Canavan Capital Partners

Monthly Investor Report

Canavan Capital Partners Australian Share Fund | Month ended 31 October 2026

FUND RETURN, NET	S&P/ASX 300 TR (REFERENCE)	PERFORMANCE HURDLE	INVESTED / CASH
1.56%	**1.11%**	**0.80%**	**45% / 55%**

October Performance

The Canavan Capital Partners Australian Share Fund increased 1.56% in October.

In the two months since inception, the Fund is up 1.28%.

Following the RBA's rate rise on 29 September, the monthly performance hurdle increased to 0.80%. As a reminder, the Fund's performance hurdle is the RBA cash rate plus 5% a year.

October was a very volatile month at the stock level; however, at the index level, markets held up well, with the ASX 300 total return index up 1.11%.

This was largely because the banks, which carry a heavy index weighting, offset the weakness in resources. For example, the ASX 300 metals and mining index fell 7% for the month while the ASX 200 banks index surged 10%.

Monthly volatility is interesting, sometimes useful, and often scary. It was useful for us this month in that it provided some opportunities to continue to deploy our cash at what I think will prove to be good long-term prices.

We added another four positions to the portfolio in October, and now hold a total of 15. At the end of the month, the portfolio was 45% invested, with 55% in cash. Given we are still building a position in these four new companies, I won't disclose their names in this update. But you will likely hear about them in future reports.

It was pleasing to see the portfolio perform well with such a large cash weighting. The key contributors were those companies that we bought during the panic in September, which bounced back in October.

This is just the result of prices moving around from one month to the next. Value takes longer to accrue. But as you will see, we are accumulating a good bunch of businesses generating attractive returns on tangible capital at what I consider to be discounts to their intrinsic value.

Volatility during October was extreme at the smaller end of the market and particularly prevalent in the resources sector.

Thankfully, we had no exposure to small cap resources or gold stocks. That may change in the future, depending on valuation and sentiment.

To remind you, the Fund is an all-cap fund and sector-agnostic. It will invest in large caps, small caps or microcaps, depending on valuations, profitability and expected returns. I believe this flexibility is a big advantage in a market where capital moves with increasingly short-term time horizons.

When you buy with valuation as a key discipline, volatility is something to take advantage of, not something to stress about.

Read on below for a look at how the portfolio is shaping up, and for a discussion about the broader market and investment environment.

Fund / index / benchmark	October	Basis
Canavan Capital Partners Australian Share Fund	1.56%	Fund return, net of fees
S&P/ASX 300 Total Return Index	1.11%	Reference only; not the performance benchmark
RBA cash rate + 5% p.a. (performance hurdle)	0.80%	Fund performance benchmark, as a monthly hurdle

Since Inception

Fund / index / benchmark	Since inception	Basis
Canavan Capital Partners Australian Share Fund	1.28%	Fund return, net of fees
S&P/ASX 300 Total Return Index	-1.32%	Reference only; not the performance benchmark
RBA cash rate + 5% p.a. (performance hurdle)	1.58%	Fund performance benchmark

Commentary – Staying mentally flexible in the age of AI

The stock market is a complex adaptive system. That means it is not predictable in any repeatable way, especially over the short term.

This idea first came to prominence back in 1987 when 20 academics across multiple disciplines came together at the Santa Fe Institute to discuss the economy as a complex system.

They concluded that an economy has three defining features: 1. it is a network of agents acting in parallel; 2. control is widely dispersed; and 3. agents adapt to a changing environment as they gain knowledge and experience.

Over time, researchers applied this seminal work to financial markets.

The upshot is that no one can predict markets with any degree of certainty, especially when it comes to shorter time horizons. Millions of people are all acting in parallel, making variable decisions based on a constantly changing environment.

There are times when stock market participants are all in agreement and things appear certain. For example, ‘everyone’ knows that AI is a transformative technology and will change the world.

The problem with certainty is that it comes with higher valuations. Value doesn’t live where there is certainty.

The AI trade was a certainty for a long time.

But recently, that has changed. The tech sector is under pressure and uncertainty is increasing. Is the AI bubble bursting? Will all the capex pay off? Is compute just a commodity where returns will be competed away down to marginal cost?

I don't know the answer to that. Nor do most people. But that hasn't stopped everyone having an opinion. And most opinions right now are bearish. Comparisons to 2000, 2008, and even 1929 are commonplace.

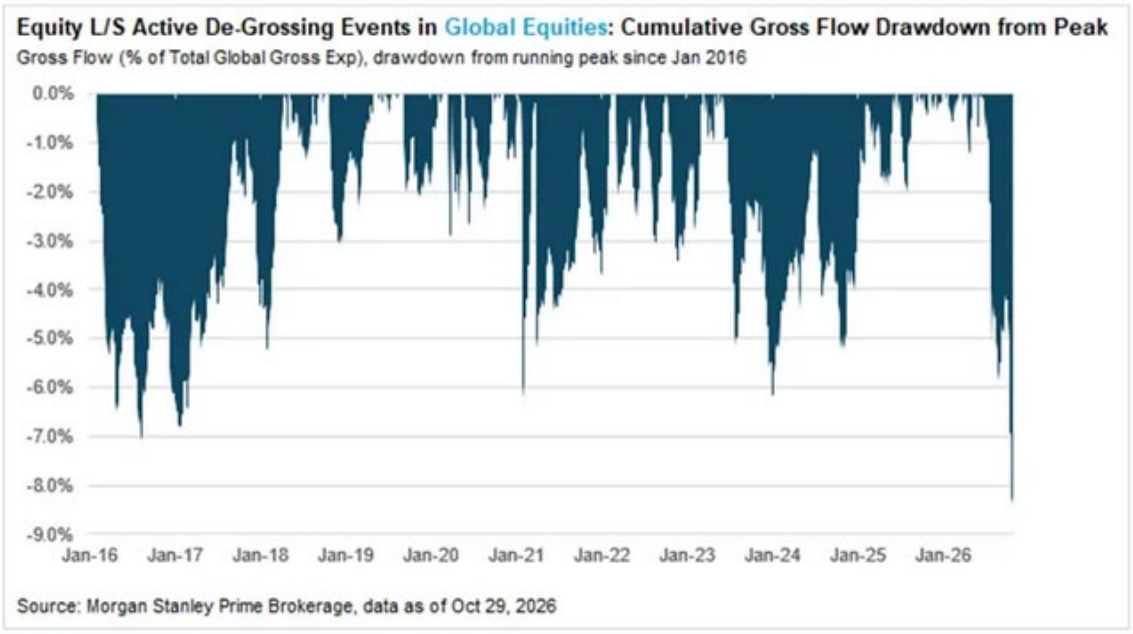
When a bubble starts to burst, what you want to see (if you're a bear) is denial and ongoing bullishness.

It doesn't feel like that is happening here. I recognise that, in this day and age, when algorithms curate your newsflow, you can get wall-to-wall bullishness or bearishness depending on your bias.

But I try to be reasonably balanced in my reading and listening. And in my view, the bears represent consensus thinking more than the bulls right now.

And that's translated into market positioning too.

According to Morgan Stanley Prime Brokerage data, October saw the biggest hedge fund de-grossing event in 10 years. In other words, hedge funds aggressively cut their exposure, selling longs and covering shorts.



Source: Macrocharts, Morgan Stanley Prime Brokerage

With the bearish narrative dominant, it makes me think: what could the bears be missing?

Maybe this is just another scary correction in the long AI build-out?

AI is often compared to the railway boom. That took decades to play out and involved a number of booms and busts. It wasn't one event like the dot-com bubble or the credit crisis.

Everyone likes to find a historical analogue to help them make sense of a complex adaptive system that defies prediction. 'This is like the dot-com bubble', or 'this is like the 1970s' is a common refrain.

But the reality is, this is not like anything we've seen before. No two booms and busts are alike. This time is always different. History says booms end in busts. But it doesn't say when and from what point.

This is why I think it's important to understand that we're operating in a complex adaptive system. We cannot know what happens next week, next month, or next year. Thinking you do know how things will play out will only wear down your mental capital, as you get predictably buffeted by being wrong.

In *Thinking, Fast and Slow*, Daniel Kahneman wrote:

> '*Subjective confidence in a judgement is not a reasoned evaluation of the probability that this judgement is correct. Confidence is a feeling, which reflects the coherence of the information and the cognitive ease of processing it. It is wise to take admissions of uncertainty seriously, but declarations of high confidence mainly tell you that an individual has constructed a coherent story in his mind, not necessarily that the story is true*.'

A coherent story makes us feel good, because it helps us deal with uncertainty. But it's just a story, constructed by our own mental biases.

Here are two coherent stories about the AI boom. One is bearish, the other bullish. Investors usually hold onto one or the other, depending on their bias. The better option, to preserve mental capital, is to hold onto both.

The bearish story is that all the capital expenditure on data centres will turn US tech companies from capital-light to capital-intensive businesses. Depreciation and reinvestment will erode profitability and cashflows.

As a result, these businesses will trade on lower earnings multiples because returns on capital will be lower. In addition, Chinese open-source models will be cheaper to use than those from OpenAI and Anthropic, and will undermine their returns.

When everyone wakes up to this, the boom turns to bust.

The bullish story is that AI is one of the most transformative technological revolutions in human history. We are still in the very early stages of its development. It will go on for decades. The massive capex programs will generate a substantial return because the capital invested *will replace human capital*.

That's not a pleasant thought. But the use of agents (agentic AI) has only just started. And so have the job losses. An hour of GPU compute costs less than the minimum wage. Having an AI agent complete a task often costs a fraction of what you'd pay a person to do it.

If this bullish view is the one that plays out, it has huge implications for markets. The top might still be a few years away.

Given these opposing views, and the plausibility of each one, it's very important to maintain mental flexibility in this defining age of AI. Taking a 'side' will only make it harder to see the opposing view play out if you're wrong.

I say all this despite not being a direct investor in AI stocks. But that doesn't matter. The bull or bear case will have major ramifications for all capital markets and investors in different stocks and sectors in the US and Australia.

The key takeaway is to not bet on an outcome.

But we don't need to. The simple beauty of our investment process is that we aim to buy companies when uncertainty and fear are high or when there is complete disinterest in a stock or sector. Of course, these situations must coincide with valuation support.

Times of fear and uncertainty usually provide more favourable investing situations. As Buffett wrote in a 1979 *Forbes* article:

'*The future is never clear; you pay a very high price in the stock market for a cheery consensus. Uncertainty actually is the friend of the buyer of long-term values.*'

There has certainly been an increase in uncertainty over the past few months. As you'll see below, it has allowed us to enter positions in some quality companies that produce strong cashflow.

But it has mostly resulted in heavy selling at the more speculative end of the market. This is an area I avoid.

So how is the portfolio positioned?

Let's have a look…

Portfolio positioning

As mentioned, we added four new positions to the portfolio in October. At the end of the month, the portfolio was 45% invested in 15 companies, with 55% in cash.

Most of the companies we own are not yet 'full positions'. We have bought into these companies during sell-offs or after extended downtrends. There is strong valuation support, but sentiment and trend usually win out over valuation in the short term.

So I am building a position over time, rather than allocating all at once. Many of these companies are a work in progress.

The top three performers for the Fund in October were **WiseTech Global [ASX:WTC]**, **Hansen Technologies [ASX:HSN]** and **ResMed [ASX:RMD]**.

We bought into WTC and HSN during the September sell-off.

HSN was a simple case of taking advantage of the market's short-termism. At its annual results announcement, it said that FY27 would be an investment and transition year. The algos and short-term investors dumped it, creating a value opportunity.

HSN is a high-return, strong-cashflow business with minimal debt, trading around 12 times FY28 consensus estimates. For a business that reinvests around 60% of its earnings, and one that I estimate will generate a 28% return on tangible capital in FY28, this is an attractive valuation.

WTC sold off after its results too, giving us an opportunity to build a position. The stock is down around 80% from its high reached two years ago.

WTC is a near monopoly provider of the core software operating systems that run the world's largest logistics companies. It's a great business. The problem has always been around valuation.

But the valuation bubble has unwound over the past two years, helped by concerns around corporate governance.

WTC guided to a weaker first half of FY27, which is why the stock sold off after the results. More market short-termism.

An ASIC investigation into share trading by founder Richard White and two other employees concluded in October with no further action, which helped boost the share price.

After a near 35% rally from the lows, the share price is not as compelling as it was in September. But if the business can keep delivering, it will continue to be a core long-term holding in the Fund.

RMD is another high-return, strong-cashflow business with minimal debt and very good long-term growth prospects. We bought during September weakness and recently added when it plunged around 10% despite delivering a healthy set of quarterly results.

The main detractors from the Fund in October were **Mader Group [ASX:MAD]** and **GQG Partners [ASX:GQG]**.

We bought into MAD during the early September sell-off. The stock bounced a little, before falling sharply on news that the CFO, Paul Hegarty, had stepped down from the role. The market never likes a CFO leaving abruptly, but the intra-day move lower of nearly 20% seemed overdone and we added on the sell-off.

MAD trades on undemanding PEs of 16.5 times FY27 and 14.4 times FY28 consensus earnings. I estimate it can generate a sustainable return on tangible capital of around 28%. It pays no dividend, reinvests its earnings, and currently has a $30 million buyback in place.

We also bought into GQG during the September sell-off. It has continued to decline on the back of the weakness in tech and its well-publicised change in stance on the AI boom/bubble. I've noticed on the social media platform X that GQG is the subject of much ridicule.

In general, people don't take kindly to mental flexibility, especially when it looks like you've got it wrong in the short term. However, I believe such flexibility is a valuable attribute in a money manager (as opposed to stubbornness) and GQG shouldn't be written off too early.

In my view, the current share price of around 90 cents is pricing in a very grim outlook for the business. Consensus earnings per share estimates for FY28 are US11 cents, down 30% from the 2025 peak. At an exchange rate of 70 US cents to the Australian dollar, that equates to 15.7 cents, or a PE of 5.7 times.

That's a 17.5% earnings yield. So the market clearly expects GQG's earnings to fall well short of consensus.

On my estimates, a 90 cent share price implies funds under management (FUM) of somewhere between US$100 billion and US$110 billion. FUM at the end of September was US$149.2 billion, so the market appears to be implicitly pricing in a further 26–33% decline in FUM.

Poor October investment performance (thanks to the AI sell-off) and more outflows will no doubt see October FUM decline when the data is released in November.

It will be important to watch the share price reaction on this release.

We only have a small position, but this is a potentially compelling opportunity to add and build a more meaningful stake in the months to come.

There is a lot of uncertainty around GQG right now. This is where potential value lives.

I'm also seeing potential value in the coal stocks. In September we initiated positions in **Yancoal [ASX:YAL]** and **Whitehaven Coal [ASX:WHC]**. At current coal prices, these companies are generating significant free cashflow.

However, the market is yet to reward them. Coal stocks generally remain unloved and overlooked by the market. That's especially the case for WHC and YAL.

The graphic below shows the price-to-book multiples these businesses trade on. WHC trades around 1.07 times book value and YAL around 0.89 times book. The market's preferred coal exposure right now is **New Hope Corp [ASX:NHC]** (green line), which trades at a price-to-book of around 1.91 times.



Source: TIKR

WHC and YAL are good value relative to NHC, and in my view good value on a standalone basis.

Cash

Cash levels in the portfolio were at 55% at the close of the month. I will continue to add to a number of our existing positions as ongoing volatility will no doubt provide opportunities to do so.

I will only add new positions that fit our process and expected future return profile. With five interest rate rises currently working their way through the Aussie economy (their full impact will hit later in 2027) I anticipate the market will continue to throw up plenty of opportunities for us in the months ahead.

Just remember though, if the market turns bullish, we will lag in the short term. Holding high cash levels is like being underweight the market. It cushions us when the market falls and drags on performance when the market rises. As we head into what is generally a seasonally strong time for equities, that is worth keeping in mind.

As compelling long-term opportunities present themselves, I will invest the cash. But I won't chase short-term market moves.

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