Australian Eagle
Asset Management

Long-Short Quarterly Report – March 2020

Portfolio Performance

As at 31 Mar 2020	3mth	6mth	1yr	2yr p.a.	3yr p.a.	Net Return S/I p.a.	Total Net Return S/I
Aust. Eagle Long-Short*	**-17.41%**	**-16.09%**	**-4.14%**	**4.46%**	**8.61%**	**12.17%**	**53.86%**
S&P/ASX 100 Acc**	-23.01%	-22.47%	-13.73%	-1.48%	-0.47%	3.79%	14.95%
Out/(under) performance	5.59%	6.37%	9.58%	5.94%	9.08%	8.39%	38.91%

Performance figures are net of fees and expenses
*Inception date 1 July 2016
** Performance benchmark, past performance is not an indicator of future performance

Portfolio Commentary

The Portfolio returned -17.41% after fees for the March 2020 quarter versus -23.01% for the S&P/ASX 100 Accumulation Index. Despite sharp falls in the market during the quarter, the Fund's longer term return has remained positive at 12.17% p.a. and annualised outperformance has increased to +8.39% since inception.

The Australian market fell with world markets peaking in mid-February and subsequently falling over 30% as the highly contagious COVID-19 virus spread to over 180 countries, causing governments to lockdown residents and shut borders. As the global economy slowed, central banks and governments around the world announced stimulatory monetary and fiscal policies to support their countries. The oil price fell 54% as OPEC and Russia failed to agree to extend supply cuts. Bond yields fell to record lows as investors sought safety from the market volatility.

The Long side of the portfolio contributed to performance as ResMed announced it would aim to triple production of ventilators and masks to assist COVID-19 patients. Fortescue remained steady as management announced no interruption to their cash-flows despite widespread shutdowns in China. ASX Ltd experienced higher trading volumes in light of increased recent market volatility after announcing pleasing growth in all divisions at the 1H20 result.

The Short side of the portfolio contains companies that are overvalued, of poorer quality compared to long portfolio stocks and have no emerging growth delta arguments. As a result, the Short side contributed to performance in the quarter from positions in Flight Centre, Link Administration and Unibail Rodamco. All three companies had balance sheets and/or business models already under pressure prior to the pandemic and positions were built up in prior months. Flight Centre's corporate travel division failed to offset poor performing Australian leisure stores. Link doubled down on a mediocre UK acquisition track record by raising over $250m in debt to buy a European mortgage servicing business. Unibail's UK shopping centres were under pressure from weak consumer demand impacted by Brexit and a number of US retail tenants were actively reducing stores.

Portfolio Highlights

Positives:
ResMed Inc (Long) – The Company's ventilators were subject to high demand during the quarter due to COVID-19 virus affecting the breathing of patients. Gross margins have also steadily expanded due to an increasing contribution from its fast growing digital health division.

Flight Centre Ltd (Short) – The demand for the Company's products and services were negatively impacted by governments shutting down borders resulting in reduced leisure and corporate travel activity. High levels of debt and poor operating cashflow led to the cancellation of the interim dividend payment to conserve cash.

ASX Ltd (Long) – The Company's infrastructure experienced a doubling of trading volume during the quarter from increased market volatility. The Company's interim report also highlighted growth in all divisions and increased demand for its technical and information services.

Negatives:
Oil Search Ltd (Long) – The share price followed the oil price lower after fears of a global recession from shutdowns would result in a fall in demand for oil and gas. OPEC and Russia also failed to agree on future supply cuts, sending the oil price over 50% lower in March.

Japara Healthcare Ltd (Long) – The share price fell after a Sydney aged care home suffered multiple COVID-19 deaths, forcing every Australian nursing home into lockdown. The Company withdrew FY20 guidance but received $16.9m cash for 2 recent property transactions.

QBE Insurance Group Ltd (Long) – The share price fell despite the Company stating that insurance premium growth was continuing its strong momentum from last year. However, Central banks around the world cut interest rates, impacting the return on its $24bn investment book.

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Market Overview

The Australian market fell over 30% during the March quarter before recovering at quarter end as the government announced over $213bn worth of stimulus measures. Companies withdrew guidance, deferred or even cancelled dividend payments and started to raise capital to shore up their balance sheets. Fortescue maintained production guidance as they experienced no disruption to their business operations. Pushpay upgraded FY20 profit guidance as churches tried to stay connected as they were unable to congregate in person. Cochlear conducted a $930m share placement as elective surgeries ground to a halt. Sydney Airport experienced a large decline in passenger traffic in February as the government barred Chinese and South Korean nationals from entering the country due to large numbers of COVID-19 infections.

Portfolio Changes

Increased Exposure:

Evolution Mining Ltd (+3.00%; New Long): A low cost gold producer. The Company expects to extract 25,000 oz of high grade gold per quarter from its recently acquired Red Lake Gold Mine in Canada. This long life mine is the first international mine added to its low cost Australian gold portfolio.

Goodman Group Ltd (+1.50%; New Long): An industrial property fund manager and developer. The $4.3bn globally diversified development work book and strong balance sheet have laid a strong platform for future organic growth.

Domino's Pizza Enterprises Ltd (+3.25%; Exit Short): A multinational pizza franchise company. The Company has returned to growth in Europe and Japan despite a slowdown in the core Australian market.

Decreased Exposure:

Treasury Wine Estates Ltd (-3.25%; Long): An Australian wine maker and distributor. The US supply chain problems have persisted and the Company downgraded their long term targets.

NIB Holdings Ltd (-3.00%; New Short): An Australian private health insurance company. The Company has been experiencing higher claims inflation along with minimal membership and premium growth. The recent acquisition of QBE Travel Insurance has encountered integration issues.

Sydney Airport (-3.00%; Long): An Australian infrastructure operator. Significant decrease in domestic and international passenger traffic may weaken cash flow and put pressure on the balance sheet and distribution yield.

Quarter-End Position & Portfolio Exposures

As at 31 March 2020, the fund had a net exposure of 96.18% and gross exposure of 194.35% to equities. Cash was 3.82%.

Major portfolio exposures were to medical devices & services and technology stocks with less portfolio weight in major banks and construction materials stocks.

Stock Highlight

A Changing Cash-Flow Profile

Chorus Limited (CNU) – New Long Position

Growth Delta Argument: Chorus is a New Zealand based company that demerged from Telecom New Zealand in 2011. With the help of a $929m subsidy from the NZ government, it is currently building and operating the country's Ultra-Fast Broadband Network as well as owning the legacy copper based network. While similar to Australia's NBN Co, Chorus has spent $6bn in the last decade building a superior fibre to the home network and is already listed as a public company. The company offers its services to the wholesale market and is managing the long term task of transitioning from copper based connections to fibre based. As demand for greater bandwidth increases and Chorus being the near monopoly supplier of these services in >80% of NZ, the opportunity exists to create a strongly growing infrastructure asset.

Trigger: After 10 years of building the network, the key changes for the company transforming into a significant cash-flow generating infrastructure asset has only just occurred. Hence, the triggers for investment in the 1H FY20 financial report were the fact that the company has now past their peak capex payments which are now expected to fall significantly over the next 2 years. The company has completed the first and largest phase of network build and unusually this has happened within time and budget, highlighting their strong management credentials around managing this considerable risk. They have received a draft government review on regulated pricing along with stronger than expected broadband uptake, providing an indication of revenue and cash flow outlook.

Outlook: Given that Chorus is the owner of a highly privileged asset, at the current yield of 4% it is fairly priced. However, as the company transitions to infrastructure style distributions there is opportunity for significant increases in distributions as capex falls. For low capex infrastructure assets in Australia, an easy estimation for cash available for distribution is Net Earnings plus Depreciation and Amortisation. On a similar basis, Chorus could eventually have nearly NZ$0.90 per share available to distribute per year. With the share price at about NZ$6.50 and structural tailwinds assisting its cause, Chorus has potential for significant upside going forward.

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Australian Eagle Trust Long Short Fund - Net Monthly Returns

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FY
2016/17	10.52%	0.99%	-1.08%	-4.14%	2.94%	5.16%	-0.25%	5.15%	-0.06%	1.94%	1.31%	0.36%	**24.48%**
2017/18	-1.70%	5.27%	0.20%	5.35%	1.05%	1.10%	2.41%	3.08%	-3.86%	4.18%	2.34%	3.60%	**25.13%**
2018/19	-1.09%	1.45%	-2.24%	-7.62%	-0.53%	2.23%	5.98%	3.70%	1.76%	3.65%	2.15%	6.57%	**16.27%**
2019/20	4.00%	-2.46%	-0.18%	-0.34%	3.80%	-1.78%	5.45%	-6.50%	-16.24%				**-15.04%**

Past performance is not an indicator of future performance

About the Australian Eagle Trust Long-Short Fund

Australian Eagle Asset Management Ltd is an Australian boutique wholesale fund manager specialising in Australian equities. Australian Eagle's investment process seeks to deliver significant outperformance by identifying mispriced stocks with changing growth profiles and building concentrated portfolios of those stocks.

The Australian Eagle Trust Long-Short Fund aims to outperform the Australian equity market over a period of 5 years by allowing clients to access Australian Eagle's demonstrated historical strength in constructing Australian share portfolios applied to a long-short product.

How to Invest

The Australian Eagle Trust Long-Short Fund is only available to investors via the Australian Eagle Trust Product Disclosure Statement (PDS) that is available on www.austeagle.com/how-to-invest/. The Product Disclosure Statement offers investors the opportunity to invest a minimum of $25,000 in the Australian Eagle Trust (the Fund). The Trustee has the discretion to waive or vary this minimum requirement.

The offer of units in the Fund are available to investors both residents in Australia, New Zealand and elsewhere receiving this document (including electronically) in Australia, New Zealand or elsewhere. Investors who are not residents in Australia can invest in the Fund where they are permitted by law to do so. The Trust Company (RE Services) Ltd ABN 45 003 278 831 AFSL 235150, part of Perpetual Ltd, is the responsible entity and issuer of units in the Australian Eagle Trust ARSN 632 568 846. The Investment Manager of the Fund is Australian Eagle Asset Management Pty Ltd ABN 89 629 484 840, a corporate authorised representative of Alleron Investment Management Pty Ltd AFSL 278856.