continued broad adoption of Nvidia's products across all industries, while also highlighting the substantial leadership that the company enjoys in the space versus its competitors. To put this in perspective, Nvidia now looks on track to sell over $100bn in data centre accelerators, or GPU's, this year to cloud service providers, enterprises and sovereign buyers. The next closest competitor, AMD, will sell less than $5bn. Competition is clearly coming to the space, but Nvidia has a huge lead, and with practically every company in the world looking to adopt this technology to improve the way they operate and the experience they provide their customers, it's hard to see why they would risk using an inferior product.

So, how did Nvidia find itself in such a dominant position? Nvidia was founded in 1993 as a fabless semiconductor firm designing graphics accelerator chips for PCs. The initial market opportunity they identified was in gaming, where traditional central processing units (CPUs) dominated the market. These chips were designed to execute math-intensive commands one-at-a-time, which created inefficiencies when rendering video experiences in real time, resulting in slower speeds for certain compute-intensive applications. This led Nvidia to take a different path from the rest of the industry and develop the GeForce 256 graphics processing unit (GPU), a dedicated chip with substantially more cores that allowed these commands to be performed in parallel, resulting in faster execution of complex workloads. In 2006, Nvidia added software to all their chips called CUDA, which has since evolved into a parallel computing platform and programming model used by developers to accelerate their applications by harnessing Nvidia's GPUs. Over the years, new uses for parallel processing have emerged as Nvidia's chips have become more powerful and the software more usable. Eventually moving off PC's and into the data centre to power AI recommendation engines like the Facebook algorithms that control your news feed or ecommerce algorithms that tell you what you might want to buy next. These improved algorithms became the beginning of AI use cases, that sowed the seeds of an even larger opportunity. In August 2016, Jensen Huang, CEO and Co-Founder of Nvidia donated the first DGX-1 supercomputer to a technology start up called OpenAI "in support of democratising AI technology" (see picture below). Six years of intense computer training later, OpenAI launched ChatGPT in November 2022, bringing to life the real use cases of generative AI, forcing every enterprise in the world to evaluate the generational opportunity this technology presents for their industry.

Jensen Huang delivers the first DGX super computer to Open AI in 2016. MUNRO



This has led to the insurmountable demand for Nvidia's AI systems over the last year, as generative AI begins to proliferate through everything we do in our lives. Nvidia is now rapidly becoming the hardware and software platform for generative AI. From here, the question is not who can catch Nvidia, but how big AI will be. Today, Nvidia trades at the same 30x earnings multiple it traded on when we first invested back in 2019. Since then, its net income has risen 15-fold from $4bn to $60bn projected for this year. Looking ahead, we still see growth ahead as more and more industries adopt this technology to drive the next industrial revolution.

STOCK STORY: CONSTELLATION ENERGY

Constellation

AREA OF INTEREST: **Climate**
MARKET CAP: **USD $58.3 bn**

Constellation Energy added 143 bps to Fund performance for the quarter.

Constellation Energy (CEG) was spun-out of Exelon Energy in January 2022 and is an independent power producer that own and operates the largest nuclear fleet in the US, holding over 55% of the nation's unregulated capacity. With plants stretching from the Midwest across to New York, CEG provides >180TWh of carbon-free electricity to Americans each year, which amounts to ~120mn metric tons of CO_2 avoided annually.

At their recent earnings release, CEG initiated 2024 EPS guidance which was 26% ahead of expectations. Management provided lots of helpful insights, breaking the guidance down into 'base earnings' (assuming that they receive the nuclear production tax credit (PTC) floor value of $43.75/MWh on their nuclear generation) and 'enhanced earnings' (driven by higher power prices, retail margins and volatile power markets). They also outlined expectations for these base earnings to grow at 10% per year, as a function of inflation adjustments to the nuclear PTCs and continued strong operating performance. This has since led to a greater investor appreciation for the underlying earnings power and resilience of the base business, in a power industry that is typically deemed cyclical, and the stock has since re-rated to reflect a new earnings profile.

We also see considerable long-term upside to the 'enhanced earnings' component of CEG's guidance stemming from their unique ability to sign long-term contracts with data centre customers to provide carbon-free, baseload generation. During the quarter, a smaller US nuclear generator company, signed a contract with Amazon to repurpose their Susquehanna plant to solely power a new 960MW data centre, highlighting the attractiveness of nuclear power's characteristics. Rough maths implies that Amazon is paying a $30/MWh premium to the nuclear PTC floor (67% uplift), substantially higher than historical retail margins of $3.50/MWh. This dramatic step-up is due to the scarcity of nuclear power, with ~40GW in the US, and only 24GW well-suited for data centre usage (of which we estimate CEG own more than 60%). We expect CEG to follow suit with a considerable portion of its dual unit nuclear capacity, driving company-wide retail margins higher, which has a very strong flow-through to earnings. Ultimately, we can see a path to CEG's earnings tripling over the next 6 years.

STOCK STORY: META

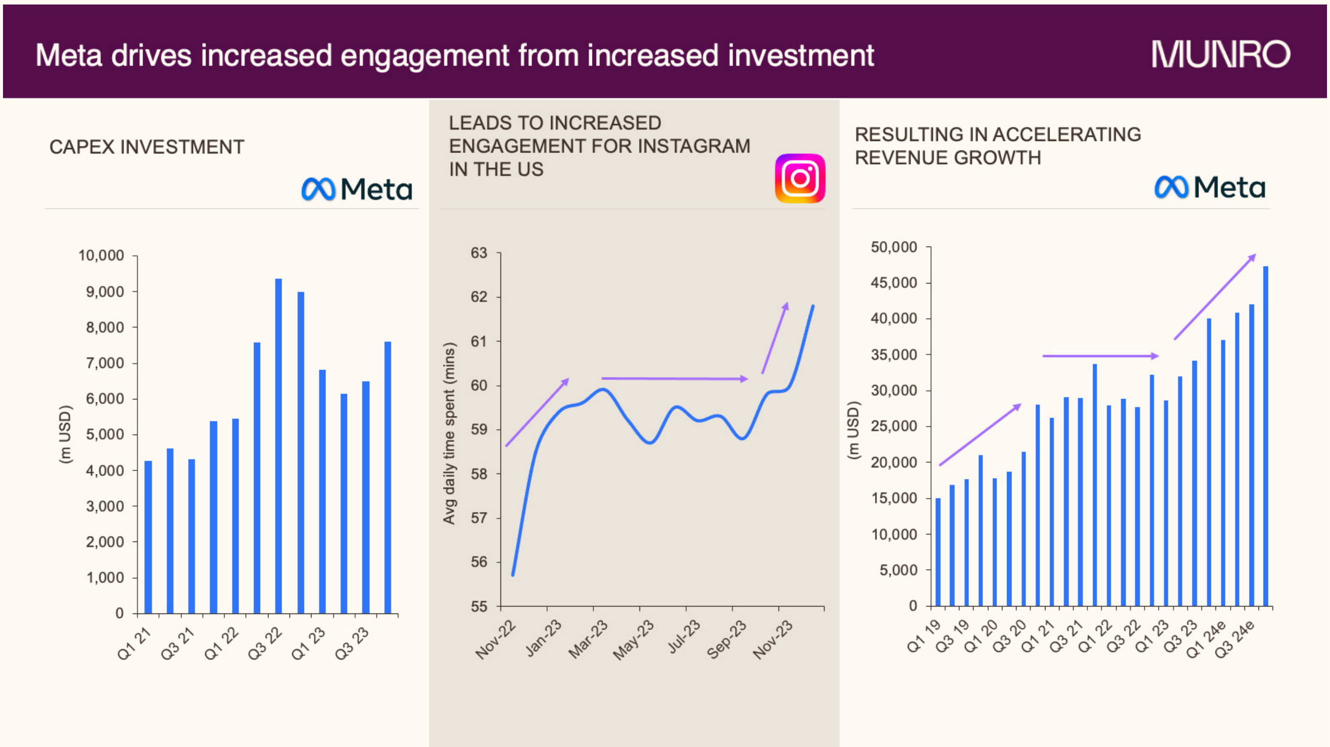
Meta

AREA OF INTEREST: **Digital Media & Content**
MARKET CAP : **USD $1.2 tn**

Meta contributed 122 bps to performance for the March quarter after having returned to the portfolio in 2023. Meta delivered a strong Q4 result during the first quarter, leading to a 20% stock price move on the day, and perhaps the best example of AI at work we saw in the results season.

In 2022, Meta was impacted by several revenue headwinds, including more stringent regulation of consumer data as well as internal limitations on their ability to continue to generate a superior return for their advertiser customers, given technology constraints. Meta's revenues declined year-on-year in 2022, having grown at an almost 29% CAGR in the previous 3 years. Through this difficult period for the company, user growth and engagement began to stagnate. To solve this problem, we estimate the company has spent approximately USD 12.5 billion on Nvidia GPUs to improve its recommendation engine, which is now being used on their short-form video product, Reels. By investing in the best technological capabilities via capital expenditure, the company could re-accelerate engagement with the platform and thus generate revenues from advertisers who are attracted by the increased time spent on the platform (see below). This surprised the broader market with the company's Q4 2023 result, where the guidance provided was for a continuation of the mid-20% growth rate in revenues. Meta had seemingly solved its engagement problem with better recommendation algorithms powered by Nvidia GPU's. Those with teenage children or users of social platforms will have witnessed this transformation firsthand as time spent on Instagram continues to increase.

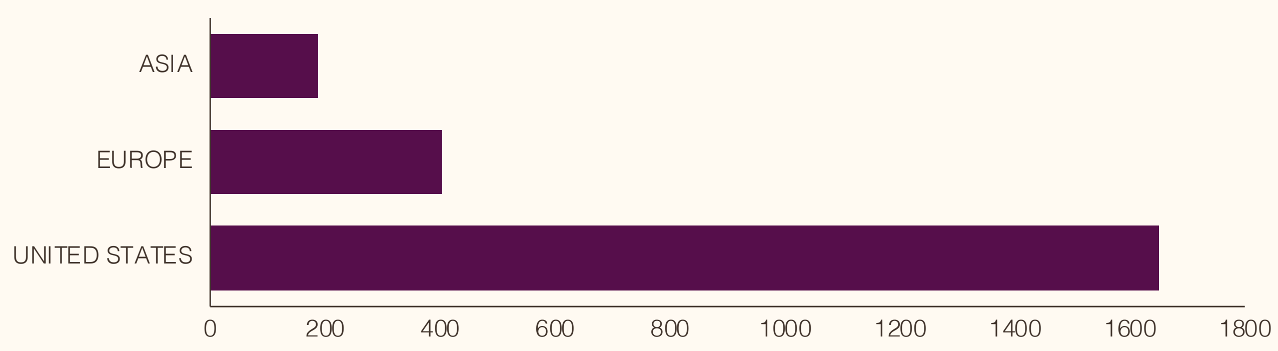
We believe the company can continue to grow its earnings given this advancement in its technological capability, and in our view, it is direct evidence of the merit of acquiring high-end computing power from Nvidia. As Reels continues to grow, we believe advertisers can earn a superior return on spend with Meta, supporting the earnings growth over the medium term. In our view, Reality Labs, (the company's business line focused on machine learning and virtual reality), has the potential to provide upside optionality by management either reducing cost associated with this division or continuing to invest for a return of increased revenue growth. We continue to like the earnings runway for the company and believe it is attractively valued on only ~24x blended forward 12 months earnings estimates.



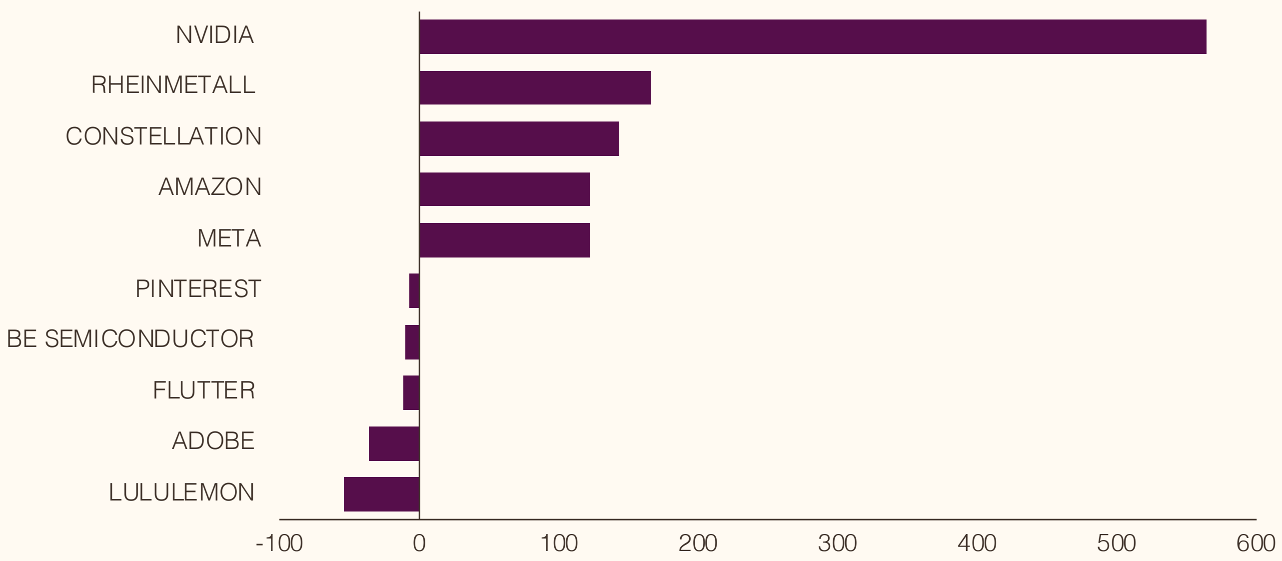
Source: Industry research 31 Jan 2024, Munro Partners estimates, Meta company filings

QUARTERLY FUND ATTRIBUTION (BASIS POINTS)

By region (equities only)



Top & bottom contributors (equities only)



Category

EQUITIES	97.2%
CASH	2.8%
NO. OF POSITIONS	32

Sector

INFORMATION TECHNOLOGY	43.0%
CONSUMER DISCRETIONARY	14.7%
COMMUNICATIONS SERVICES	10.6%
FINANCIALS	8.8%
INDUSTRIALS	8.6%
OTHER	11.4%
CASH	2.8%

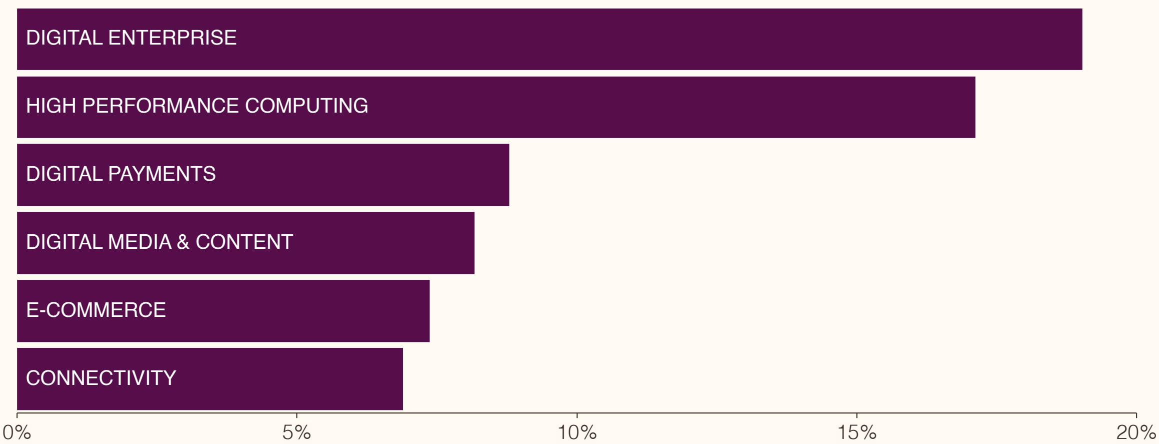
Region

	LONG
UNITED STATES	76.1%
EUROPE	11.9%
NETHERLANDS	3.5%
GERMANY	3.0%
DENMARK	2.4%
FRANCE	1.9%
IRELAND	1.0%
UNITED KINGDOM	2.3%
SOUTH KOREA	2.5%
TAIWAN	4.4%
TOTAL	97.2%
CASH	2.8%

Holdings

TOP 10 HOLDINGS	
NVIDIA	10.1%
AMAZON	7.4%
MICROSOFT	6.9%
CONSTELLATION ENERGY	4.7%
META	4.7%
TSMC	4.4%
SERVICENOW	4.1%
VISA	3.8%
SYNOPSYS	3.5%
RHEINMETALL	3.0%

Top 6 Areas of interest (AOI)



Net Performance - MCGGF

	3 MTHS	6 MTHS	1 YEAR	2 YRS	3 YRS	INCEPT (P.A.)	INCEPT CUM.
MUNRO CONCENTRATED GLOBAL GROWTH FUND (AUD)	24.8%	33.9%	44.6%	20.2%	14.5%	18.2%	109.0%
MSCI WORLD (EX-AUS) TR INDEX (AUD)	14.0%	20.1%	28.7%	15.9%	14.4%	13.5%	74.9%
EXCESS RETURN	10.8%	13.8%	15.9%	4.4%	0.1%	4.7%	34.1%

INCEPTION: 31 OCTOBER 2019

	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
2020FY				0.0%	4.9%	-1.2%	7.4%	-1.1%	-4.2%	6.7%	4.4%	1.3%	19.0%
2021FY	4.4%	4.4%	1.0%	2.0%	3.1%	0.5%	1.2%	-0.4%	-0.2%	3.6%	-2.2%	6.6%	26.5%
2022FY	4.7%	4.6%	-4.7%	1.5%	5.1%	-1.4%	-7.9%	-4.7%	-0.2%	-5.7%	-0.9%	-4.3%	-14.2%
2023FY	7.2%	-3.2%	-2.4%	5.9%	2.0%	-6.6%	1.1%	0.6%	7.6%	2.4%	5.3%	1.7%	22.7%
2024FY	0.5%	3.4%	-5.2%	1.1%	5.3%	0.8%	8.5%	12.0%	2.8%				31.9%

Net Performance - MCGG.ASX

	3 MTHS	6 MTHS	1 YEAR	2 YRS	INCEPT P.A.	INCEPT CUM.
MCGG.ASX (AUD)	24.7%	33.5%	43.9%	19.6%	15.4%	36.2%
MSCI WORLD (EX-AUS) TR INDEX (AUD)	14.0%	20.1%	28.7%	15.9%	12.1%	27.9%
EXCESS RETURN	10.7%	13.4%	15.2%	3.7%	3.3%	8.4%

INCEPTION: 3 FEBRUARY 2022

	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
2022FY								-4.4%	-0.3%	-5.7%	-1.3%	-4.3%	-15.2%
2023FY	7.3%	-3.8%	-2.5%	6.0%	2.1%	-6.5%	1.1%	0.5%	7.7%	2.5%	5.2%	1.4%	22.0%
2024FY	0.5%	3.5%	-5.2%	1.0%	5.1%	0.8%	8.4%	11.9%	2.8%				31.6%

Differences in performance between the Munro Concentrated Global Growth Fund and MCGG.ASX (ASX quoted fund) may be due to cashflow movements, the buy/sell spread of the iNAV for MCGG.ASX, the timing difference between the issuing of units during the day on the ASX for MCGG.ASX and the purchase of units in the Munro Concentrated Global Growth Fund at the end of the day. This may result in variances in performance.