



# Australian Eagle Asset Management

## Long-Short Quarterly Report – June 2019 FOR WHOLESALE INVESTORS ONLY

### Portfolio Performance

As at 30 Jun 2019	3mth	6mth	1yr	2yr p.a.	Net Return S/I p.a.	Total Net Return S/I
<b>Aust. Eagle Long-Short*</b>	<b>12.83%</b>	<b>26.18%</b>	<b>16.27%</b>	<b>20.63%</b>	<b>21.91%</b>	<b>81.10%</b>
S&P/ASX 100 Acc**	8.57%	20.21%	12.63%	12.35%	13.11%	44.66%
Out/(under) performance	4.25%	5.97%	3.64%	8.28%	8.80%	36.44%

Performance figures are net of fees and expenses

\*Inception date is 1 July 2016

\*\* Performance benchmark

### Portfolio Commentary

The Portfolio finished the 2019 financial year strongly, returning +12.83% after fees for the June 2019 quarter and outperforming the ASX 100 for the 3<sup>rd</sup> consecutive quarter. The Fund has just completed its 3<sup>rd</sup> year of managing money, rewarding investors with returns of 22% p.a. representing cumulative outperformance of +8.8% p.a. since inception.

The Australian market outperformed global markets in the June quarter, boosted by the re-election of the Coalition government in May. The market rose as the big miners and Fortescue followed the iron ore price higher while the big banks and other income stocks rose post the election after previously pricing in a Labor Party victory. The copper and oil prices fell on escalating trade war concerns while financial services suffered from net outflows and further reputational damage from the aftermath of the Royal Commission.

The Long side of the Portfolio contributed positively to performance as iron ore miners rose and healthcare stocks recovered after a period of underperformance. Fortescue rose after declaring a special 60cps dividend. Xero's share price rose as the FY19 result revealed the improving trajectory for profitability and cashflow from their fast growing international operations. ResMed and Cochlear both recovered after underperforming in the previous quarter with a positive 3Q19 report and a new product launch respectively.

The Short side of the Portfolio also contributed to performance as Challenger fell after downgrading earnings for FY20 after already earlier downgrading FY19 earnings due to weak annuity sales in Japan. IOOF also fell after being served with a "show cause notice" from APRA regarding alleged breaches of their license conditions. Caltex downgraded FY19 earnings guidance with Convenience Retail EBIT halving from FY18 and Lytton Refinery only breaking even due to lower refiner margins and production outages.

### Portfolio Highlights

#### Positives:

*Fortescue Metals Group Ltd* (Long) – The Company declared a special 60cps dividend after releasing the 3Q19 production report, returning franking credits to shareholders. The iron ore price continued to climb to new multi-year highs as the disruption of a competitor's Brazilian mine has not been rectified as yet.

*Xero Ltd* (Long) – The Company's FY19 results showed strong international growth with UK adding over 100k subscribers in 2H19. The Company also achieved other major milestones with its inaugural positive free cash flow and 2H net profit result.

*Challenger Ltd* (Short) – The Company's reaffirmed its downgraded FY19 guidance while also noting that persistent headwinds and a lower interest rate environment have triggered a negative growth outlook for FY20.

#### Negatives:

*OZ Minerals Ltd* (Long) – The share price fell with the copper price. The Company's quarterly report showed cash cost and production numbers ahead of guidance in addition to Carrapateena mine development on track for Q4 commissioning.

*QBE Insurance Group Ltd* (Long) – The share price consolidated after the RBA cut interest rates and the US Fed confirmed the case for lower future rates. Management reiterated key operating metric guidance for FY19 at the recent AGM, backed by cost saving initiatives and strong momentum in premium growth.

*Japara Healthcare Ltd* (Long) – The share price fell as the Royal Commission into Aged Care revealed an instance of resident abuse in a Company facility. The Company remains on track to add 1,000 net new operational places in the next 3 financial years.

### 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%





# Australian Eagle Asset Management

## Market Overview

The Australian market rose +8.57% over the June quarter as income stocks were boosted by the Coalition election victory and the RBA cut interest rates to a record low 1.25%. AMP continued to suffer significant fund outflows in the aftermath of the Royal Commission. Resmed's quarterly result showed a strong contribution from all categories especially from recently acquired SaaS companies. Cochlear released its new implant suitable for MRI scans. Invocare reported improving profitability with number of deaths starting to revert to the long term trend.

## Portfolio Changes

### Increased Exposure:

*Nearmap Ltd* (+1.50%; New Long): An international aerial imagery business. The Company's recent expansion into the US has started to gain momentum and become a material portion of earnings. Management have also reaffirmed cashflow breakeven for FY19.

*Pushpay Ltd* (+1.50%; New Long): A mobile donation and engagement system provider for the faith sector. The Company is continuing to experience strong organic growth in the US market and has recently become cashflow and EBITDA positive.

*Janus Henderson Ltd* (+3.25%; Exit Short): A global fund manager. In addition to conducting a US\$200m on-market share buyback, the Company has been a beneficiary of rising markets after a period of underperformance.

### Decreased Exposure:

*Computershare Ltd* (-3.00%; Exit Long): An international share registry and mortgage services company. Earnings growth has been disappointing, with the UK mortgage services business unable to resolve system migration issues. Lower interest rates have also decreased margin revenue outlook.

*Carsales.com Ltd* (-2.25%; Exit Long): A multinational vehicle classifieds platform owner. The Company's troublesome financing division, Stratton Finance, has been put up for sale. Vehicle sales numbers have been falling for over a year in the Australian market, stifling organic earnings growth.

*Reliance Worldwide Corporation Ltd* (-2.25%; New Short): A global plumbing and heating solutions company. The founder retired from his position as Chairman and sold his entire shareholding after the HY19 result. The Company subsequently downgraded earnings guidance after a warmer than expected US winter, resulting in less sales.

## Quarter-End Position & Portfolio Exposures

As at 30 June 2019, the fund had a net exposure of 95.98% and gross exposure of 194.79% to equities. Cash was 4.02%.

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

## Stock Highlight

### ResMed Inc (RMD) – Long Position

*Growth Delta Argument:* As with a number of large capitalisation growth companies, Australian Eagle has a long track record of investing in ResMed Inc. The current positive view and long position dates back to 2008 and is a result of the change in growth trajectory following the rectification of a product recall. The change was not only the result of the rectification but the growth in home testing of Sleep Disordered Breathing (SDB) and new mask releases driving European take-up. Fast forward to the present, ResMed has not only cemented itself as the world leader in the still growing SDB treatment market, but the change in the business growth (or as we like to say, "Growth Delta") in the Connected Health Software as a Service (SaaS) division could greatly improve the future outlook should the company take advantage of this new market opportunity.

*Trigger:* The December 2018 result confirmed that its relatively new Connected Health SaaS division revenue grew +44% with the help of recent acquisitions. The importance of the growth was that the company was reaching the critical mass that would build a healthcare ecosystem, creating revenue growth synergies for both the Connected Health division and the existing SDB products business. This was highlighted by the purchase of Propeller Health, which connects chronic breathing disorder patients with healthcare professionals, an area that is seen as a large potential growth avenue for its SDB products.

*Outlook:* ResMed Inc. is expected to grow revenue and earnings at above GDP rates as its core SDB business continues to take advantage of low penetration rates. Continued research supports the use of SDB products (CPAP) in treatment and prevention of serious diseases. Australian Eagle will be focused upon the ability of the Connected Health SaaS division to contribute to an increasing growth trajectory and therefore provide an almost free call option on top of owning a quality business.





# Australian Eagle Asset Management

## 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/](http://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 Responsible Entity 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.

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