MORPHIC ETHICAL EQUITIES FUND

Monthly Report
January 2024

A proud founder of: Climate Action 100+

Signatory of: PRI Principles for Responsible Investment

Fund Objective

The Morphic Ethical Equities Fund Limited (MEC) seeks to provide investors a way to grow their wealth and feel confident they do so without investing in businesses that harm the environment, people, and society.

MEC excludes direct investments in entities involved in environmental destruction, including coal and uranium mining, oil and gas, intensive animal farming and aquaculture, tobacco and alcohol, armaments, gambling and rainforest and old growth logging.

Investment returns*

	1 Month	3 Months	6 Months	1 Year	3 Years (p.a.)	5 Years (p.a.)	ITD (p.a.)
MEC[1]	1.82%	11.88%	-3.24%	10.26%	2.67%	7.79%	6.74%
Index[2]	3.83%	10.29%	6.09%	22.26%	11.52%	12.34%	11.20%

* Past Performance is not an indication of future performance.

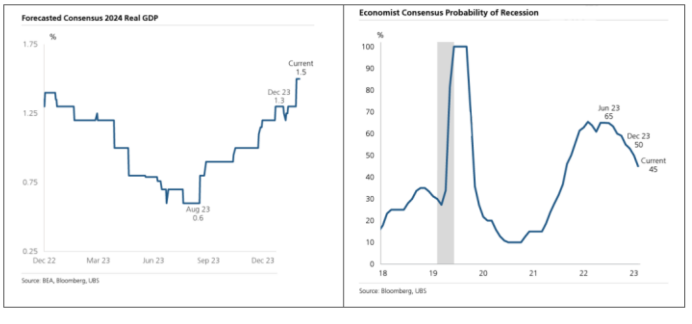
Performance Summary

MEC increased +1.82% net during the month. underperforming the MSCI All Countries World Daily Total Return Net Index which increased by +3.83% over the same period.

Market Commentary

The portfolio's top three contributors DigitalBridge, Ciena and Advantest adding 121bps to performance while GDS, Chart Industries and Soitec detracted 167 bps during the month.

Global indices came in quite mixed during January despite economic releases coming in particularly strong driven by solid payrolls, consumer confidence and a rebound in global PMIs. These data points have led to improving economic forecasts, with upward revisions to 2024 GDP growth forecasts driving the likelihood of a recession down over the past few months. The Fed pivot in early November 2023 kickstarted the initial equity rally however we have seen indices continue to march upwards, and this is likely driven by the following charts:



There are many predictions on the Fed's interest rate path over the next 12 months however with inflation declining quite materially from its peak, there is scope for some meaningful cuts going forward. Now with inflation currently under control, the Fed put comes back into play which should help cushion markets in time of stress.

Net Tangible Assets (NTA)

NTA value before tax[3]	$1.0842
NTA value after tax[3]	$1.1086

Investment Returns since inception[4]

Over the past couple of years, it was impossible for the Fed to fight inflation while providing any monetary support to the market in the form of rate reductions. Now with the supply side inflation shock in the rear mirror, there is scope for monetary support and the market recognises this potential risk mitigation.

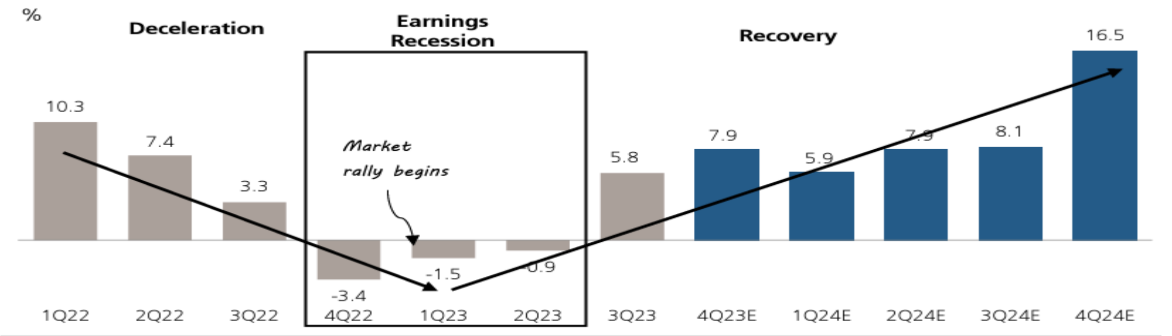
This will likely become more relevant over the next couple of quarters as the delayed impact of past monetary tightening works its way through the system. Economic growth has certainly exceeded expectations however with fiscal stimulus turning into a mild headwind, consumer spending likely normalising as Covid savings are depleted and many companies working off large order backlogs as supply chains normalise, we should see a dampening effect on near term growth.

At the time of writing, we are in the midst of the fourth quarter reporting season with approximately 65% of the S&P500 having reported results. Going into results, December quarter revenues had been forecast to grow by 3.1% with earnings growing at a 7.9% clip. According to UBS, so far earnings are beating estimates by 6.8% with 71% of companies topping expectations.

What is interesting is that we are now cycling some pretty weak comparisons as the market already went through an earnings recession in late CY22 and early CY23. There will clearly be diverging trends in underlying company performance however in aggregate there looks to be a couple of quarters of solid prints coming in. The real question in the divergence of earnings will be which companies raised prices because they should (and will hold them) and those that raised prices just because they could in an inflationary environment (and will give them back):

Earnings – Growth

Figure 6: S&P 500 EPS Growth



Source: Standard & Poor's, Refinitiv, FactSet, UBS
Note: Blend of actuals where available and estimates

Regional discussion:

As highlighted earlier, the stronger economic data coupled with peak interest rates is leading to a reduction in recession expectations however global equity performance was quite mixed. The S&P500 and Nasdaq were up 1.7% and 1.0% respectively while the Russell 2000 gave back some its extraordinary gains in December, declining 3.9% in January. The FTSE (down 1.3%) CAC (up 1.6%) and DAX (up 0.9%) were overshadowed by Japan's Nikkei 225 which was up 8.4% during January.
The US stock market showcased strong performance driven by economic resilience, with a 3.1% GDP growth in 2023, robust consumer spending, and low unemployment rates. Anticipation of potential interest rate cuts contributed to investor optimism, further buoyed by significant gains in technology and AI sectors. The market's positive trajectory was influenced by a narrow set of tech and communication service companies, highlighting the impact of specific sectors on overall market dynamics. Despite high valuations, investor sentiment remained positive, reflecting confidence in the economy's outlook and the continued growth of key industries.

The positive performance in Japan was attributed to a variety of factors, including optimism about the global economy, a positive turn for the Japanese economy, and specific local market reforms aimed at improving market efficiency, corporate governance, and transparency, all of which buoyed investor sentiment. We had previously increased our exposure to the region and therefore benefitted from this exposure.

One major negative call out during January was the Hang Seng Index which was down by 9.2% with challenges primarily due to economic concerns in China and regulatory measures. Persistent economic weakness in China, as evidenced by a contraction in manufacturing activity for the third consecutive month, directly impacted market sentiment in Hong Kong. The Purchasing Managers' Index (PMI) data, indicating continued economic contraction, raised concerns among investors about the health of the economy closely tied to China's. Additionally, regulatory interventions by China to stabilize stock prices, such as suspending securities lending of restricted shares, aimed to stem market routs but also highlighted underlying market vulnerabilities.

Sector discussion:

Communication Services had a solid month as the advancements in AI leads to improved customer experiences, operational efficiencies, and new revenue opportunities for companies within the sector. Additionally, strategic mergers and acquisitions, expansion into new markets, and the development of new products or services that capture consumer interest also significantly contribute to the sector's strong performance.

Information Technology had a strong performance driven by continued technological innovation, increased adoption of digital technologies across various industries, and significant earnings growth among leading tech companies. The sector capitalized on ongoing trends such as cloud computing, artificial intelligence, and cybersecurity, reflecting investors' growing confidence in technology's role in driving future economic growth and efficiency gains.

For Financials, the outlook appears more optimistic, influenced by macroeconomic factors and the prevailing high interest rate environment. This landscape has significantly altered the sector, creating opportunities for discerning stock selection. Investors see potential value include banks with robust deposit bases, firms engaged in capital markets, and select life insurers, presenting a promising arena for investment strategies. More recently we have seen some pressure in the regional banks as New York Community Bancorp's (NYCB) poor profit performance raised CRE concerns for the group. We consider this scenario to be quite different to that of March/April last year when regional bank liquidity was called into question. While the outlook for CRE is certainly not rosy, this weakness could provide an opportunity as the issues with NYCB appear idiosyncratic.

The Real Estate sector performed poorly in January 2024 primarily due to its sensitivity to interest rates. The market was initially expecting rate cut to begin as early as first quarter of 2024. Now investors were concerned that the Federal Reserve might not lower the cost of borrowing as quickly as the markets had hoped.

Portfolio Commentary

Turning back to January performance, key contributors for the month were:

DigitalBridge Group (+0.44%) is the largest pure play digital infrastructure asset manager in the world focusing on the assets which power the unstoppable secular trend of data growth in the digital world. Its diverse portfolio covers mobile towers, edge computing, hyperscale data centres, fibre, small cells and more. As a lead investor, in January DigitalBridge announced the formation of Articul8 AI, Inc. an independent company offering enterprise customers a full-stack, vertically optimized and secure generative artificial intelligence (GenAI) software platform. This investment is buoyed by significant gains in technology and AI sectors.

Ciena Corporation (+0.42%) is the leader in supplying optical network infrastructure around the world. It is number one globally in the majority of its market segments including a dominant position in Subsea Cable Networks as well as Data Centre Interconnect. We noted that Ciena was upgraded by a global independent investment banking advisory firm as it thinks the last earnings report "sufficiently reset" expectations and could result in beat and raises throughout the rest of the fiscal year.

Advantest Corp (+0.36%) operates in the duopolistic System on Chip (SoC) testing market within the back-end supply chain of semiconductor production. It has a strong position within Android and high-performance computing which are leading these technology transitions. Advantest reported its third quarter financials in January which beat the consensus and management has upgraded FY23 guidance.

Conversely, the major detractors during January were:

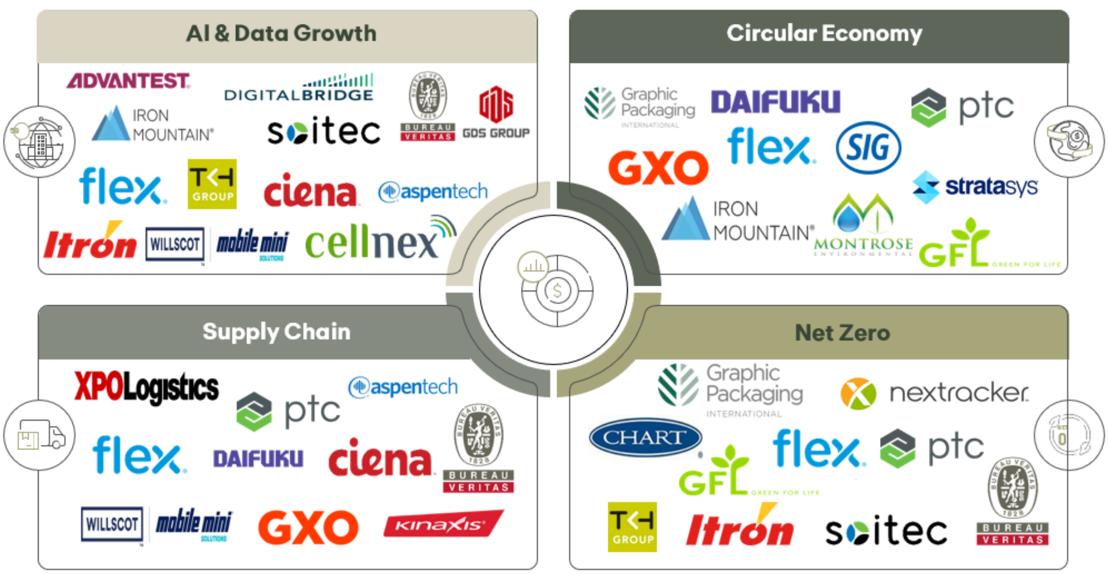
GDS Holdings (-0.73%) is a recent addition to the fund and is the leading vertically integrated provider of high-performance data centre and IT infrastructure service in China and South East Asia. No material company specific news flow during January, rather more caught up in the week Hong Kong market and economic concerns in China.

Chart Industries (-0.52%) is a global manufacturer of specialised equipment servicing multiple applications in the clean energy, industrial gas and water treatment markets. Chart provides customers with highly engineered and vital solutions across the entire liquid gas supply chain. In January, U.S. announced a moratorium on certain new U.S. LNG export permits. The market reaction has been sharp but there is no significant impact from the event for Chart.

Soitec SA (-0.41%) is a world leader in the production of innovative semiconductor materials which help to speed up the mobile and digital revolutions. Its products are used to manufacture chips that go into smart phones, tablets, computers, IT servers and data centres as well as electronic components in cars, connected devices, and industrial and medical equipment. In January, Soitec released a report on its engineered substrates to enable AI adoption. No material company specific news other than that had been announced.

With a new calendar year underway and following a very interesting trip to the CES conference in early January, we have made a number of changes in stock positioning during the month. The aim is to gain more exposure to high conviction ideas while weeding out underperformers and smaller positions to fund the shift. Accordingly, we exited small positions in Bloom Energy and Cardlytics while also exiting Rentokil (where we have concerns about integration execution) and Sensata (where we are stepping to the sidelines as EV penetration appears delayed). We allocated these funds into increased exposure to Nextracker, OBIC Business Consultants, Resona Bank and Alight. We also initiated a position in Itron which is primarily focussed on U.S. utility grids to help them manage increasingly complex grid edge infrastructures using metering and network devices.

We continue to have differentiated exposure to some pretty powerful long term thematics which should drive long term compounding benefits to us all as investors. These include 5G and the growth in data as Industrial IoT, AI and large language networks such as ChatGPT and next generation applications drive data demand, companies that enable our push to a circular economy, beneficiaries of deglobalisation as well as those helping to improve supply chain efficiency and companies which are levered to the multi trillion-dollar spending required for our "Road to Net Zero".



Source: Ellerston Capital

These businesses, as well as idiosyncratic opportunities in the Fund, should provide solid absolute and relative returns over the long term as secular and structural business drivers help mitigate earnings risk in times of economic uncertainty.

As always, we thank you for your continued support and look forward to providing further updates in the future.

Top 10 Active Positions

Stocks	Industry	Region	Position Weighting %
GFL Environmental	Industrials	North America	7.09
Cellnex Telecom	Communication Services	Europe	4.79
Option Care Health	Health Care	North America	4.42
PTC	Information Technology	North America	4.27
WillScot Mobile Mini Holdings	Industrials	North America	4.20
DigitalBridge Group	Real Estate	North America	4.12
Webster Financial Corporation	Financials	North America	3.70
Chart Industries,.	Industrials	North America	3.16
Acadia Healthcare Company,	Health Care	North America	2.86
GXO Logistics	Industrials	North America	2.85

Risk Measures	
Net Exposure[5]	94.99%
Gross Exposure[6]	94.99%
VAR[7]	1.59%
Best Month	9.59%
Worst Month	-8.94%
Average Gain in Up Months	2.74%
Average Loss in Down Months	-2.99%
Annual Volatility	13.11%
Index Volatility	10.76%

Top contributor[8] (bps)

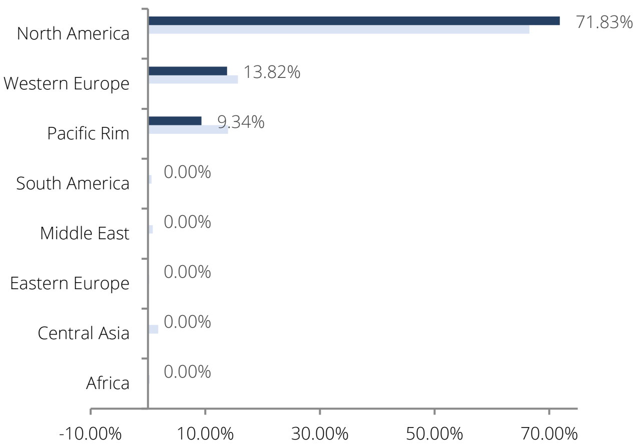
- DigitalBridge 44 bps
- Cienna Corp 42 bps
- Advantest Corp 36 bps

Top detractor[8] (bps)

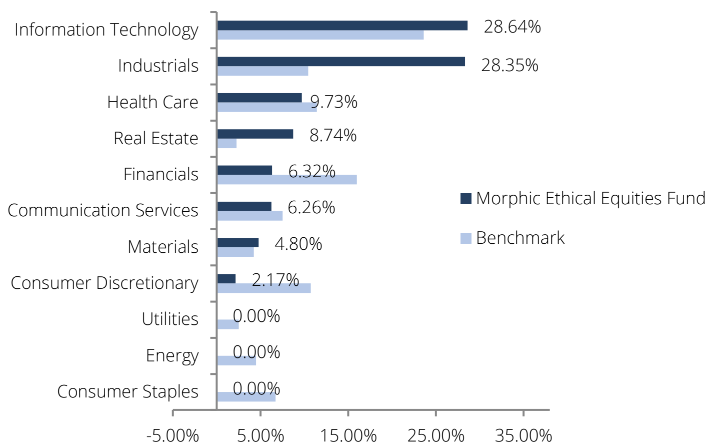
- GDS Holdings -73 bps
- Chart Industries -52 bps
- Soitec -41 bps

Key Facts	
ASX code / share price	MEC / 1.010
Listing Date	3 May 2017
Profit Reserve[9]	$0.484
Management Fee	1.25%
Performance Fee[10]	15%
Market Capitalisation	$47.6m
Shares Outstanding	47,107,860
Dividend per share[11]	$0.14

Equity Exposure Summary[12] By region



Equity Exposure Summary[12] By sector



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[1] Performance is net of investment management fees, before company admin costs and taxes; [2] The Index is the MSCI All Countries World Daily Total Return Net Index (Bloomberg code NDUEACWF) in AUD; [3] The figures are estimated and unaudited; [4] Performance is net of investment management fees, before dividends, company admin costs and taxes. Fund listing on the ASX 3 May 2017. Past performance is not an indication of future performance; [5] Includes Equities and Commodities - longs and shorts are netted; [6] Includes Equities, Commodities and 10 year equivalent Credit and Bonds - longs and shorts are not netted; [7] Based on gross returns since Fund's inception; [8] Contribution; absolute returns against excluding the effect of hedges; [9] The reserve is made up of amounts transferred from current and retained earnings that are preserved for future dividend payments. The payment of franked dividends depends on the rate MEC realises taxable profits and generates franking credits; [10]The Performance Fee is payable annually in respect of MEC's out-performance of the Index. Performance Fees are only payable when MEC achieves positive absolute performance and is subject to a high water mark; [11] Annual dividend per share. [12] Exposure Summary charts do not take into account derivative positions.