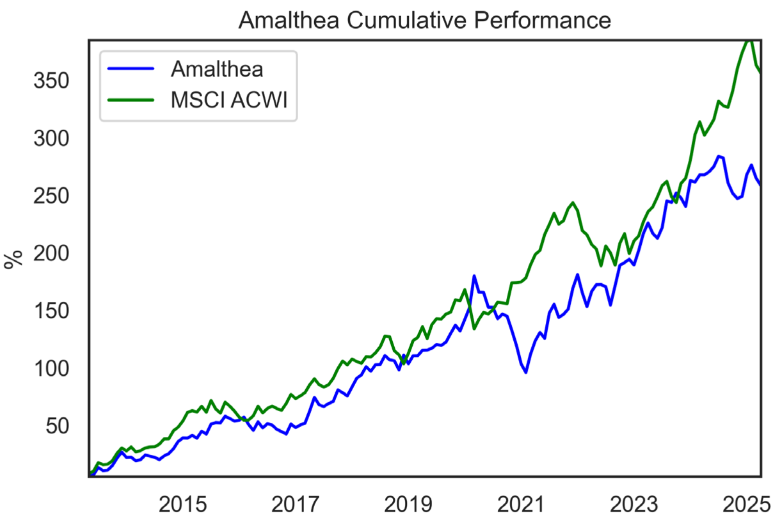
BronteCapital

Amalthea Fund – April 2025

The Bronte Amalthea Fund is a global long/short fund targeting attractive risk adjusted returns over the long term, managed by a performance orientated firm with a process and portfolio that we feel is genuinely different. Objectives include lowering the risk of permanent loss of capital and providing global diversification while reducing the market/drawdown risks typical of long-only funds. We believe a highly diversified short book substantially reduces risk and enables profits to be made in tough markets

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
FY13											5.4%	1.3%	6.8%
FY14	6.0%	-2.5%	0.4%	3.6%	5.7%	4.3%	-3.7%	0.2%	-2.6%	0.9%	3.4%	-0.8%	15.2%
FY15	-0.9%	-1.6%	2.7%	1.7%	3.4%	4.9%	2.3%	-0.1%	1.7%	-1.7%	4.4%	-1.7%	15.6%
FY16	6.1%	0.9%	-0.2%	3.8%	-1.3%	-1.4%	0.5%	1.8%	-4.1%	-3.4%	5.1%	-3.4%	3.8%
FY17	2.5%	-0.8%	-2.5%	-1.3%	-1.5%	6.1%	-2.0%	1.6%	1.0%	7.0%	7.2%	-3.7%	13.6%
FY18	-0.9%	1.5%	1.1%	5.9%	-1.3%	-1.6%	4.4%	4.1%	1.5%	3.7%	-2.0%	2.9%	20.8%
FY19	0.1%	3.8%	-1.8%	-0.4%	-3.9%	6.5%	-3.6%	3.4%	0.0%	2.2%	0.1%	0.7%	7.1%
FY20	1.5%	-0.4%	1.3%	3.4%	3.1%	-2.1%	4.3%	4.2%	11.0%	-5.1%	-0.1%	-4.8%	16.5%
FY21	-0.1%	-3.9%	1.7%	-0.7%	-5.0%	-5.7%	-7.3%	-3.7%	8.2%	5.5%	3.2%	-2.2%	-10.7%
FY22	9.7%	3.0%	-4.5%	1.1%	1.8%	7.3%	4.4%	-5.6%	-4.6%	5.2%	2.2%	0.1%	20.7%
FY23	-0.7%	-5.9%	6.7%	6.5%	0.8%	1.0%	-1.8%	4.3%	4.9%	2.9%	-2.8%	-1.4%	14.7%
FY24	2.9%	7.3%	-0.4%	2.4%	-1.2%	-2.1%	6.6%	-0.3%	1.7%	-0.0%	0.7%	1.2%	20.0%
FY25	2.4%	-0.4%	-5.6%	-2.6%	-1.3%	0.5%	5.4%	2.3%	-3.0%	-1.7%			-4.4%



Amalthea declined by - 1.74% in April compared to -1.50% for the globally diverse MSCI ACWI (in $A). Longs provided the bulk of the winners with European companies DSM Firmenich and Croda being notable alongside Discover Financial Services from USA. Regeneron and Pinterest were less successful. Contributions on the short side came from the materials and consumer discretionary sector but healthcare proved adverse. Overall, the short performance was disappointing. (see over)

Fund Features		*Metric*	*Amalthea*	*MSCI ACWI (in AUD)*
Investment Objective	Maximise risk-adjusted returns over 3-years	Sharpe Ratio[1]	0.77	1.06
Min. initial investment	$100,000 (for qualifying investors)	Sortino Ratio	1.38	1.83
Min additional investment	$50,000	Annualised Standard Deviation	12.34%	10.68%
Applications/redemptions	Monthly	Largest Monthly Loss	-7.30%	-8.00%
Distribution	Annual	Largest Drawdown	-30.01%	-15.97%
Management fee	1.5%	Winning Month Ratio	0.58	0.65
Performance allocation	20%	Cumulative return[2]	258.28%	355.96%
Administrator	Citco Fund Services	1-year annualised return	-2.50%	13.45%
Auditor	Ernst & Young	3-year annualised return	10.41%	14.09%
Custodians/PBs	Fidelity, Morgan Stanley, JP Morgan	5-year annualised return	6.18%	13.52%
		Annual return since inception	11.22%	13.48%

[1] *Sharpe and Sortino ratios assume the Australian cash rate as the applicable risk-free rate*
[2] *Returns are net of all fees*

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The fund is doing okay this year – but has been treading water for the past two months. Yes, we are up for the calendar year and the markets are down, but our advantage over the market is not large and the last two months haven't helped.

Often after we have done well, we write to you about the dearth of opportunities to deploy capital. When we have not done quite as well, we often see lots of opportunities. This is a time when we see a lot of future opportunities.

Markets have been very difficult for both fundamental investors and trend followers. Index funds seem to be proving their worth by losing only a small amount of money.

The problem for investors (as opposed to short term traders) is high volatility but relatively small aggregate movements where the volatility is driven by liquidity and politics <u>but not by the fundamentals of the underlying businesses</u>. The lack of fundamental drivers is why we see opportunities. A fair few stocks are mispriced. We can find longs which are acceptable and there is a plethora of opportunity in shorts.

Politics

Normally we are reluctant to speak about politics. There are many reasons.

a) Internally we have a wide spectrum of political viewpoints.
b) we add very little to the debate – we have little expertise, and
c) by and large politics drives markets far less than pundits think. The feedback is mostly the other way – markets, technology and economic conditions drive politics far more than politics drives markets.

That said we are going break this rule because for the past few months politics has been the major driver of markets.

April had a massive – and now almost entirely reversed – market shock. Donald Trump announced a regime of "reciprocal tariffs" that dwarfed Smoot Hawley for aggressiveness. This is the largest change in American economic policy in the post-war period.

The new trade policy was also only lightly thought through. It is possible that the tariff formula was derived by an AI. The countries were organized by the top-level domain names – so Gibraltar was a different country to the UK and Australian Antarctic Islands which have no permanent population, but which have been granted a country domain name (.hm which is separate from Australia's .au) were separately listed. Antarctic Islands populated only by penguins were charged reciprocal tariffs for how much they abused the USA in trade arrangements.

Markets went down hard – and there was talk about how this was the worst April in financial markets ever. Markets have since gone up hard and go up every time President Trump or one of his staff hints that the US Government policy is for softening.

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Markets have become sanguine. The consensus appears to be that there is a “Trump Put”. If Trump announces a policy which markets take badly that policy will be reversed. If he announces a policy that markets like (deregulation, tax cuts) that policy will be implemented, and therefore Trump’s policy is a one-way bet. It will be market friendly.

Team Fold

Let’s be more explicit about this. For the past fifteen years many market participants have believed in a “Fed Put”. The idea was nothing could go substantially wrong economically because if it did the Fed would just cut rates and liquidity would drive up stocks. The mantra (clearly often true) was that liquidity rather than fundamentals drive stock prices.

This all worked because for most of the last 15 years inflation was stubbornly below the Fed’s target rate. The Fed could just “print money” to solve any problem because there was no substantial inflation response to very easy monetary policy.

The right response (and one we did not do at Bronte in any meaningful way) was simply to buy the dip. As a 2014 YouTube video made clear you just had to buy the (expletive deleted) dip.

There was a couple of years post the pandemic when inflation was above the target rate. Much of that inflation was caused by supply shocks (Covid related supply problems). And the biggest macroeconomics debate was whether the inflation shock was temporary or permanent.

If it was temporary then the “Fed Put” was still operative, and you just had to buy the dip. If permanent, then maybe fundamentals would drive markets again as the Fed fought inflation and liquidity seeped out.

This was the biggest debate on Wall Street – mostly people old enough to remember and fear the 1970s lined up one side – and the mostly younger macroeconomists lined up for “Team Temporary” or “Team Temp”. Being an Australian in your late 50s was a disadvantage because inflation in Australia was only quelled by the 1992 recession rather than the 1982 recession in America. Australians remember inflation. Americans much less so.

Whist inflation is currently above the Fed target range it is not far above – and “Team Temp” can justifiably claim to have won. You had to buy the dip.

Fundamentals really haven’t mattered much lately, and if you traded on fundamentals, you often traded badly.

An extreme statement of this (but one which has mostly been correct) asserts that “nothing ever happens”. Sure, there are problems that are highly visible (trade imbalances, pandemics, technological hiccups) but no policy or market response is required because the Fed – by easing monetary policy – can kick the problems down the road. Implied volatility was at historic lows for much of the last decade – and realized volatility was low – because "nothing ever happened".

The tariff debate in markets is coming down to the same dynamic. There are those that believe President Trump can be taken at his word – he really is a "tariff guy" and he won't back down. They also often believe that the Chinese worry so much about "face" that they will not negotiate with Trump – especially after JD Vance referred to America's biggest trading partner as peasants.

This group believe that an economic catastrophe will happen. The (now consensus) that nothing ever happens will be spectacularly wrong.

The alternative view – which we think has become the consensus view in markets – is that Trump listens to the market and listens to the polls and to Fox News. When tariffs cause problems (price rises, empty shelves, job losses) he will suddenly reverse - and so we should not take the Liberation Day tariffs at all seriously. Robert Armstrong – markets editor in America of the Financial Times – has gone as far as to say this is "Team Fold" and to declare himself a member.

And so, as per the 2014 YouTube video - you just have to buy the (expletive deleted) dip.

So far – Team Fold looks to be winning. Trump has walked back many tariffs – and every day there is another walk-back. Sometimes these walk-backs are limited. The high tariffs on Chinese electronics have been delayed. But the consensus is that America is not ready for the sort of price rises that these tariffs imply, and they will never be implemented.
That said I thought we should lay out the stakes. Because we are Australian, we have a competitive advantage.

Australia was a highly protectionist country until the 1980s

Most Americans have little experience of tariffs. Most Australians below about 55 have little adult experience of tariffs. But Australia was a protectionist country until the middle of the 1980s and John gained his economics degree as the tariffs were finally being removed.

John, scratching back in the memory of undergraduate economics, remembers two overwhelming problems with the tariff regime of protectionist Australia – and given the new protectionist world that we seem to be entering it is worth discussing them again.

The main problems were:

a) How do you tax intermediate goods and
b) The political economy of tariffs

The first is already a subject of debate in the US and elsewhere. The second will be.

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Intermediate goods

An overwhelming problem with tariffs is how do you tax intermediate goods i.e. imported goods that are then used in the production of other goods and exported rather than consumed in country.

In Australia the issue was the car industry. Australia had a car industry that existed only because of industry protection (that is a huge tariff wall). The car industry imported some intermediate goods – and because of economies of scale it was rational to export from Australia too.

But then you had the problem of taxing inputs for an export industry thus making your export industry uncompetitive.

Unless you wanted to make your exports uncompetitive you needed to refund those taxes.

Australia implemented a complicated series of tariff import credits for anyone who exported cars or car components from Australia. (The now defunct and hugely complicated plan for eventually reducing car tariffs in Australia was known as "the Button Plan" and it involved very complicated rules on intermediate goods).

Australia was originally a big market for "muscle cars", that is cars made with oversized 8-cylinder engines and sometimes raced in car rally's and sometimes just good for burning rubber doing doughnuts. The Pontiac G8 was at one stage Pontiac's flagship car in America. It was subsidized by Australian consumers and manufactured by a wildly uncompetitive Australian car industry.

Other Australian-made General Motors cars were exported to the USA. The Pontiac GTO (sold before the G8) and Chevrolet SS (sold after the G8) were only sold with V8 engines. The V8 variants are a great example of intermediate goods, as GM stopped making V8 engines in Australia in 2000. The GTO/G8/SS had engines made in the USA, shipped to Australia to be installed into bodies made in Australia, and then shipped back to the USA as complete cars.

The car plan was the subject of endless politics, a large bureaucracy to implement it and otherwise blatant pork-barreling. It was not a good recommendation for Australian politics.

Intermediate goods will be a problem in the US

Something over 40% of the parts of a Boeing 737 (the main single isle plane made by Boeing) are supplied from overseas. The biggest part is the engine which is made 50-50 by General Electric and the French company Safran. Also, the wing leading edges are made in Scotland, the horizontal stabilizers are made in Italy and the list goes on.

Most of these planes are re-exported. Boeing planes (dominated by the 737) are a major export of the United States and are the symbol of US high tech manufacturing.

A simple prediction. Either

a) The tariff regime implemented by Donald Trump is removed or

b) The regime is modified substantially by giving export credits like the now defunct Button Plan or

c) Boeing sets up its next big plant outside America – with the aim of avoiding tariffs on intermediate goods.

We can't tell what the most likely outcome is. But the perverse outcome of tariffs (designed to support American industry) is that it will drive exporters offshore.

You may think that we are making it up. But it is already happening for products where the final assembly can be easily moved.

Croda is a maker of high-margin intermediate goods (highly specialized chemicals) in the beauty and life science industries. It tends to make the highest value active ingredients in many face creams and the like.

This was a section from their 23 April 2025 sales update when they were asked about surcharges they were applying to recover tariffs.

> *The surcharges is pretty straightforward. I mean you know what we like with pricing. We'll recover margins, all of them. So we've agreed we will do that again this time around….*
> *Quite a number of our bigger customers are trying to relocate production to manufacture in other locations. So for example, L'Oréal are now ramping up CeraVe production in France rather than America. You've got a number of the crop companies wanting to move production. So our job there is two things. One is to be clear on what the surcharges are so they can understand their total production hit or cost hit, which will help them decide on locations. And secondly, is obviously to make sure the stock is in the right place for a change in location.*

Two things are worth noting. Firstly, the active ingredient maker makes a critical component of many of these products. Because it is critical and hard to swap out, they have pricing power – and they will simply pass along the tariff.

But secondly important companies like L'Oréal are moving manufacturing out of America. They are not moving to low-cost Asia. They are moving to high-cost France. CeraVe is a business we know relatively well. It was one of the jewels of Valeant and which it sold (at a very high price) to L'Oréal when Valeant was in acute financial distress.

CeraVe is an American brand, founded by Tom Allison in New York City – and it makes strong medical claims for its face cream. These claims are supported by ingredients sourced globally but also originally by American know-how. Given the product is re-exported and there are now high taxes on the input it makes sense for L'Oréal to shift the branding to France and move the manufacturing.

What is happening with simple products now (like cosmetics) will eventually happen with the core of high-tech American manufacturing. Although, to be fair, it does not take long to move the final assembly of a cosmetic cream – and it takes a lot of effort and time to move the final assembly of a commercial airplane. Long term though we think President Trump's plans, if they are implemented without compensation for intermediate goods, will cost some Boeing workers their jobs.

Trump has already folded on some intermediate goods – especially for the car industry

If tariffs are left in place, by far the most likely outcome is a complex (and politically negotiated) set of rules for intermediate goods. Trump has already issued an amended executive order for cars to allow some of the input tariffs to be refunded.

The political economy of tariffs

Intermediate goods were not the biggest problem of the Australian tariff regime. The big problem was that tariffs distorted the political economy of Australia in destructive ways.

John's first memory of a political issue where he understood the issues was when they were raising car tariffs in Australia. The argument at the time (and which now sounds ridiculous) is that we could not compete with low Japanese wages.

What happened was that the foreigners (in this case Japanese) got better at making cars. Australian industry had three choices:

a) Get better at making cars to match the Japanese

b) Get out of the car business

c) Plead to your politicians for more industry protection.

The third choice was the easy and popular one. It will be more so in America where lobbying is such an ingrained part of politics.

Every time foreigners got better at something Australian industry would not get better, but instead do the same thing behind higher and higher tariff barriers.

If you went to sleep for thirty years you would wake up and find the world had moved on, but Australian industry had not changed, it was just doing the same thing with more and more decrepit plants protected by higher tariff barriers.

Past political economy of tariffs in America

America had a period of high and politicized tariffs particularly in the lead up to the Civil War. There were hundreds of congressional votes and extraordinarily detailed lobbying to protect various industries. [Protectionist policies were a distant but important second to slavery in the causes of the Civil War.]

The definitive history of this was written by an Australian (JJ Pincus who wound up as head of the economics Department at Adelaide University). This developed from his PhD thesis at Stanford. [His book is *Pressure Groups and Politics in Antebellum Tariffs*.]

It was not surprising that the definitive book on the political economy of tariffs in America was written by an Australian. In 1972 tariff debates were the political economy of Australia and by then tariffs were less important in America. Australians were interested but Americans had forgotten.

If tariffs remain in place we suspect we will see many more books on how they have distorted, mostly for the worse, the politics of the United States. Expect special pleading, lobbying and all the graft that goes along with it.

Ultimately the political economy becomes the point

In Australia by the end of the 1960s the most important feature of the tariff regime was how it gave certain players power. In Australia the arrangements were between corrupted unions and a corrupted (mostly Melbourne based) business elite and some captive politicians to rig markets for their favored industries and employers at a cost to other industries and most Australians.

In ante-bellum America more than a few politicians rested power on their ability to get protection for various favored groups.

Ultimately the political economy of tariffs is the point of tariffs. The next few years will show an assortment of lobbyists, industry leaders and international leaders beating a path to Washington to plead their case. [The most detailed pleadings will be about intermediate goods, and you can expect monstrously complicated industry policy to arise, exceeding in complexity the Button Plan from Australia.]

This will create a privileged position for the political class. The political class will decide who wins and who loses.

1990 style conservative politicians who mostly believed in free-enough markets, good rule of law and a modest executive hated bureaucratic nightmares like Australia's car plan. But that ideology offers few opportunities for self-enrichment. Leaving it to the market disempowers the politician (possibly deliberately).

But politicians who like to be the center of attention, and those that like opportunity for graft, love tariffs. They loved them in Australia, and they loved them in ante-bellum America.

Given the way Washington works this could be very dangerous.

Some data re the US economy

As noted above "team fold" is in the ascendancy in markets. There is very little hard data as to the damage wrought by tariffs – but there are some softer indications.

Capital One (where we own stock) thought the consumer was strong (spending is not down) but the last couple of weeks were away from things like holiday bookings and towards consumer electronics. This may be to avoid the tariffs – but domestic travel is very labor intensive and imported consumer electronics are not intensive users of American labor. This, at a minimum, indicates lower forward demand for US labor.

Brambles – the operator of the world's largest pallet pool – is very heavily weighted towards US fast moving consumer goods – and is far up the supply chain. They are already noticing falling volume.

Most importantly – and widely commented on – is a near complete dearth of China-US container volume and a collapse in volumes at the Port of Los Angeles. If this does not change, there will be shortages on shelves in a few weeks. That is – according to Team Fold – the reason why folding is inevitable.

Not a fundamentals market

This market is not driven by the fundamentals of the market, it's driven by politics and liquidity. If we had realized that Team Temp was going to claim such a large victory we would have closed all shorts at lows of April.

We think however that fundamentals will return as a driver of markets. Our short book is pregnant with profits and should make a lot of money sometime – possibly soon if the President does not fold. Our long book will probably lose money at the same time as our shorts mint cash. Net-net we should be okay – but the market will give us an opportunity to get long very high-quality companies at reasonable prices.

Day to day this is frustrating, and sometimes very difficult. We would rather think about and talk about company fundamentals than politics. We are business analysts not political analysts. We want a market that rewards fundamental investment positions rather than short term trading volatility.

That said – dislocation in markets is great long term. There are lots of opportunities as this plays out.

Long-term we are excited.

Thank you for placing your trust in us.

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