CELEBRATING 20 YEARS

BKI INVESTMENT COMPANY LIMITED

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ABN: 89 615 320 262

March 2025

CONTACT ASSET MANAGEMENT

BKI is managed by Contact Asset Management
AFSL 494045

QUARTERLY REPORT

Building Long-Term Value Through Growth Capital & Portfolio Quality

Welcome to the latest edition of the BKI Quarterly Report, prepared by Contact Asset Management ("Contact").

In this quarterly report we reiterate our long-term investment strategy with a particular focus on value creation through growth capital and portfolio quality. We've strategically adjusted our holdings in the Energy sector over the last couple of years and more recently enhanced our defensive positions to reflect evolving market conditions. We discuss key holdings, performance drivers and macroeconomic impacts, emphasising growth through capital expenditure and our commitment to high-quality, dividend-paying stocks.

February Reporting Season – a shift back to quality

February 2025 proved to be a very turbulent month for markets, illustrated by a stark contrast between the RBA's welcome 0.25% interest rate cut and a generally underwhelming reporting season. Geopolitical risks, including the ongoing conflict in Ukraine and tensions created by the US on tariffs, continued to cast a shadow over markets. Investors remained cautious as these risks could potentially disrupt global supply chains and economic activity.

The S&P/ASX 300 Accumulation Index declined by 3.8% in February, with the IT sector experiencing a huge pullback, falling 12.3%. The market fall reflected concerns over missed earnings expectations, as rising operating costs, higher cost of debt and wage pressures squeezed margins. This pressure saw many firms with declining earnings and stretched balance sheets forced to cut dividends.

Despite the overall market decline, a notable shift occurred during the month as investors focused back on quality. Companies demonstrating robust earnings, strong balance sheets and a clear long-term growth trajectory were rewarded. This "flight to quality" has been welcomed following a period of momentum investing with much of the market overlooking fundamental analysis. BKI's Portfolio Return, including franking credits, was -0.8% for the month, outperforming the index with several companies delivering standout results, highlighting the benefits of positive strategic long-term investing.

BKI's Core Strategy – Blocking out volatility, trend and momentum investing

BKI invests for the long-term in high-quality Australian companies with a track record of growing dividends. Contact manages this portfolio with a focus on cost efficiency, seeking to provide BKI shareholders with a steadily increasing income stream through fully franked dividends alongside long-term capital appreciation. Our research-driven, long-term approach targets profitable companies that prioritise shareholder returns. We like to see quality companies re-invest in their business for future earnings growth and not stand still to be swallowed up by changing market dynamics.

Our strategy has remained effective for decades, navigating various market conditions, trends and momentum investing. The recent reporting season underscored the value of this approach, with a renewed market focus on quality companies that reinvest, maintain strong balance sheets and deliver consistent profits and dividends.

Several companies, including Woodside Energy and APA Group, exemplified the benefits of strategic long-term investing, reporting increased earnings and dividends driven by sustained capital expenditure. Other notable performers, such as Commonwealth Bank, TPG Telecom, Sonic Healthcare, ARB Corporation and Coles Group, delivered positive results underpinned by capable management and long-term investment strategies.

What Constitutes Portfolio Quality?

To clarify what constitutes "portfolio quality", we thought it best to revisit our investment process. Contact Asset Management is a research-driven, active equities manager. We invest the BKI portfolio in long-term, profitable, high yielding, well managed companies. Stock selection is bottom-up, focusing on the merits of individual companies rather than market and economic trends.

Contact is focused on investing in stocks for the BKI portfolio using the 6 basic fundamentals below as part of the stock selection process:

1. Principal Activity - Sustainable Business Model, Competitive Advantage
2. Income - Dividend Yields, Franking Credits, Pay Out Ratios
3. Financial Strength – Net Cash or Low Debt Levels, Gearing and Coverage Ratios
4. Management – Strong Alignment, Experience and Skillset, Creating Shareholder Wealth
5. ESG – Positive Environmental and Social Aspects, Good Corporate Governance
6. Valuation – Growing Earnings, Attractive Valuations and Multiples

Companies meeting these criteria are deemed to qualify for inclusion within the BKI portfolio, ensuring its high quality.

Growth Capital

Despite being a generally underwhelming reporting season, there were several companies who delivered standout results during February. This highlighted the benefits of positive strategic long-term investing. Woodside Energy and APA Group, for example, reaped the rewards of significant capital expenditure over many years. Both companies reported increased earnings and cashflows, resulting in higher dividends paid to their shareholders. Other notable results included Commonwealth Bank, Telstra, TPG Telecom, Sonic Healthcare, ARB Corporation, and Coles Group. These companies delivered positive results that were underpinned by capable management teams focusing on long term investment strategies.

Woodside Energy - WDS

WDS significantly diversified its global portfolio following its merger with BHP's petroleum business, which now encompasses oil and gas assets across Australia, the Gulf of Mexico, the Caribbean, Senegal and Timor. WDS has demonstrated its commitment to future growth by reinvesting through a substantial exploration program and successfully delivering major projects. Notably, the Sangomar oil development in Senegal achieved first oil production in June 2024. This project, with a $5 billion development cost, rapidly reached nameplate capacity within nine weeks, achieving 94% reliability in Q4 2024, and generated $950 million in revenue from 16.2 MMboe production within six months.

WDS is actively progressing other major growth initiatives, including the $12.5 billion Scarborough LNG project, now 80% complete and on track for 2026 delivery, and the $7.2 billion Trion development, expected to produce in 2028. Strategic sell-downs in the Scarborough project have strengthened the balance sheet with $2.3 billion in cash proceeds and secured long-term LNG sales agreements for over 15Mt. Furthermore, WDS has expanded its LNG presence through an acquisition in Louisiana LNG and entered the lower-carbon ammonia market with an investment in Beaumont New Ammonia, aiming for 2025 ammonia production.

These generational projects, requiring substantial capital, are expected to deliver significant long-term returns, supporting WDS's attractive dividend yield. Given the significant amount of cash being generated from both current and future development assets, we have been comfortable adding to the WDS position for BKI over the last couple of years.

APA Group - APA

APA has announced strong financial results with significant growth in earnings, cash flow and distributions. Revenue rose by 7.1% to $1,364 million and EBITDA grew by 9.1% to $1,015 million, driven by newly acquired asset performance, increased customer demand for seasonal gas transmission capacity, inflation-linked tariff increases, effective cost management and contributions from its strategic long-term investment in the Pilbara Energy System. APA's Pilbara Energy System, including the Port Hedland Power Station, Newman Power Station, and Chichester Solar Farm, plays a crucial role in powering the region's mining operations. Further long-term investment by APA will deliver critical infrastructure projects to meet the Pilbara's growing energy demands, integrating gas pipelines and renewable energy for reliable and sustainable power solutions.

APA continued strategic investment in growth projects, with $339 million in capital investment during the first half of FY2025. This included the completion of the Port Hedland Solar and Battery project, the Kurri Kurri lateral pipeline project and the initiation of East Coast Gas Grid expansion projects. APA also progressed future growth projects, including the Sturt Plateau Pipeline Development Agreement, electricity transmission corridor development in WA and the announcement of its five-year East Coast Gas Grid Expansion Plan.

APA's Free Cash Flow reached $552 million, a 3.6% increase, enabling an Interim Distribution of 27.0cps to be paid. APA's updated Final Distribution guidance for FY2025 also aligns with our expectations of 30cps. These increases in distribution demonstrate management's execution of long-term strategic growth projects, ensuring shareholder wealth creation. APA remains BKI's most active position with a portfolio weight of 4.9%, which is an overweight position of 4.5% compared to an index weight of 0.4%.

Commonwealth Bank – CBA

In the half-year ended 31 December 2024, CBA increased its investment spending by 11% to $1.1 billion, up from $988 million in the prior period. This investment was allocated across key areas, including productivity and growth initiatives at $489 million, risk and compliance projects at $333 million and infrastructure and branch refurbishment at $274 million. Years of capex has enhanced CBA's digital capabilities, streamlined banking processes, strengthened risk management and modernized technology and infrastructure. As a result, CBA now leads the market in consumer mobile apps and digital offerings, with 8.8 million active app users and 12.3 million daily logins. Building on its significant digital investments, CBA allocated over $800 million in 2024 to protect clients against fraud, scams, financial and cybercrime, with a further $450 million invested in the first half of FY2025. CBA's consistent, disciplined capital management strategy and ongoing investment have driven growth and scale, leading to superior and sustainable shareholder returns over the long term.

TPG Telecom - TPG

Over the past five years TPG has made substantial capital investments focusing on both infrastructure and spectrum. Excluding spectrum costs their cash capital expenditure reached $2.2 billion over the last two years alone. After many years of investment, projected annual expenditures for TPG are much lower with $900 million expected in 2025 and $500-650 million from 2027 onwards. TPG also anticipates a $100 million reduction in operating costs following the sale of their fibre and EGW fixed assets. Since 2019 they have invested $586 million in spectrum and in January 2025 TPG activated a major regional network sharing agreement with Optus, significantly expanding their mobile network coverage to over 1 million sq/km now reaching 98.4% of the Australian population. This expansion coupled with their extensive mobile network of over 5,700 sites has solidified TPG's position as Australia's second-largest fixed voice and data network.

Sonic Healthcare – SHL

Over the last few years, SHL has expanded its footprint through several acquisitions in Germany, Switzerland and the USA. In February 2025, SHL received unconditional investment clearances to acquire German Laboratory Group Dr. Kramer & Colleagues, with the transaction expected to settle on 1 July 2025. SHL also made capital investments of $170 million in 2024 and $224 million in 2023 and purchase of controlled entities and investments of $35 million in 2024 and $884 million in 2023. SHL has grown to now become one of the world's leading healthcare providers with locations in Australia, New Zealand, United States, United Kingdom, Germany, Switzerland, Belgium and Ireland. It has grown into the largest medical laboratory provider in Australasia and in Europe and is the third largest in the US. From its first dividend payment of 2cps back in 1994, SHL's consistent organic growth and acquisition strategy saw it declare a record interim dividend in February of 44cps, adding to SHL amazing 30-year track record of never cutting its full year dividend.

ARB Corporation – ARB

ARB has an exceptional track record of investing for the future and the first half of FY2025 was no different. ARB has continued its focus on strategic investments to enhance long-term growth, allocating a further $25 million to increase its ownership in ORW USA, Inc. from 30% to 50% and facilitating the acquisition of US 4WD distributer 4WP. Additionally, ARB expanded its Australian Aftermarket footprint by acquiring retail stores and MITS Alloy, a manufacturing business, for a total of $13.3 million. The company also invested $23.7 million in property, plant, and equipment to support ongoing operations and expansion. ARB currently has 75 ARB stores across Australia and will deliver a further 5 independent flagship stores in 2H FY2025. In addition, they deliver product to over 100 countries worldwide. This expansive distribution network is the result of sustained investment, strategic planning and a forward-thinking management team dedicated to long-term shareholder value.

Coles Group - COL

Over the past five years, Coles has invested over $6 billion in capital expenditure, primarily focused on modernizing its supply chain through the rollout of automated distribution centres (ADCs) and customer fulfillment centres (CFCs). This strategic, long-term investment in technology-driven innovation has significantly improved efficiency, sustainability, and safety within their distribution network, achieving a 99% fulfillment rate and expanding the product range by 25% compared to a typical Coles store. Notably, Coles eCommerce continues to demonstrate strong performance, reporting sales growth of 22.6% in the first half of FY2025.

Conclusion

The recent reporting season highlighted the value of investing in quality companies. Those companies who are consistent in reinvestment and can demonstrate a commitment to growth across all market cycles. This reinforces BKI's strategy of building a portfolio of high-quality, long-term investments, which has proven effective in navigating market volatility. BKI, through Contact's research-driven approach, focuses on fundamentally strong, dividend-paying companies. This has enabled BKI to perform strongly in a market full of macroeconomic uncertainties. The success of key holdings, including Woodside Energy, APA Group and others, highlights the importance of strategic capital expenditure and effective management. BKI's long-term investment philosophy, characterised by patience and support for strong management teams that prioritize reinvestment, ensures sustained shareholder value and consistent dividend growth.