L1 Capital International Fund (Managed Fund)

Quarterly Report | DECEMBER 2023

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L1 CAPITAL INTERNATIONAL

Introduction

In this Quarterly Report, we have outlined:

- **Our assessment of the current investment environment including:**
  - **Why we expect inflation to continue to decline**
  - **Current perspectives, including ongoing normalisation of operating conditions**
  - **Our continued expectations for an economic ‘soft-landing’ and why we are not surprised that economic growth is exceeding consensus expectations**
  - **Why financial commentary is overly focused on changes to short-term interest rates and why rates may stay ‘higher for longer’ compared to consensus expectations**
  - **L1 Capital International Fund positioning**
- **Our review of the last quarter and 2023 calendar year, including key contributors and detractors to the Fund’s performance**
- **Recent Portfolio adjustments**
- **An overview of HCA Healthcare, the leading for-profit hospital operator and outpatient services provider in the United States.**

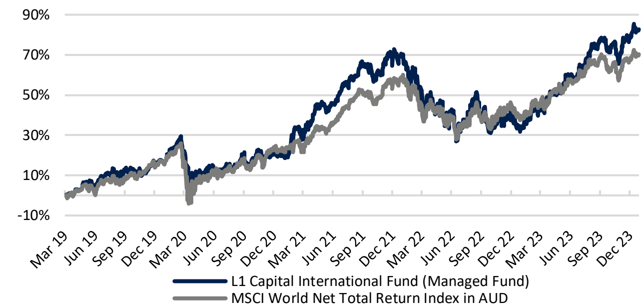
Fund performance (Net) (%)

Fund performance (Net) (%)	Fund	Index**	Alpha
3 months	6.7	5.4	+1.3
1 year	36.9	23.0	+13.9
3 years p.a.	15.1	11.8	+3.3
Since inception* p.a.	13.3	11.6	+1.6
Since inception* cumulative	82.7	70.2	+12.5

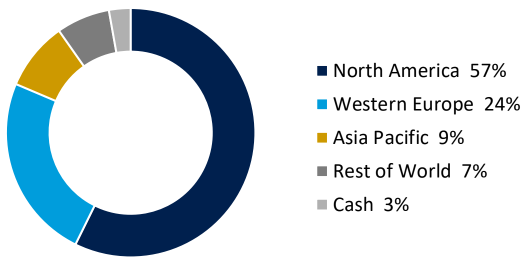
NAV price as at 31 December 2023	$5.1055

** Unit Trust Inception is 1 Mar 2019 (returns measured from Index close). ETMF Inception is 22 Nov 2023. Numbers rounded to one decimal place and may not add due to rounding. ** MSCI World Net Total Return Index in A$.*

Fund (Net) and benchmark returns since inception*



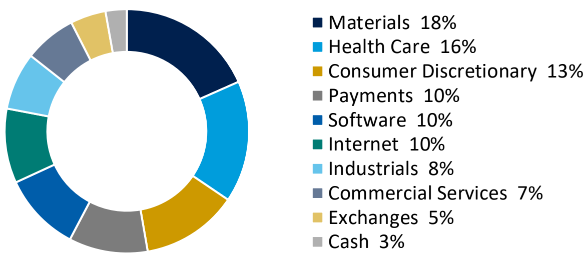
Revenue exposure by region[1]



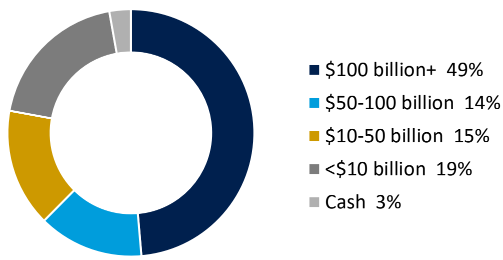
Top 10 holdings *(In alphabetical order)*

Top 10 holdings	Sector
Amazon.com	Consumer Discretionary / Internet
Booking Holdings	Consumer Discretionary
CRH	Materials
Eagle Materials	Materials
Graphic Packaging International	Industrials
HCA Healthcare	Health Care
Mastercard	Payments
Microsoft	Software
Natural Resource Partners	Materials
UnitedHealth Group	Health Care

Sector exposure[2]



Market capitalisation exposure (in US$)



1. Revenue by region is internally estimated on a look through basis based on the underlying revenues of the individual companies held in the portfolio. 2. Sector exposure is defined by L1 Capital International to best describe the nature of the underlying businesses. Past performance should not be taken as an indicator of future performance.

Current investment environment

"By three methods we may learn wisdom: First, by reflection, which is noblest; Second, by imitation, which is easiest; and third by experience, which is the bitterest."

Confucius

2023 macroeconomic reflections

December Quarterly reports trigger reflections on the year just past and this report is no exception. The World Health Organisation (WHO) finally declared the end of the COVID-19 pandemic. Geopolitics remain tragic, with ongoing conflicts in Russia-Ukraine, the Middle East, Africa and other regions, and as well as bizarre events such as the shooting down of a Chinese spy balloon over the U.S. Domestic politics in key global economies remained messy at best. We have lost count of the times Trump has been indicted or ruled ineligible to be a candidate for the U.S. Presidency. Though, it seems no-one told the U.S. population.

A U.S. regional banking crisis came and went, while the Swiss hastily arranged for UBS to acquire Credit Suisse. World temperatures reached record highs while fires, earthquakes, floods and hurricanes caused immense humanitarian and economic damage across the globe. The world's population exceeded 8 billion people, with India overtaking China to become the most populous country, while over 1 in 10 people in Japan are now aged over 80 years. Artificial Intelligence started to become mainstream. Charles III was coronated King of the U.K., and Charlie Munger, the King of Investing, passed. On a lighter note, scientists bred mice from two biologically male parents, the movie Barbie grossed over US$1.4 billion, and Taylor Swift was Time Magazine's Person of the Year with her Eras Tour estimated to have grossed over US$1 billion.

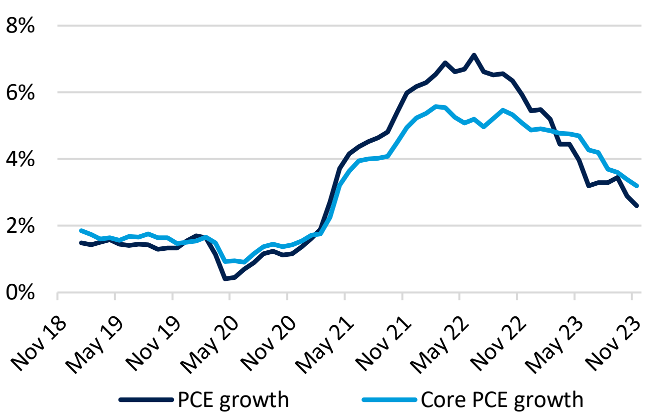
Needless to say, the world is complex and unpredictable. **Compared to world events, the 2023 macroeconomic environment was relatively simple and predictable, although it didn't always feel that way.**

In our **December 2022 Quarterly Report** we noted that "**we expect interest rates and inflation to again dominate financial markets in 2023**." No big round of applause expected for getting that correct. We also commented that "Investors are expecting the Federal Reserve [and other Central Banks around the world] will do what it takes to tame inflation through tightening monetary policy to achieve its inflation policy objectives" and that "…**investors are expecting lower inflation is going to come at the cost of an economic recession**."

Central Banks did not disappoint, with the Federal Reserve continuing its tightening policy, increasing the Federal Funds Rate a further 1.0% to 5.25% to 5.5%.

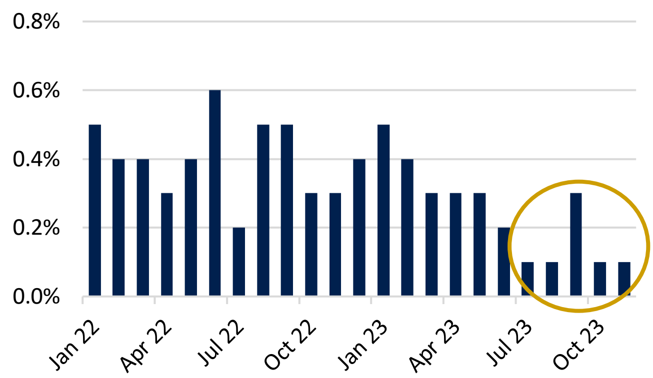
Inflation has declined quite rapidly – not yet to the Federal's Reserve's target of 2%, but well on the way with core PCE growth (the Federal Reserve's preferred measure of inflation) falling to 3.2% in November 2023 and core PCE growth for the last six months of around 1%:

Figure 1: U.S. PCE and Core PCE growth



Source: St Louis Federal Reserve, U.S. Bureau of Economic Analysis

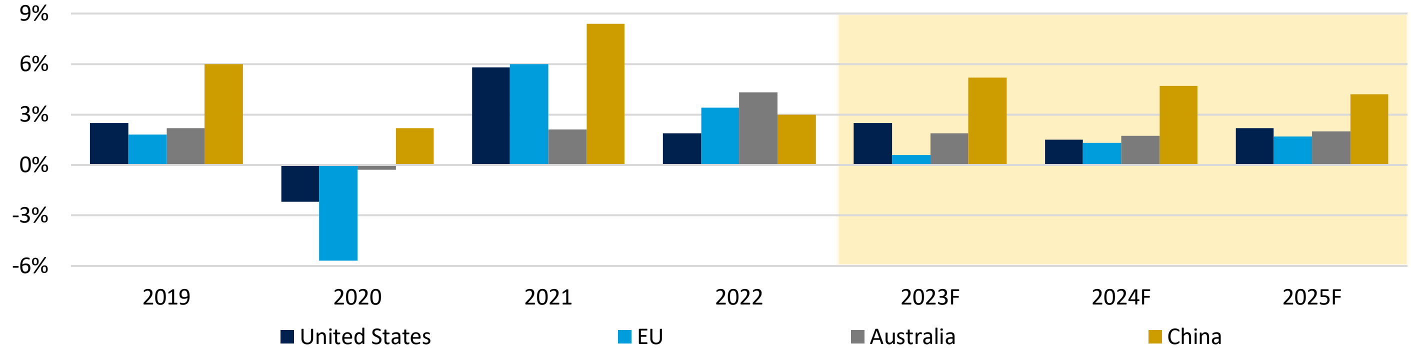
Figure 2: Recent monthly Core PCE growth has been subdued



Source: St Louis Federal Reserve, U.S. Bureau of Economic Analysis

Growth has slowed, with U.S. GDP growth falling to the low-to-mid 2% range (September 2023's growth rate was a strong outlier) and is expected to contract further to 1.5% in 2024 and the low 2% range in 2025. Anaemic growth is also forecast in the EU and Australia as well as slowing growth in China. However **economic activity**, particularly in the U.S., **has remained well above recessionary conditions** with Jerome Powell, the Federal Reserve Chairman, commenting in December 2023 that "**We see the same thing other people see, which is a strong economy, which really put up quite a performance in 2023… [but growth] appears to be moderating.**"

Figure 3: Real GDP growth



Source: World Bank, Federal Reserve, U.S. Congressional Budget Office, European Commission, Reserve Bank of Australia, OECD

Against this challenging backdrop, the MSCI World Index increased by 23.0% (in Australian dollars) in 2023. The L1 Capital International Fund, returned 36.9%, outperforming the Index by 13.9%. At the end of 2022 the market was pricing in a 'hard landing', particularly for many of the companies in the L1 Capital International Fund Portfolio. We commented at the time "**an over-emphasis on short-term challenges is driving share prices well below fair value, providing compelling investment opportunities for longer term investors**." The strong performance of equity markets in general, and the L1 Capital International Fund in particular, reflect a stronger operating environment for many of the businesses we have invested in, particularly compared to overly subdued expectations a year ago, with valuations generally returning towards fair value.

2024 macroeconomic outlook

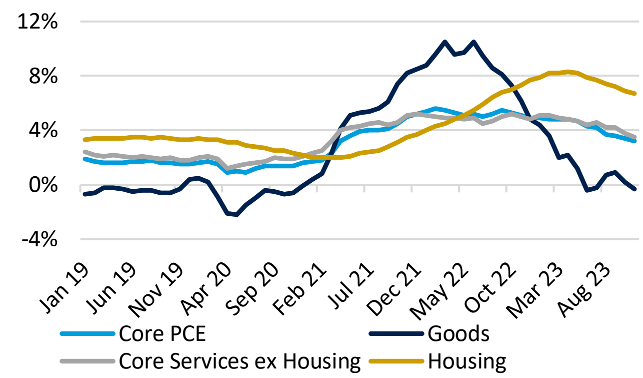
Our **June 2023 Quarterly Report** outlined why we saw parallels between 2023 and the mid 1990s macroeconomic and investment environment. What we wrote then remains current today. **The takeaways were that an economic 'soft landing' was looking more likely and that rising interest rates alone do not by necessity mean the world is heading for a sharp economic recession or that share markets will fall**. Our views have not changed.

Share markets have had a solid six months since then and our confidence in a 'soft landing' or a slowing of economic growth but no recession, particularly in the U.S., has only increased. We remain conservative, sceptical and continue to worry about what may happen next, but so far, the **economic data is looking reasonable.**

Not only is inflation falling, but there is **increased transparency that inflation will continue to ease**. **Goods** (which account for around 25% of Core PCE) are **already deflationary**. Services (which account for around 55% of Core PCE) are still inflationary but are no longer driving up the headline inflation rate. Housing inflation (which accounts for around 20% of Core PCE) has been sticky at high levels but has peaked.

We will now discuss the drivers of these trends in more detail.

Figure 4: Core U.S. PCE growth by category



Source: Bureau of Economic Analysis

It is important to remember that the widespread high levels of inflation in recent times were caused by COVID-19 distortions. In answering a question on whether there was something different about inflation or the U.S. economy this time, Powell responded:

"Inflation was not the classic demand overload, pot-boiling-over, kind of inflation that we [typically] think about. It was a combination of very strong demand, without question, and unusual supply-side restrictions, both on the goods side but also on the labor side, because we had a participation shock. So this is just very unusual."

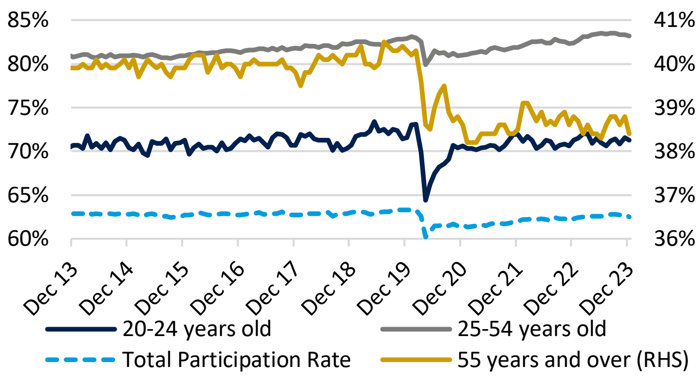
Jerome Powell, December 2023

In our day-to-day activities we interact with a wide range of management teams and businesses. In any given year we log many hundreds of discussions and meetings, as well as review a huge number of results calls and presentations by companies, not just for our Portfolio or Bench of opportunities, but also many other companies that provide relevant information to formulate our investment decisions. As part of these discussions, we have focused on understanding trends in **supply chain normalisation**, as well as **labour conditions**.

There are now very few industries which face any meaningful supply chain disruption (good luck, however, if you are after a new Boeing aircraft in a hurry). Recent security disruptions to shipping in the Middle East pose a risk, but hopefully will not escalate.

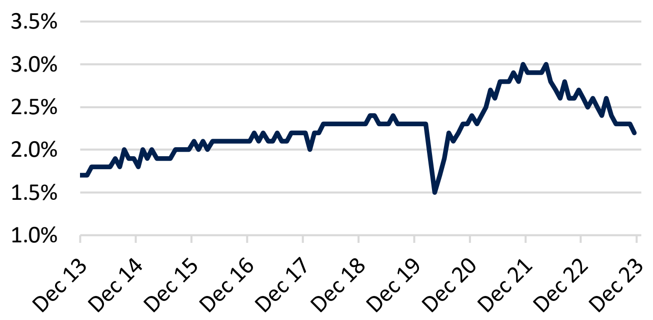
Labour is also becoming easier to attract and retain. Labour force participation rates have reverted back to pre-COVID-19 levels (except for people aged 55 and over, where participation in the workforce has not recovered) and the 'Great Resignation' phase has normalised:

Figure 5: U.S. labour participation



Source: U.S. Bureau of Labor Statistics

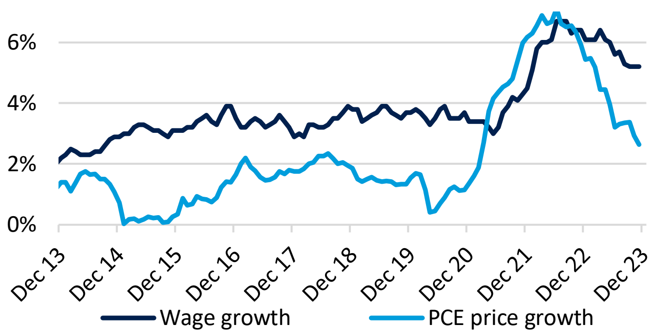
Figure 6: Monthly number of U.S. people quitting their jobs



Source: U.S. Bureau of Labor Statistics, seasonally adjusted

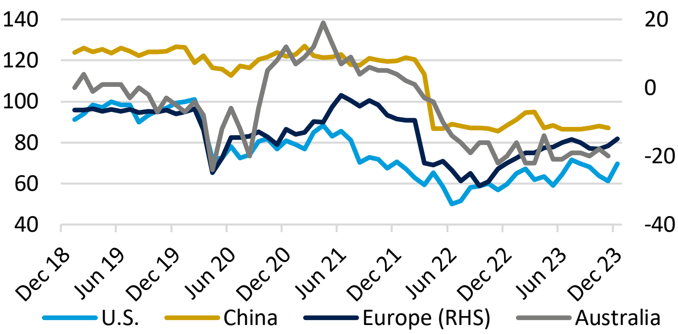
Our empirical discussions support the **continued trend for nominal wage growth to revert to more normal levels**. This view is supported by reported data. **Lower nominal wages growth should result in lower Services inflation over time.** Importantly, from a consumer perspective, **U.S. real wage growth is now positive** (i.e. wage growth is higher than inflation) **which will support nominal spending levels and help to address cost of living pressures.** So even though consumer confidence is low in the U.S. and around the world, we still expect continued growth in nominal consumer spending which will **support economic growth, albeit likely at relatively subdued levels**:

Figure 7: U.S. nominal and real wage growth



Source: Federal Reserve Bank of Atlanta, U.S. Bureau of Economic Analysis

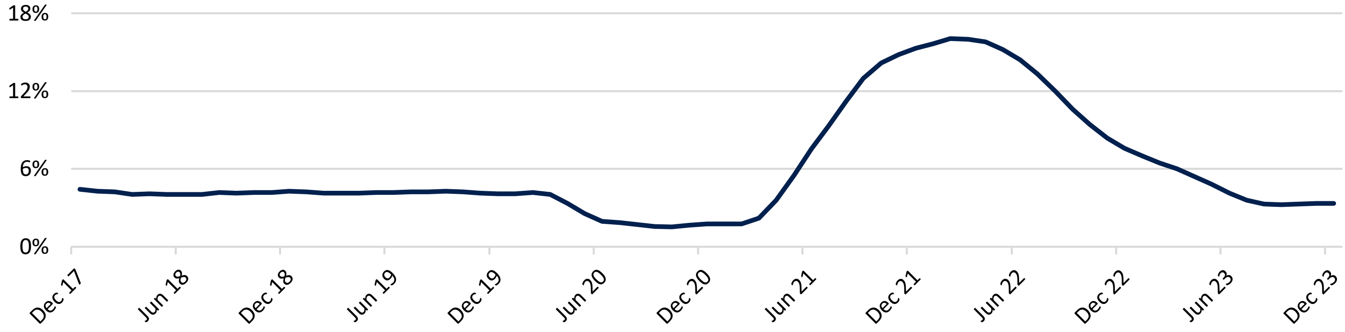
Figure 8: Consumer confidence



Source: St Louis Federal Reserve, Bloomberg, European Commission

Housing inflation remains high at nearly 7% and accounts for over one third of current core PCE growth. Housing's contribution to PCE lags changes in asking rents. While available data is less precise, empirically, **current housing inflation is rapidly falling** and will be reflected in the core PCE inflation calculation over coming months:

Figure 9: U.S. rent growth



Source: Zillow – US Rent Index (all homes)

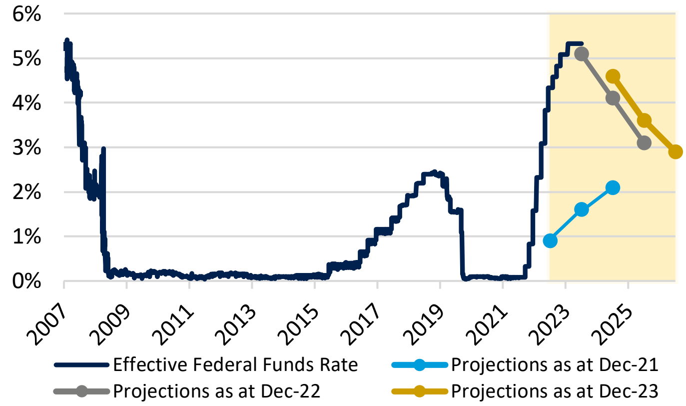
Portfolio positioning

"I want it all, I want it all, I want it all, and I want it now."

Queen

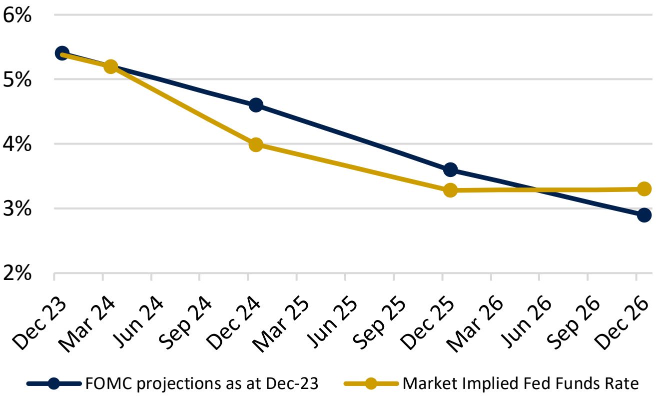
Messaging from the Federal Reserve and other developed market Central Banks globally has changed over recent months. There is general consensus that the current monetary policy tightening cycle is over. **The debate has shifted to when Central Banks will begin to cut interest rates, and by how much.** The FOMC dots are implying the U.S. Federal Funds rate will fall to around 3% by the end of 2026, similar to current market expectations:

Figure 10: Federal Reserve Funds Rate and expectations



Source: St Louis Federal Reserve, Federal Open Market Committee

Figure 11: Federal Reserve vs. market interest rate expectations



Source: St Louis Federal Reserve, Bloomberg

Every month traders and market commentators work themselves into a frenzied reaction to the inflation reports, trying to second guess market trends and central banker reactions to fractional movements in inflation rates relative to expectations. **Most, if not all, of this short-term focused discussion and activity is irrelevant to longer-term investors.**

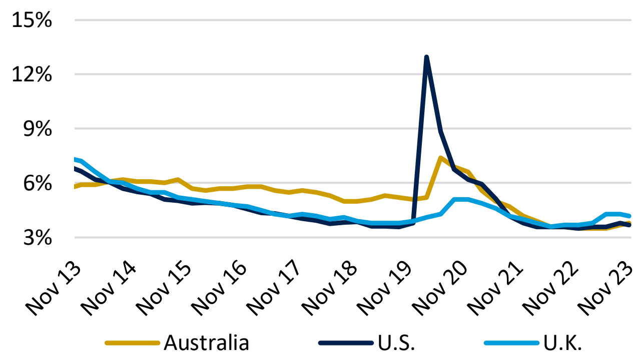
Central Banks generally have two main policy objectives – **full employment** and **price stability** (usually defined as inflation around 2% or sometimes 2% to 3%). When COVID-19 hit Central Banks were solely focused on supporting the economy and employment. For a while post COVID-19 these dual objectives were out of kilter – employment was generally strong, but inflation was well above targeted levels. This led to the rapid increase in interest rates we all know too well. **Today, employment remains robust, and inflation, while coming down, is still meaningfully above targeted levels.**

Longer-term inflation expectations remain well-anchored. Longer-term interest rates (nominal and real) have increased, but not excessively. **We are more focused on long-term interest rates than second guessing precise changes to short term interest rates.**

It is important to consider the reasons why the Federal Reserve and other Central Banks adjust monetary policy. Most market participants view lower interest rates positively for equity markets and higher interest rates negatively.

Sometimes you need to be careful what you wish for. If rates are being reduced because the economy is weak then equity markets may also be under pressure. **Wanting it all** (full employment, price stability and lower interest rates) and wanting it now made for a great song lyric but could be **wishful thinking**.

Figure 12: Unemployment rate



Source: St Louis Federal Reserve, Office for National Statistics, Australian Bureau of Statistics

Central Banks were late in raising interest rates this cycle, and we do not expect Central Banks will pre-emptively reduce interest rates while inflation remains above targeted levels and employment remains robust. Figure 11 on the previous page illustrates that FOMC expectations for interest rates have shifted slightly 'up and to the right' i.e. **short-term interest rates staying higher for longer**. We believe this trend may continue.

We expect **ongoing bifurcation in the spending behaviour of consumers** depending on their socio-economic status. Wealthy consumers benefitting from asset price growth, such as their home and share market portfolio, and higher interest on cash and bond investments are doing well. Middle consumers with steady employment and real wages growth are increasing their aggregate spending and doing O.K. but are being more selective in their spending. Poorer consumers who are disproportionately impacted by cost-of-living pressures and may be dependent on Government assistance are having a tougher time. Credit performance for consumers with the weakest credit ratings is deteriorating the most, and credit availability is also reducing for these consumers.

We also **expect bifurcation in business performance**. Investors have become accustomed to assuming that a company can increase prices and simply blame 'inflation'. **Genuine pricing power is rare**. We are already seeing goods deflation in many industries, and services inflation is rapidly reducing. By definition this means pressure on companies raising prices. However, the cost base for many companies is still inflating – not at the rate experienced in 2022 – but still significantly. Wages growth has slowed, but wages are still growing. Many costs such as insurance, compliance and security (physical and cyber) are unlikely to decrease. In this environment, **margin pressure is likely to be prevalent for many industries and businesses**.

We have spent a number of pages discussing monetary policy, but **fiscal policy** also needs to be considered. In many regions **fiscal policy is supporting economic growth** (and inflation) and super-charging growth in some areas such as development of physical infrastructure. **Immigration policies** are also normalising following COVID-19 disruption and are **pro-growth**.

To summarise, inflation is slowing, growth is slowing, and many consumers (but not all) are under pressure reflected in low consumer confidence. Geopolitics pose continued risks. However monetary policy has peaked (although interest rates may stay higher for longer compared to some expectations), fiscal and other Government policies remain supportive of growth, employment remains fairly robust, consumers are still spending more in aggregate and COVID-19 distortions are largely resolved.

In this context, business selection is of increased critical importance. Investors can no longer rely on TINA or 'There Is No Alternative' that permeated the recent zero interest rate environment. **Valuations matter.** Capital has a cost, and capital is no longer freely available to all businesses.

Our central objective is to invest at sensible valuations in quality companies that have experienced management teams and enduring competitive advantages and financial strength to deliver shareholder returns over time, regardless of short-term fluctuations in economic conditions. We believe our unique definition of Quality, prudently and cautiously applied, results in a diversified portfolio of businesses that can deliver strong risk-adjusted returns across business cycles.

2023 calendar year and December 2023 quarterly review

Performance

In the December 2023 quarter, the Fund returned 6.7% (net of fees), outperforming the Benchmark return of 5.4% by 1.3% (all in Australian dollars). The Australian dollar appreciated 5.7% against the U.S. dollar and appreciated 1.0% against the Euro, decreasing the Fund and Benchmark Australian dollar reported quarterly returns.

In 2023, the Fund returned 36.9% (net of fees), outperforming the Benchmark return of 23.0% by 13.9% (all in Australian dollars). Currency had a limited impact on Australian dollar returns of the Fund and Benchmark in 2023, with the Australian dollar appreciating 0.4% against the U.S. dollar and depreciating 3.2% against the Euro.

Key contributors and detractors

Much has been written about the Magnificent 7 technology companies (Amazon, Alphabet, Apple, Meta, Microsoft, NVIDIA and Tesla) and their strong share price outperformance in 2023 (less has been written recently about the sustainable competitive advantages, exceptional financial performance and strong outlook for many of these businesses or the underperformance by some members of the Magnificent 7 in 2022 which has now reversed).

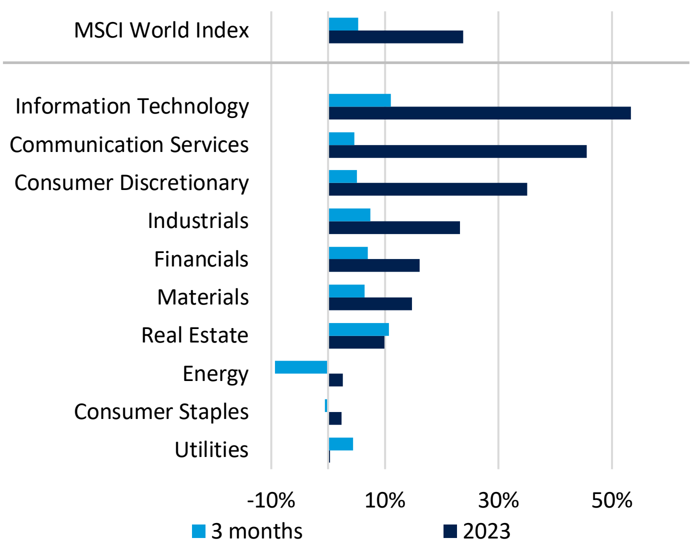
The contribution of the Magnificent 7 to index returns can be seen in Figure 14, with the Magnificent 7 increasing by over 100% in 2023, while the S&P 500 total return was around 24% and the S&P 500 excluding the Magnificent 7 only increasing around 13% (all in U.S. dollars). The impact of the Magnificent 7 can also be seen in Figure 13, with the Information Technology, Communication Services and Consumer Discretionary sectors increasing the most in 2023.

While the Fund's performance benefited from having investments in three of the Magnificent 7, pleasingly **the Fund's returns were very broad based**, across a range of sectors and companies with a wide range of market capitalisation, not just 'mega-tech'.

During the December 2023 Quarter, the share price of around 60% of the Fund's holdings increased by more than 10% in local currency. Six companies each positively contributed 0.5% or more (in AUD) to the Fund's returns for the quarter (in alphabetical order **Amazon.com**, **Booking Holdings**, **CRH**, **Eagle Materials**, **Intuit** and **Microsoft**).

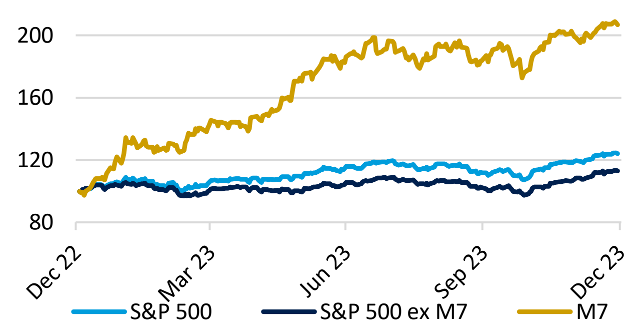
We have written about these businesses in past quarterly reports. They continue to perform in line or ahead of our base case expectations, but following strong share price appreciation are now generally trading within our fair value range. We have selectively reduced the position size of some of these investments, as discussed in the Portfolio adjustments section of this report.

Figure 13: MSCI World Index (in A$) – Sector Performance



Source: Bloomberg

Figure 14: Magnificent 7 compared to the S&P 500 Index – U.S. Equity Prices, 1 Jan 2020 = 100



Source: Macquarie and Bloomberg

No companies detracted from the Fund's returns by 0.5% or more (in AUD) in the December 2023 Quarter.

For the entirety of 2023, the Fund had investments in less than 30 companies. Half of these investments each positively contributed 1.0% or more (in AUD) to the Fund's returns for 2023. The Fund's investments in Alphabet, Amazon.com and Microsoft contributed just over a quarter of the Fund's total gross returns for 2023. **Advanced Micro Devices**, **Booking Holdings**, **CRH, Eagle Materials, Intuit and Natural Resource Partners** also each contributed over 2% (in AUD) to the Fund's 2023 returns.

These companies span a range of industries and vary in market capitalisation. **At L1 Capital International we do not believe in the traditional categorisation of investment philosophy as being either 'Growth' or 'Value'. Rather, investments must meet our unique definition of Quality. Our investment philosophy and investment process provide the opportunity to invest in a portfolio of businesses that can deliver strong risk adjusted returns across a wide range of market conditions.** This can be seen by the contributors to the Fund's performance both in the December 2023 quarter, and over calendar 2023. Technology, Consumer Discretionary, Building Materials, Commercial Services, Healthcare, Resources and Industrials were just some of the industry sectors that positively contributed to the Funds returns, with the market capitalisation of the Fund's investments ranging from around U.S.$1 billion up to nearly U.S. $3 trillion.

No companies detracted from the Fund's 2023 performance by 0.5% or more (nothing came close to this threshold).

Portfolio adjustments

Portfolio adjustments during the December 2023 quarter were again relatively modest, totalling well under 10% of the Fund's investments.

We continued to trim our investment in **Intuit** as, after strong share price appreciation, we now consider the business to be fully valued. We also fully divested our investment in **Analog Devices**, again purely due to valuation considerations. We remain very comfortable with the quality of both of these businesses, with Intuit retained as a smaller holding and Analog Devices moving to our Bench of potential future investments. As outlined earlier in this report, our base case view is that there will not be a recession, particularly in the United States. However, growth is slowing, and this will negatively impact demand for many of Analog Devices' products.

We continued to add to our investment in **HCA Healthcare** (HCA). HCA is the leader in for-profit hospital and outpatient services in the United States. Operating performance will be less impacted by fluctuations in the macroeconomic environment. We have provided a detailed overview of HCA and our investment thesis starting on page 9 of this report.

Other changes were relatively small, but targeted. For example, we reduced our investment in **CME Group** and increased our investment in **Intercontinental Exchange**, two over-lapping but meaningfully differentiated derivatives exchanges. CME has benefitted from U.S. interest rate volatility and overall is a more defensive business compared to Intercontinental Exchange. We expect Intercontinental Exchange's mortgage technology business to benefit from lower residential mortgage rates over time.

Zooming out to look at portfolio adjustments from a 12-month perspective, seven of the top 10 holdings at the start of 2023 are still in the top 10 holdings at the end of 2023, while the remaining three businesses are portfolio investments with smaller position sizes. **We are investors, not traders.** HCA and Natural Resource Partners were added to the Fund in 2023, while the position size of **UnitedHealth Group** (UnitedHealth) was increased during the year.

While the top 10 holdings look broadly similar at the end of 2023 compared to the start of the year, **meaningful changes have been made to the overall portfolio exposure over the past 12 months**. In general, following a strong increase in share prices, we have reduced the portfolio's investments in Technology businesses, and increased exposure to the more defensive Healthcare sector. We have also increased exposure to sectors of the economy which we anticipate will have strong growth over coming years, despite macroeconomic uncertainty, such as physical infrastructure spending in the United States. New residential construction activity in the United States has also proven to be very resilient in the face of rising mortgage rates. We expect construction activity to remain strong, although business selection is critical. Many consumers are under pressures caused by rising interest rates and inflation increasing cost-of-living expenses. Our Consumer Discretionary exposure is highly selective.

The strength of the Magnificent 7 obfuscated wide divergence in business and share price performance in 2023. The current macroeconomic and business environment is challenging. We expect divergence in business and share price performance to continue.

The Fund has remained largely fully invested throughout the year and the Fund usually will be fully invested. **We are yet to meet the investor who can consistently time market exposure**, both when to reduce their investments and when to correctly time reinvestment. We focus on delivering strong long-term risk adjusted returns through capital appreciation over time by investing in a portfolio of high quality, well managed businesses trading at attractive valuations. **We believe the Fund's portfolio of businesses remains well-placed to deliver strong returns to investors over our investment horizon.**

Portfolio investment – HCA Healthcare

Introduction

In the **June 2023 Quarterly Report** we outlined why UnitedHealth, as the leading scale player with unrivalled depth and breadth of healthcare capabilities, was exceptionally well placed to benefit from ever-growing U.S. health spending while also lowering overall healthcare system costs.

In this report, we would like to continue the healthcare theme by introducing **HCA Healthcare** (HCA) and outlining why this business is also well placed to benefit from long-term healthcare drivers.

Overview

HCA operates 183 hospitals, 317 urgent care centres, 142 FSERs (free standing emergency rooms), 148 ambulatory surgery centres, 137 imaging centres, over 100 home health and hospice agencies or behavioural health sites of care, and over 1,600 physician practices at last count. HCA is one of the largest hospital systems in the U.S. operating across 20 states as well as in the U.K. Around 60% of revenue is generated from inpatient services and 40% from outpatient services.

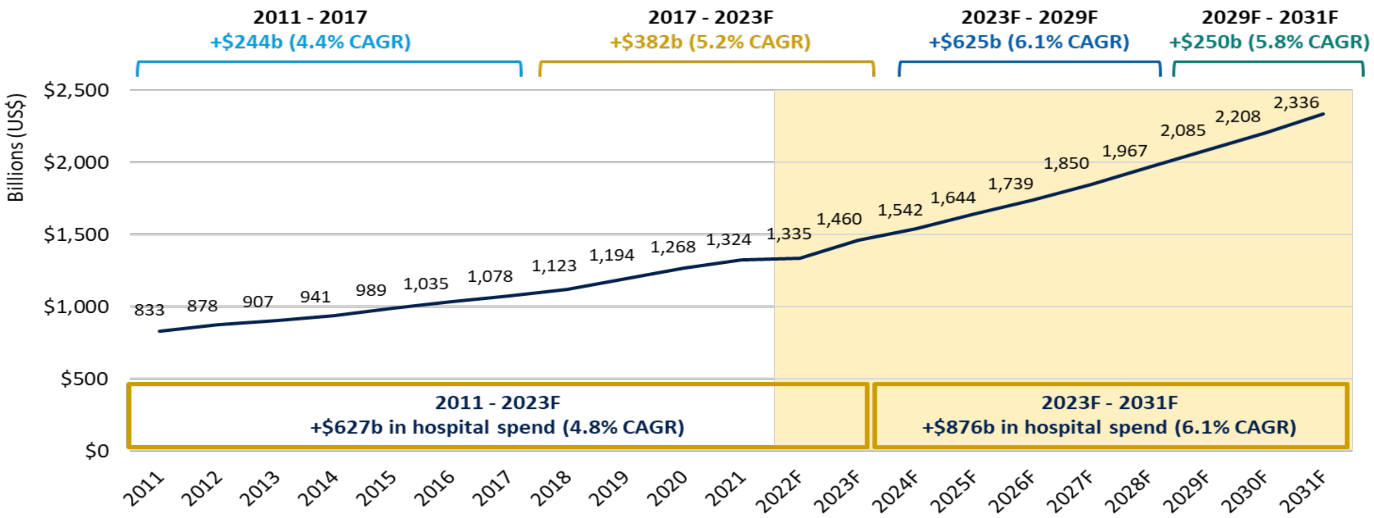
HCA benefits from:

- Sustainable long-term growth drivers,
- A geographic footprint with above average demand growth,
- A number 1 or number 2 inpatient market share in over 80% of markets in which it operates, as well as a comprehensive network of outpatient facilities and services to drive increasing overall health services market share,
- Having leading facilities which attract the best physicians and enable HCA to increase its share of revenue from high acuity services, and
- Operating efficiencies and cashflow generation that exceed the majority of its competition, supporting sustainable and profitable growth.

Long-term growth drivers

According to the CMS' (Centers for Medicare and Medicaid Services) projections, U.S. government spending on hospital services is expected to accelerate in the coming decade relative to the previous decade. This growth in spending is driven by improving but expensive healthcare treatments, as well as an aging population.

Figure 15: U.S. hospital expenditure

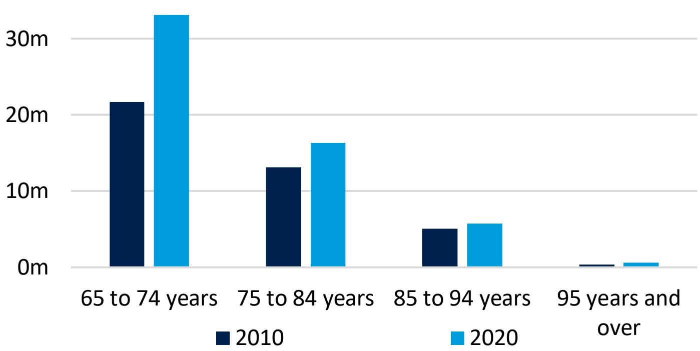


Source: Office of the Actuary in the Centers for Medicare & Medicaid Services, released June 2023, HCA

The percentage of the population aged 65+ years has increased from 5% in 1920 to 10% in 1960 and today is around 17%. Older people attend emergency rooms (ER) more frequently than younger people, and their acuity needs are higher. Overall, 75% of hospital admissions originate in the ER and 50% of inpatient surgeries originate in the ER.

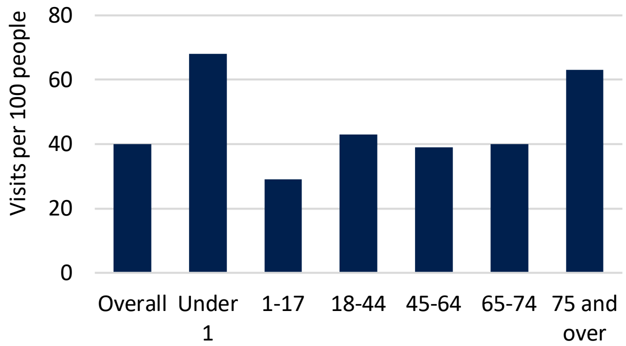
There are simply more older Americans than there used to be, and this is the population that disproportionately makes use of medical services. We estimate people aged 60 to 70 years account for twice as many hospital admissions as 40- to 50-year-olds despite being a slightly smaller population size.

Figure 16: Increasing population size of older age groups,



Source: U.S. Census Bureau, U.S. Department of Health and Human Services, L1 Capital International

Figure 17: Emergency department visits by age group – 2020



Source: U.S. Census Bureau, U.S. Department of Health and Human Services, L1 Capital International

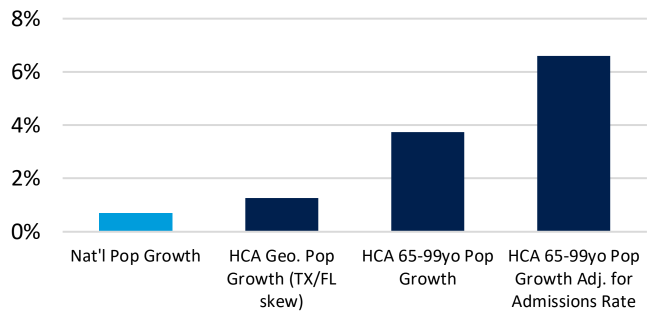
Footprint and market share

Approximately 80% of HCA's hospital beds are located in states with almost 2x the national average population growth, including Texas and Florida which account for over 55% of HCA's total hospital beds. Within that footprint, the population aged 65+ is growing at over 5x the national average population growth.

If we adjust for the higher rate of hospital admissions of this age group, the growth rate almost doubles again (9x the national population growth). Texas and Florida are also fast-growing states for employment growth, supporting commercial health insurance growth and associated hospital coverage**. HCA's favourable demographic and geographical footprint are long-term tailwinds supporting HCA's continued growth.**

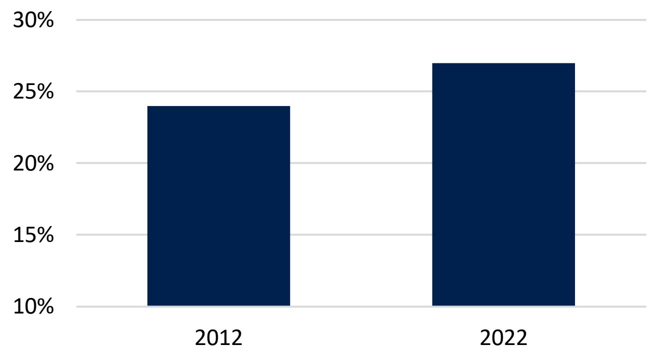
In addition, HCA continues to gain market share over time in its core geographies through concerted investments in their physical network, physicians, nurses and other employees, and the range of services provided. HCA estimates it has either the leading or the second largest inpatient market share in over 80% of the markets in which they operate.

Figure 18: Population, age and admissions growth 2010-2020



Source: US Census Bureau, HCA, National Library of Medicine-National Institutes of Health (NIH), L1 Capital International

Figure 19: Inpatient market share



Source: HCA

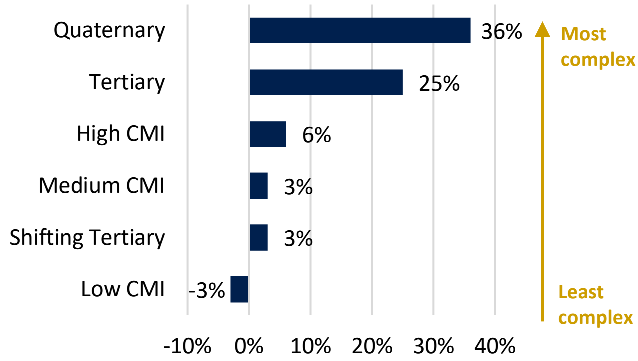
Improving case mix and diverse revenue base

Over the past decade, HCA's case mix index (CMI) has grown by greater than 25% cumulatively. The CMI is a measure of acuity and is linked to reimbursement for procedures. The increase in CMI is by design.

In the past decade, HCA has invested to nearly quadruple its advanced stroke centres, and more than triple its trauma and burn programs. The number of transplant and cellular therapies provided annually has more than doubled over the past decade, while significant investments have been made in cardiac and vascular programs.

High acuity services are forecast to be key growth areas for inpatient services over the next decade.

Figure 20: Inpatient services growth – 2023 to 2033

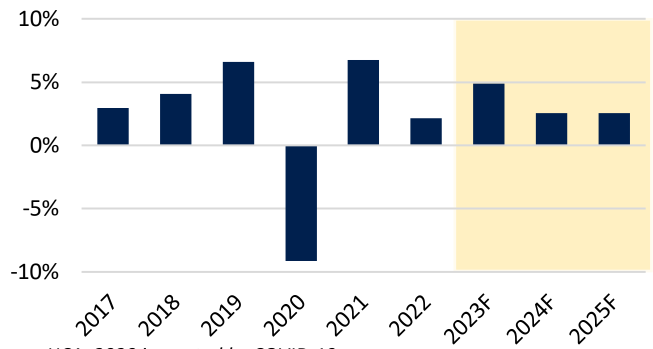


Source: HCA – Sg2 Growth Modelling, July 2023

Consistent revenue growth, improving operating efficiencies

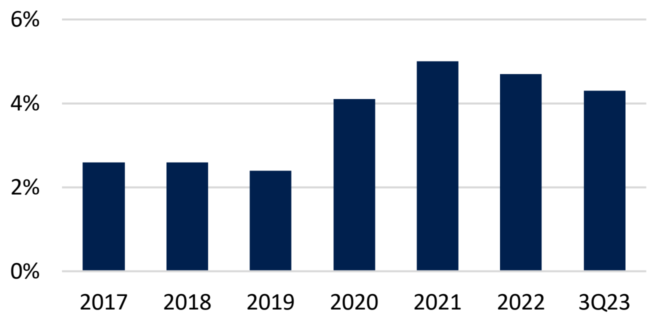
HCA's revenue growth algorithm is straightforward. Equivalent admissions (HCA's measure of volume) should grow 2 to 3% per year driven by population growth, an aging population and increased market share. Revenue per equivalent admissions should also increase around another 2 to 3% per year driven by case mix improvements. Outpatient revenue has grown in line with inpatient revenues over time. Combined, this supports consistent 5 to 6% revenue growth per year.

Figure 21: Equivalent admissions



Source: HCA. 2020 impacted by COVID-19

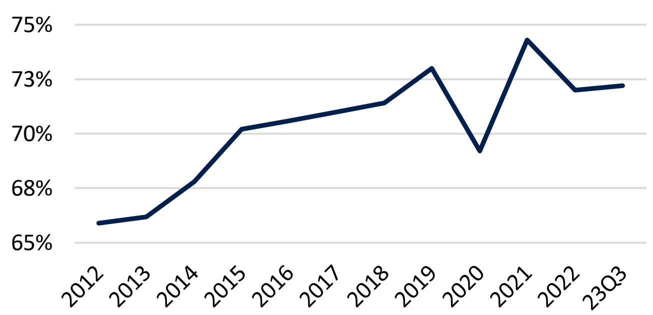
Figure 22: Revenue per equivalent admission – 5y rolling CAGR



Source: HCA

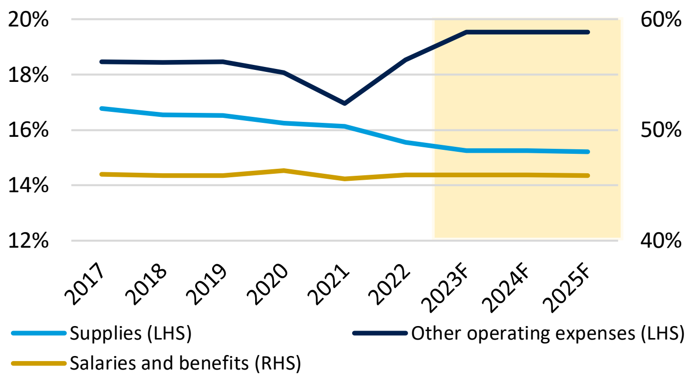
Hospital occupancy has continued to inch up and expenses have been tightly managed to offset periodic cost pressures and maintain margins.

Figure 23: Inpatient occupancy



Source: HCA

Figure 24: Expenses as a percentage of revenue

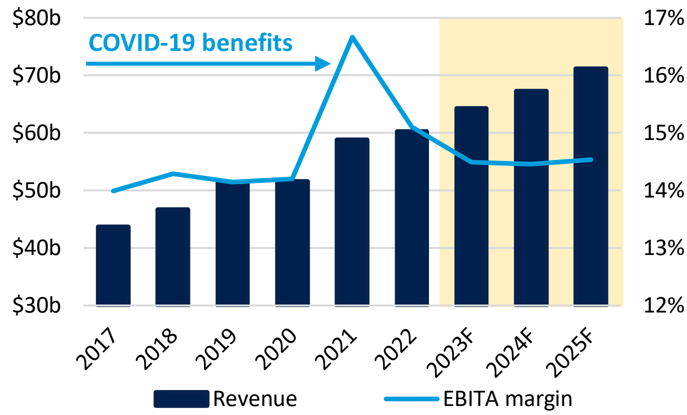


Source: HCA, L1 Capital International

Attractive financial performance

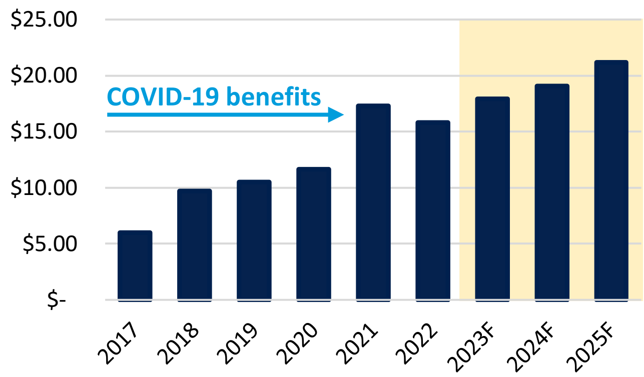
Strong long-term growth drivers, leading market positions and service capabilities and experienced and aligned management combine to deliver consistent, dependable growth in cashflow and profitability. Cashflow has been reinvested to fund this growth, generating attractive returns on incremental invested capital. Free cashflow after reinvestment has funded dividends and buybacks, delivering double digit EPS growth which we forecast to continue over time.

Figure 25: Revenue and EBITA margins



Source: HCA, L1 Capital International

Figure 26: Earnings per share



Source: HCA, L1 Capital International

We materially added to our investment in HCA a few months ago when the share price over-reacted to some short-term cost pressures. The share price has increased strongly since then, with HCA now trading on a forward PE ratio of under 15x and a free cashflow yield of over 5%. HCA still offers an attractive base case risk adjusted return and is currently a top 10 Portfolio holding.

L1 Capital International Fund (Managed Fund)

Quarterly Report | DECEMBER 2023

APIR: ETL1954AU ASX:L1IF

Fund Information

Name	L1 Capital International Fund (Managed Fund)
Portfolio management	David Steinthal, Chief Investment Officer
Types of investments	Listed securities globally. Developed market focus. No shorting, no leverage
Number of investments	20 to 40
Cash weighting	0% to 25%
Minimum initial investment	$25,000
Hedging	Unhedged
Structure	Dual Registry
Domicile/Currency	Australia/A$
Inception	1 March 2019
Management fee	1.2% p.a. inclusive of GST and net of RITC
Expenses	Nil (included in Management Fee)
Benchmark	MSCI World Net Total Return Index in A$
Performance fee	15.38% over Benchmark inclusive of GST and net of RITC*
High watermark	Yes
APIR / ISIN / ASX Ticker	ETL1954AU / AU0000302960 / L1IF
Platform availability	Asgard, Australian Money Market, BT Panorama, CFS Firstwrap, Hub24, Macquarie Wrap, Mason Stevens, MLC, Netwealth, North, Powerwrap, Praemium

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L1 Capital International overview

L1 Capital International is an independent active manager of global equities established as a joint venture with L1 Capital. We apply a detailed investment process built on a fundamental assessment of quality and value. We aim to deliver attractive risk-adjusted returns by investing in high-quality companies that have favourable cashflow-based valuations in well-structured industries. Capital preservation over the investment horizon is central to our investment philosophy and process. We view risk as the potential for a permanent loss of capital as opposed to volatility in share prices. Additional information on L1 Capital International is available at **www.L1International.com**.

L1 Capital is a global investment manager with offices in Melbourne, Sydney, Miami and London. The business was established in 2007 and is owned by its senior staff, led by founders Raphael Lamm and Mark Landau. L1 Capital's clients include large superannuation funds, pension funds, asset consultants, financial planning groups, family offices, high net worth individuals and retail investors. Additional information on L1 Capital is available at **www.L1.com.au**.

Key service providers for the Fund are: Responsible Entity – Equity Trustees Limited, Fund Administrator and Fund Custodian – Apex Group, Fund Auditor – EY, Legal Advisor – Hall & Wilcox. There have been no changes to key service providers since the last report.

* There must be positive absolute performance (adjusted for distributions) in the performance period. Otherwise, positive relative performance carries forward to next Period.