

Portfolio performance

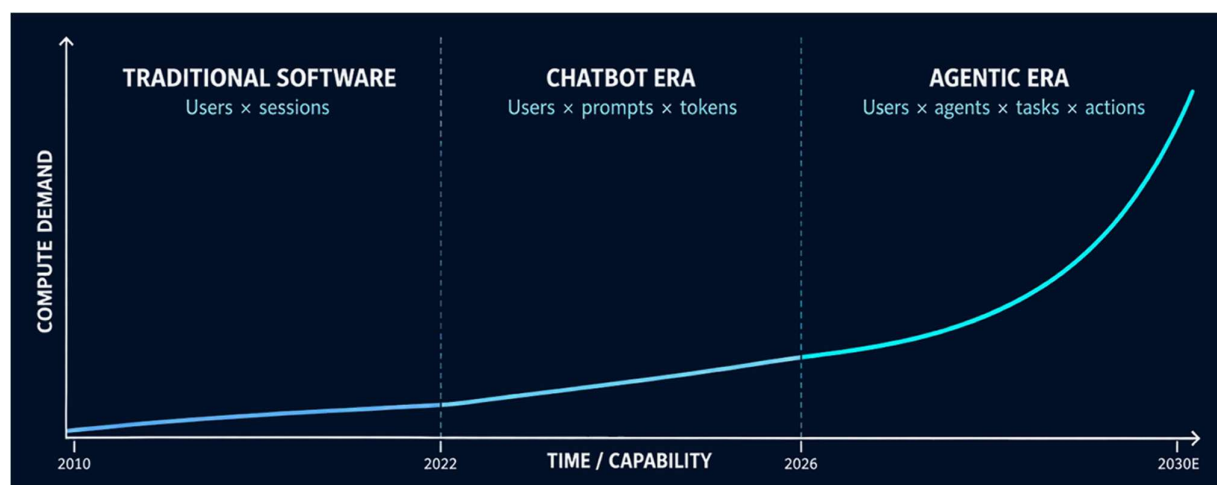
Quarter	1 Year	3 Years (p.a.)	7 Years (p.a.)	10 Years (p.a.)	Inception (p.a.)
9.91%	(0.69%)	13.41%	7.16%	10.81%	10.51%

1. Executive summary

Quarterly return: 9.91%

The September quarter was an important period of portfolio repositioning. We established new positions in Alphabet and Meta and re-established positions in ASML and TSMC, while exiting several holdings where we believed the opportunity cost of continuing to hold them had increased. We also reallocated capital across several existing positions and ended the quarter with a meaningful cash balance.

The most important development during the quarter was a strengthening of our view around the transition from generative AI to agentic AI. Until recently, much of the discussion around artificial intelligence has centred on chatbots: a user asks a question and receives a response. The next phase will be materially different. AI agents will be capable of reasoning through tasks, accessing data, calling software, interacting with other agents and executing actions on a user's behalf.



Salesforce provided one of the clearest examples we have seen of this transition moving into real-world production. During its most recent quarter, Salesforce reported that Agentic Work Units, which measure discrete tasks completed by AI agents in production, increased 97% sequentially to 3.2 billion.

That was significant to us because it suggested that AI is beginning to move from experimentation toward doing actual work. As illustrated above, the transition from traditional software to chatbots and now to agents materially changes the relationship between users and compute. A chatbot generally responds to a prompt; an agent can undertake multiple tasks and actions in pursuit of a single objective. This led us to reassess the likely duration and scale of the infrastructure required to support it. Rather than thinking about AI infrastructure primarily as a large but finite build-out, we now see a much longer-duration increase in computing intensity.

2. Portfolio positioning

The changes made during the quarter reflect an evolution in how we are positioning the portfolio around this opportunity.

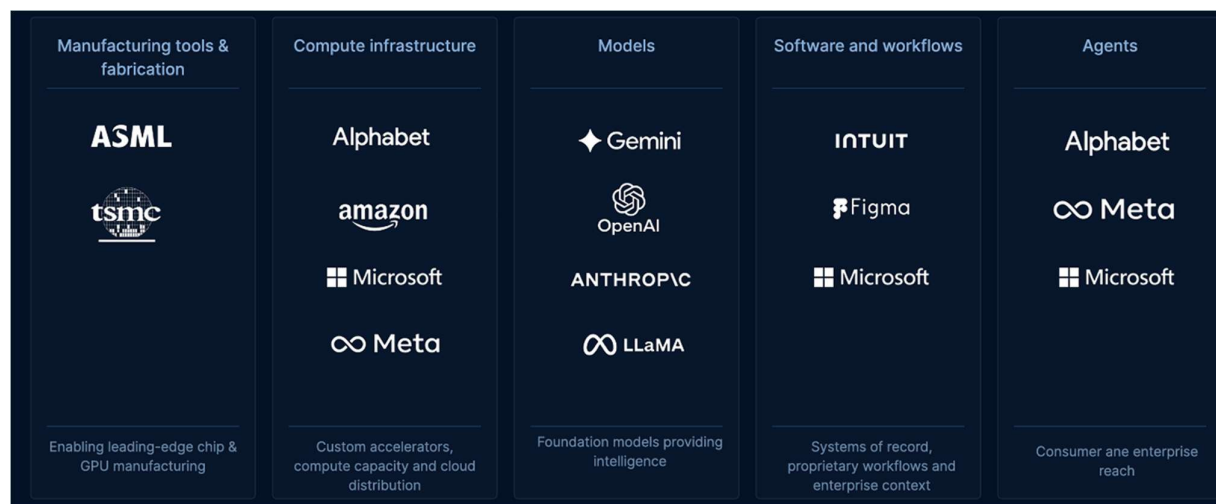
The first change was evidence. As agentic AI began to move into real production workflows, we revisited some earlier assumptions about where the most attractive opportunities sat across the value chain. We had previously reduced our exposure to ASML and TSMC because we believed valuations had begun to reflect a substantial amount of future AI demand. As the evidence around agentic adoption strengthened, we concluded that the opportunity remained sufficiently large and durable to justify re-establishing those positions.

The second change was a stronger preference for companies with multiple ways to win. Amazon, Microsoft and Alphabet are not dependent on a single AI outcome. They can benefit from higher cloud demand, proprietary silicon, first-party models, enterprise software and distribution. If AI infrastructure demand remains strong, they participate directly. If capital spending moderates, lower capital intensity can support free cash flow. If third-party models become commoditised, they retain the ability to invest behind their own products and platforms. We increasingly value this optionality.

The third change was a greater emphasis on structural rather than idiosyncratic growth. Many excellent businesses remain dependent on product cycles, consumer demand or execution within relatively narrow markets. By contrast, businesses such as ASML and TSMC sit behind broad secular increases in semiconductor intensity, while the hyperscalers sit behind rising demand for compute. We believe these underlying demand drivers are easier to underwrite over a five- to ten-year horizon.

Finally, we have been deliberate about how we express this view. We do not invest in themes; we invest in businesses that are driving structural change and strengthening their competitive positions because of it. That was true of our investments in Visa and Mastercard as payments moved from cash to digital, and it is the same approach we are taking with AI. Rather than seeking the most speculative beneficiaries of the build-out, we have concentrated on businesses that sit at critical points in the ecosystem and have the scale, balance sheets and competitive advantages to capture value as the transition unfolds.

How the portfolio is positioned across the AI value chain



- At the semiconductor manufacturing layer, ASML provides the lithography equipment required to manufacture the world's most advanced chips and is the sole commercial supplier of EUV lithography systems. TSMC is the world's leading advanced semiconductor foundry, with a dominant position in leading edge process nodes.
- At the compute layer, Amazon, Microsoft and Alphabet operate three of the world's largest cloud platforms. Increasingly, these companies are also developing their own processors, networking, software and AI systems, while maintaining exposure to leading foundation models through their own development efforts and strategic partnerships.
- At the application layer, we own businesses such as Figma and Microsoft that are positioned for an agentic world. Both are embedding AI more deeply into existing workflows, with Figma extending from design into code and agent-driven creation, and Microsoft integrating agents across productivity, development and enterprise software. We believe software platforms that already own workflow, context and permissions will be more valuable as agents increasingly perform work on behalf of users.
- At the distribution layer, Alphabet and Meta possess assets that are extraordinarily difficult to recreate. Alphabet has 13 products with more than one billion users, including five with more than three billion users, while Meta reported that approximately 3.6 billion people use at least one of its family of apps each day. We believe this distribution will become more valuable in an agentic world. Companies that already own the consumer relationship, identity, data, payments, communications or workflow layer will be best positioned to become the interface through which personal and enterprise agents operate.

3. Investment developments

One of the most interesting developments during the quarter was the increasing strategic importance of proprietary silicon at Amazon and Alphabet. For many years, the major cloud platforms relied predominantly on third-party processors. That is changing.

Amazon has built a substantial semiconductor capability through Annapurna Labs, including Graviton CPUs and Trainium/Inferentia AI accelerators. Management stated during the quarter that Amazon's chip business had grown to more than US\$25 billion of annual revenue run-rate. It has also said that if its custom silicon business were treated as a standalone company selling chips to AWS and external customers, it would represent approximately US\$50 billion of annual revenue run-rate. Amazon has disclosed more than US\$225 billion of revenue commitments for Trainium, including large multi-year commitments from Anthropic and OpenAI. Management is also considering selling Trainium independently of AWS because external demand has become sufficiently significant.

Alphabet has been developing TPUs¹ for approximately a decade and is now on its eighth generation. Its latest TPU architecture separates chips optimised for training from those designed for inference. Google has stated that its custom AI chip business is approximately twice the size of the next-largest cloud competitor's. We think these developments are strategically important for several reasons.

- First, custom silicon reduces dependence on a single external supplier.
- Second, it allows the hyperscalers to retain economics that would otherwise accrue to third-party chip vendors.
- Third, vertically integrating chips, networking, data centres, software and models may allow them to optimise the entire system rather than individual components.

This will become more important as inference becomes the dominant AI workload over time. In a world where billions of agents are operating continuously, the ability to deliver compute at lower cost will be a major competitive advantage. We therefore increasingly view Amazon and Alphabet not simply as cloud companies purchasing enormous quantities of AI infrastructure, but as vertically integrated computing companies developing significant intellectual property at almost every layer of the stack.

Another important development is the increasing evidence that agentic AI is moving from pilot programs toward production. Salesforce's Agentic Work Units are one example, but the broader trend is visible across enterprise software, with companies such as ServiceNow, Workday, SAP and Intuit increasingly embedding agents into their platforms. The important point is not that every current agent will succeed. Rather, it is that the software industry is beginning to reorganise around the idea that agents will increasingly perform work inside existing systems. That has important implications for cloud demand, data infrastructure and the value of software platforms that can provide agents with context, identity, permissions and workflow access.

4. Risk and capital preservation

AI infrastructure is becoming increasingly critical to the future of computing. The scale of investment required to support that transition is substantial, with several trillion dollars of additional capital expected to be deployed into AI and data-centre infrastructure through the end of the decade. We believe this creates a significant long-term opportunity, although the path will not necessarily be linear.

This is one reason we have preferred the hyperscalers over more narrowly exposed AI infrastructure businesses. Amazon, Microsoft and Alphabet have substantial existing cash flows, strong balance sheets and multiple ways to deploy their infrastructure. If AI demand remains strong, they benefit directly. If the pace of infrastructure spending moderates, capital intensity can fall and free cash flow can improve. They also retain the ability to redirect investment toward first-party products and applications. We believe this creates a more resilient way to participate in the opportunity. We believe this creates a significant long-term opportunity, but the path will not necessarily be linear. Our preference is therefore to own financially strong businesses that can benefit across a range of AI adoption and infrastructure spending outcomes.

The portfolio also ended the quarter with a meaningful cash balance. We do not regard this as a forecast about markets. Rather, it reflects our view that this is a sensible time to preserve optionality. There is considerable enthusiasm surrounding AI and valuations in parts of the market are elevated. As our long-term thesis plays out, we expect the path to be uneven. Cash gives us the ability to respond when volatility creates attractive opportunities.

We also continue to regard Intercontinental Exchange (ICE) as an important stabilising component of the portfolio. ICE is much broader than an exchange business. It combines exchanges, fixed-income data and analytics, network

¹ A TPU (Tensor Processing Unit) is a type of ASIC, or application-specific integrated circuit, designed for particular workloads. One way to think about the difference is that a GPU, such as NVIDIA's, is like a decathlete: highly capable across many events, while an ASIC is more like a specialist athlete optimised for a narrower task. Google's TPUs and Amazon's Trainium chips are examples of ASICs designed specifically for AI workloads.

infrastructure and mortgage technology. Approximately 49% of revenue is recurring, while the transaction-based portion is diversified across areas including energy futures, financial futures, options, equities and fixed income.

This creates an attractive economic mix. Some parts of ICE resemble recurring infrastructure businesses, while other areas can benefit from higher volatility and market activity. We therefore think the combination of a meaningful cash position and a substantial holding in ICE provides a useful counterweight to the portfolio's higher-growth technology exposure.

Our objective is not to eliminate short-term volatility. An equity portfolio will inevitably experience periods of significant fluctuation. Our focus is instead on avoiding permanent impairment of capital and retaining the ability to invest aggressively when the risk-reward becomes attractive.

5. Long term perspective

The transition toward agentic AI is a structural trend rather than a short-lived investment cycle. As AI systems move from responding to users toward performing more work autonomously, we expect computing intensity to increase materially across both enterprise and consumer applications. The important point for us is not simply that AI usage grows, but that a greater share of economic activity may increasingly involve software systems reasoning, acting and interacting on behalf of users.

We also do not believe the opportunity ends with software agents. The same advances in models, compute and inference economics are likely to enable subsequent technology waves, including autonomous vehicles, robotics and other forms of physical AI.

We do not expect this progression to occur linearly. There will be periods of overinvestment, technological disappointment and market volatility. But the underlying direction is increasingly clear: software is moving from assisting humans to performing more work autonomously, and over time intelligence is likely to move beyond software into vehicles, machines and robotics. For that reason, our preference is to own businesses that do not require us to predict the precise application, model or architecture that ultimately wins, but that occupy critical and difficult-to-replicate positions within the broader ecosystem.

Our objective is therefore not to predict every technological outcome correctly. It is to own businesses that remain valuable across a wide range of outcomes and become more valuable if our broad view of the future proves correct.

6. Closing remarks

The September quarter reinforced an important principle in our investment process: we must be willing to revisit previous conclusions when the evidence changes. Selling a company does not mean we can never own it again, just as owning a company does not mean we are committed to it indefinitely.

Our job is to continually compare each holding against the best opportunities available to us. During the quarter, we acted on that view by reallocating capital toward businesses where we see stronger structural tailwinds and multiple ways to win, while maintaining meaningful liquidity and a continued focus on downside protection. We acted on that view while maintaining meaningful liquidity and a continued focus on downside protection.

We expect the coming decade to contain considerable volatility and periods when expectations move well ahead of fundamentals. Our approach remains unchanged: to own a small number of exceptional businesses, continually reassess the opportunity cost of every holding, and remain willing to change our minds when the evidence changes.

Location

Level 1, 3142 Surfers Paradise Blvd
Surfers Paradise QLD 4217
Email: info@swellasset.com.au
Telephone: (07) 5551 0299

Disclaimer

This document has been prepared by Swell Asset Management Pty Ltd (ABN 16 168 141 204) ('Swell, 'we' or 'us') a Corporate Authorised Representative of Hughes Funds Management (ABN 42 167 950 236), who is a holder of an Australian Financial Services Licence (AFSL 460572) and is for general information purposes only and is not an offer or solicitation for the purchase or sale of any financial product or service. The material has been prepared for investors who qualify as wholesale clients under sections 761G of the Corporations Act 2001 (Cth) or to any other person who is not required to be given a regulated disclosure document under the Corporations Act. The material is not intended to provide you with financial or tax advice and does not take into account your objectives, financial situation or needs.

Although we believe the material is correct, no warranty of accuracy, reliability or completeness is given, except for liability under statute which cannot be excluded.

Investments involve risk

Please note that past performance may not be indicative of future performance and that no guarantee of performance, the return of capital or a particular rate of return is given.

This material is proprietary to Swell Asset Management. The recipient of this material agrees not to reproduce or distribute this material in whole or in part and not to disclose any of its contents to any other person.