



# Australian Eagle Asset Management

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

### Portfolio Performance

| As at 30 Sep 2019              | 3mth         | 6mth          | 1yr           | 2yr<br>p.a.   | 3yr<br>p.a.   | Net Return<br>S/I p.a. | Total Net Return<br>S/I |
|--------------------------------|--------------|---------------|---------------|---------------|---------------|------------------------|-------------------------|
| <b>Aust. Eagle Long-Short*</b> | <b>1.26%</b> | <b>14.24%</b> | <b>20.03%</b> | <b>19.21%</b> | <b>18.44%</b> | <b>20.51%</b>          | <b>83.38%</b>           |
| S&P/ASX 100 Acc**              | 2.48%        | 11.27%        | 13.67%        | 13.51%        | 12.23%        | 12.88%                 | 48.26%                  |
| Out/(under) performance        | -1.23%       | 2.97%         | 6.35%         | 5.70%         | 6.21%         | 7.63%                  | 35.12%                  |

Performance figures are net of fees and expenses

\*Inception date 1 July 2016

\*\* Performance benchmark

### Portfolio Commentary

The Portfolio returned +1.26% after fees for the September 2019 quarter, continuing to add positive performance after 3 years of consistently strong double digit returns. The Fund has maintained positive outperformance over medium and longer term time frames with +7.63% p.a. outperformance since inception.

The Australian market moved in line with volatile global markets in the September quarter, assisted by 2 interest rate cuts from both the RBA as well as the US Fed. The US yield curve fell and flattened with the 10 year yield closing the gap to the 2 year level to 5bps at quarter end. US-China trade negotiations continued to affect market sentiment along with ongoing Brexit negotiations with the deadline approaching.

The Long side of the Portfolio contributed positively to performance as iron ore miners rewarded shareholders with increased dividends from higher iron ore prices resulting from the Brazilian dam disaster. Healthcare stocks all exceeded FY19 earnings expectations and rose strongly with CSL, Cochlear and ResMed all outperforming in August. Technology stocks also rose with positive momentum and bullish outlook statements despite the general slowing economic conditions. Treasury Wine Estates high margin Asia division continued strong growth with 13% of total volume contributing 44% of group profit for FY19.

The Short side of the Portfolio detracted from performance as IOOF rose after its former directors and executives were cleared of any wrongdoing after being accused by APRA of acting against clients' best interests. Reliance Worldwide announced the integration of John Guest was tracking ahead of schedule. Flight Centre rose after strong North America corporate earnings growth more than offset the problems of the Australian leisure business. Domino's rose despite missing earnings guidance for the 3<sup>rd</sup> consecutive year with same store sales slowing in both ANZ and Europe.

### Portfolio Highlights

#### Positives:

*CYBG plc* (Short) – The Company increased provisions for its legacy PPI costs by GBP300-450m as the number of compensation claims increased significantly towards the 29th August 2019 deadline. Uncertainty remains around the effect of this on the bank's capital levels.

*Treasury Wine Estates Ltd* (Long) – The Company discredited negative short seller reports and reaffirmed its FY20 targets with strong progress and detailed plans for achieving 25% profit margins in its key US market.

*ResMed Inc* (Long) – The Company's sales of masks returned to double digit growth, pushing gross margins up past previous levels. Recent highly synergistic acquisitions in the Connected Health division also added to the result and have made progress towards building an eco-system with a strong network effect.

#### Negatives:

*James Hardie Ltd* (Short) – The share price rose after the Company announced a better than expected 1Q20 report with modest growth in US housing supporting low single digit growth in fibre-cement volumes. The claims for the Company's asbestos fund is still running ahead of payments.

*Domino's Pizza Enterprise Ltd* (Short) – The share price rose despite the Company reporting slowing same store sales in its core ANZ division and a 3<sup>rd</sup> straight year of missing its own profit guidance. Europe sales growth has also slowed while the Japan division has recovered from a recent downturn in sales.

*Flight Centre Ltd* (Short) – The share price rose as the Company reported strong sustained growth in North America Corporate TTV and earnings. The turnaround in the core Australian leisure business is still in progress with management reconfirming FY22 group transformation targets.

### 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% | <b>24.48%</b> |
| 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% | <b>25.13%</b> |
| 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% | <b>16.27%</b> |
| 2019/20 | 4.00%  | -2.46% | -0.18% |        |        |       |        |       |        |       |       |       | <b>1.26%</b>  |





# Australian Eagle Asset Management

## Market Overview

The Australian market rose +2.48% over the September quarter as mid cap stocks rebounded to outperform larger stocks and the RBA cut interest rates twice to a record low level of 0.75%. AMP announced they had retained the majority of their corporate superannuation clients in the aftermath of the Royal Commission. Lend Lease won a large urban development project for Google worth \$20bn. Cochlear announced strong growth in Japan and UK assisted by the support of new government funding.

## Portfolio Changes

### Increased Exposure:

*AMP Ltd* (+4.50% Exit Short, +3.75% New Long): A diversified wealth management and financial services company. With the security of a successful \$780m capital raising, the CEO has outlined his 3 year turnaround strategy for the company and renegotiated the sale of AMP Life with a larger cash component to settle in 1H20.

*Lend Lease Ltd* (+3.75% Exit Short, +1.50% New Long): A diversified multinational construction and property funds management company. The Company has decided to sell its troublesome Engineering business and focus on its highly profitable Development and Funds Management divisions.

*James Hardie Industries plc* (+3.25%; Exit Short): A multinational fiber-cement and building products company. The Company announced solid 1Q20 results with stronger volumes, leading management to reconfirm top of the range guidance supported by modest US housing growth.

### Decreased Exposure:

*CIMIC Ltd* (-3.00%; New Short): A multinational construction and engineering company. Despite winning numerous new contracts, previous concerns about cashflow conversion were confirmed with an EBITDA conversion rate of 52% at the HY19 result.

*Link Administration Holdings Ltd* (-3.50%; Short): A data processing and information registry company. After downgrading earnings guidance in May 2019, the Company painted a further gloomy outlook with lower FY20 profits guidance due to persistent Brexit uncertainty affecting client activity levels and business sentiment.

*ANZ Banking Group Ltd* (-2.75%; Long): An Australian and New Zealand bank. The share price is approaching our valuation target. Recent interest rate cuts in both New Zealand and Australia have increased pressure on the bank's net interest margin.

## Quarter-End Position & Portfolio Exposures

As at 30 September 2019, the fund had a net exposure of 95.55% and gross exposure of 195.17% to equities. Cash was 4.45%.

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

## Stock Highlight

### The Contrarian Purchase!

#### AMP Limited (AMP) – New Long Position

*Growth Delta Argument:* Australian Eagle Asset Management (AEAM) has had a long history in both owning and shorting AMP. It is this long history that allows us to be able to identify which aspects of the company are of higher quality and have potential growth. The August 2019 reporting season confirmed that while remaining under pressure, the Wealth Management adviser network is still producing acceptable returns along with that of AMP Bank. However, the opportunity for significant growth comes from AMP Capital where their infrastructure team have a flourishing, globally scalable product. AEAM identified an opportunity for AMP to benefit from this potential growth engine should they be able to stabilise the existing advisory business.

*Trigger:* The HY19 report highlight for AEAM was the growth in base management fees to AMP Capital, in particular the net fund inflow growth for the Infrastructure and Real Asset division and net inflows from offshore clients. This signifies that the brand is still rated highly in global institutional markets. Further, the successful capital raising and renegotiated sale of its troublesome AMP Life business with a larger cash component provides the required latitude to restructure problem areas and significantly reduces the risk profile of those changes.

*Outlook:* At the current market capitalisation value of \$5.4 billion, the AMP stock price has priced in much of the downside. They are likely to receive \$3bn for the AMP Life and earnings are expected to be over \$400m p.a. for the remaining businesses. As part of the CEO's \$1.3bn transformational plan to reduce costs and de-risk the company, the volatility of earnings should lessen given the simplified nature of AMP. There is significant potential for earnings growth and a positive re-rating should AMP Capital earnings continue to grow.





# 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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