



Australian Eagle Asset Management

Long-Short Quarterly Report – September 2021

FOR WHOLESALE INVESTORS ONLY

Portfolio Performance

As at 30 September 2021	3mth	6mth	1yr	2yr p.a.	3yr p.a.	5yr p.a.	Net Return S/I p.a.
Aust. Eagle Long-Short*	4.61%	20.95%	29.77%	16.78%	17.86%	17.77%	19.08%
S&P/ASX 100 Acc**	1.56%	10.16%	30.94%	8.08%	9.91%	10.55%	11.03%
Out/(under) performance	3.05%	10.79%	-1.17%	8.70%	7.94%	7.22%	8.05%

Performance net of fees & expenses, *Inception 1 July 2016, **Performance benchmark, Past performance is not an indicator of future performance

Portfolio Commentary

The Portfolio returned +4.61% after fees for the September 2021 quarter, consolidating recent positive returns and generating +10.79% outperformance for the past 6 months. Despite recent volatile markets, the team has stayed true to the consistent implementation of the Australian Eagle investment process. The result of a stable investment team and process has generated positive outperformance over the benchmark of +8.05% p.a. since July 2016.

The market experienced a volatile period in the September quarter with global COVID-19 cases still rising despite growing vaccination rates. Inflation concerns lingered as long-term bond yields continued to rise. Central banks around the world started discussions around winding back stimulatory monetary policy as international borders gradually started to reopen. Oil and coal prices rose as a perfect storm of challenging conditions created a global shortage of supply. Iron ore prices fell from US\$214/t to US\$114/t as China clamped down on steel production due to pollution concerns.

The Long side of the portfolio contributed to performance as quality companies with strong competitive advantages outperformed. Incitec Pivot benefited from an uplift in commodity prices despite an erratic recovery from previous production problems. ResMed profited from a recent competitor product recall as management remained confident that market share gains would be permanent. Macquarie Group's share price rose as management expect a positive contribution from its Commodities and Global Markets division in 1H22 in addition to the sale of their UK commercial and industrial smart meter portfolio.

The Short side of the portfolio also contributed to performance as poorer quality stocks continued to disappoint during reporting season. Magellan's exposure to large US and Chinese technology companies suffered from rising bond yields and regulatory challenges in addition to growing client outflows. AGL Energy fell as higher wholesale prices and onerous legacy contracts continued to hurt revenue and margins, resulting in large impairments for company assets. Appen continued to fall due to a disappointing 1H21 result from lower revenue from large US tech companies as well as a downgrade for FY21 profit. Management have also warned that earnings may take longer to recover after they recently acquired a mobile location and Point-of-Interest data provider for up to US\$45m.

Portfolio Highlights

Positives:

Magellan Financial Group Ltd (Short) – The share price fell as the Company's exposure to US and Chinese technology companies remained as the Chinese government cracked down on larger foreign listed companies. The Company has also been experiencing recent net outflows of both retail and institutional funds.

Incitec Pivot Ltd (Long) – The share price rose after the Company announced the Waggaman ammonia plant was restarted after no significant damage was found after Hurricane Ida. The ramp up of production has also coincided with a recent increase in fertiliser prices while their explosives divisions also continue to perform well.

AGL Energy Ltd (Short) – The share price fell after reporting a disappointing result and confirmation of continuing operating headwinds in FY22, leading to a cancellation of its special dividend. Recovery of earnings is not expected to start until at least FY23. Uncertainty remains high in the lead up to the demerger for 4Q22.

Negatives:

Fortescue Metals Group Ltd (Long) – The share price fell with the iron ore price as China curbed domestic steel production on pollution concerns in the lead up to the Olympic games. Management have fast tracked their carbon neutrality targets 10 years earlier to 2030 and remain committed to advance their green hydrogen and renewable energy portfolio.

AusNet Services Ltd (Short) – The share price rose after being subject to a bidding war between multiple parties despite falling revenues and profits from challenging operating conditions. Record low interest rates have triggered increased M&A activity, making infrastructure assets attractive targets to large institutions.

Cochlear Ltd (Long) – The share price fell as the Company's FY22 outlook statement for double digit growth was deemed too conservative by the market. The Company has maintained its majority market share as implant sales have continued their recovery momentum with the UK and developing countries set to follow as they emerge from COVID restrictions.





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Market Overview

The Australian market rose during a volatile September 2021 quarter as accelerating vaccination rates provided state and federal leaders with certainty over a reopening timeline. Telstra introduced its T25 strategy featuring mid-teens EPS growth from FY22. Commonwealth Bank reported growing market share in both business and retail banking as well as a \$6bn off-market buyback. AMP's new CEO announced the \$300m transformation plan remains on track for completion by FY22.

Portfolio Changes

Increased Exposure:

Newcrest Mining Ltd (+5.50%; Exit Short, New Long): A multinational gold miner. The Company's flagship low-cost long-life Cadia mine will experience a growing copper production profile, providing extra cashflow to fund the development of growth projects in Australia and Canada.

IAG Ltd (+3.00%; Exit Short): An Australian general insurer. After a challenging FY21 with significant one-off corporate expenses, the Company is experiencing recovering margins as the insurance premium cycle continues to improve. The Company's investment book is also a beneficiary of recent rising bond yields.

IGO Ltd (+2.50%; New Long): An Australian clean energy metals producer. The Company transformed its portfolio with the divestment of the Tropicana gold mine and investment in a JV with Chinese lithium giant Tianqi. The existing low-cost Nova nickel mine provides additional exposure to the clean energy battery storage market.

Decreased Exposure:

Japara Healthcare Ltd (-3.75%; Exit Long): An aged care owner and operator focused on care of dementia patients. The Company received multiple takeover offers in the aftermath of the Aged Care Royal Commission. The board of directors have recommended shareholders accept a takeover offer by Calvary at \$1.40 per share.

Lendlease Ltd (-3.50%; New Short): A global property owner, developer and fund manager. After failing to benefit from the recent worldwide property boom, uncertainty around execution remains after a new CEO was appointed, introducing a new ambitious 5 year strategy aiming to double annual production to over \$8bn.

BHP Group Ltd (-3.00%; Long): A diversified global miner. The Company's divestments of coal and petroleum assets were at or close to the bottom of their respective commodity price cycles. Senior management also face increased scrutiny for the lack of material targets for reduction of future Scope 3 carbon emissions.

Quarter-End Position & Portfolio Exposures

As at 30 September 2021, the fund had a net exposure of 96.64% and gross exposure of 196.36% to equities. Cash was 3.36%.

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

Stock Highlight

The Current Volatility of Fortescue

Fortescue Metals Group Limited (FMG) – Long Position

Growth Delta Argument: Fortescue was last mentioned as a stock highlight in the September 2016 quarterly report, featuring its addition to the long side of the portfolio some 8 months prior. The change or "Growth Delta" argument at that time revolved around the improved balance sheet and cost of production. We have benefited from holding the stock since that time but how does our process manage the position given the recent stock price falls?

FMG has become a high conviction portfolio holding through both maintaining the qualities that were central to its initiation as well as constant improvement of these qualities and emergence of new growth. The company's cash cost of production has become arguably the lowest in the world and has allowed management to preserve a healthy balance sheet. Key to the improvement of its quality rating has been the cumulative payment of \$7.28 per share in franked dividends to shareholders since 2016. Through recent investment in higher grade mines, FMG is the only major iron ore miner to grow their production profile, effectively reducing downside risk by improving the quality of the company. The resulting large cash flows allows the company sufficient capital to invest in new growth engines while still providing strong returns for shareholders.

Trigger: The most recent trigger events were the completion of Eliwana mine and continued construction of the Iron Bridge project. Upon completion of Iron Bridge by December 2022, the production profile will have increased by over 30% since 2016. The current increase in investment for renewable energy projects also provides further upside potential not yet factored into the valuation.

Outlook: Despite recent falls in the iron ore price, it is evident that FMG is still producing significant cashflow and dividends. At current prices, the stock would be close to a 20% dividend yield. We therefore manage the currently high commodity volatility by maintaining a reduced position in FMG as our only substantial exposure to iron ore while also decreasing other iron ore exposures. Additional upside may also be possible should renewable energy investments start to deliver.





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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%	8.32%	9.97%	3.34%	4.59%
2020/21	3.60%	1.83%	-3.53%	4.35%	-0.62%	0.00%	0.13%	1.86%	1.45%	7.26%	3.63%	4.02%	26.24%
2021/22	3.37%	3.02%	-1.76%										4.61%

Past performance is not an indicator of future performance. Net monthly returns are calculated using exit prices after taking into account all of the Australian Eagle Trust's ongoing fees as disclosed in the PDS and assuming reinvestment of distributions. No allowance has been made for entry fees, the buy sell spread or taxation.

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 \$20,000 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 who are residents in Australia or New Zealand. 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.

The PDS and target market determination can be obtained by calling 02 8252 7559 or visiting our website <http://austeagle.com/how-to-invest/> for the PDS or <https://documents.feprecisionplus.com/Tmd/PCT/TMD/P9IY-ALR2783AU.pdf> for the target market determination.

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