

A person stands on a sandy beach at night, looking out at the ocean. The sky is dark and filled with stars, with a vibrant green aurora borealis visible in the distance. The person is holding a flashlight, which illuminates the sand in front of them. The overall scene is serene and majestic.

# Bongiorno - MDA

## Australian Long Short Equity Review

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Mishan Dahia – Investment Analyst  
Nick Hatzis – Investment Analyst

October 2024

**Atchison**

# Purpose

The Incumbent Long/Short Australian Equities manager, Auscap, is deemed to have undergone a significant transition of their strategy, removing the short book.

Atchison is of the view that an Australian long/short strategy remains relevant in context of the asset class.

As such Atchison has performed a due diligence process to recommend an alternative allocation to fulfil the desired long short exposure.

## Analysis Includes:

- Australian Long/Short Equity manager review
  - Australian Eagle
  - Blackwattle
  - L1
  - Regal
- Performance analysis
- Recommended actions



# Australian Long Short Equity Product Comparison

October 2024

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# Product comparison

| Name                  | Auscap Long Short Australian Equities Fund | Blackwattle Long-Short 130/30 Quality Fund                            | Australian Eagle Trust (Long Short Fund)                              | L1 Capital Long Short Fund (Daily Class)                              | Regal Australian Long Short Equity Fund                               |
|-----------------------|--|---|---|---|---|
| Style                 | Quality/Value                              | Quality/Value   | Quality/Value   | Quality/Value   | Value   |
| Description           | Long only, 35-45 holdings.                 | Long-Short with typical exposure 130/30. 35-55 Longs and 15-25 shorts | Long-Short with typical exposure 150/50. 25-35 Longs and 12-25 shorts | Long-Short with typical exposure 150/50. 50-70 Longs and 15-30 shorts | Long-Short with typical exposure 150/50. 40-150 Longs and 0-60 shorts |
| Region - Aus          | 100%                                       | 100%  | 100%  | 70-100%   | 100%  |
| Region – Int.         | 0%   | 0%  | 0%  | 0-30%   | 0%  |
| FUM in Fund           | \$360M                                     | \$28M   | \$450M  | \$4.2B  | \$560M  |
| Man. Fee              | 1.54%                                      | 0.92%   | 1.23%   | 1.54%   | 0.8%  |
| Perf. Fee             | 15.38%                                     | 17.94%  | 20.5%   | 20.5%   | 15%   |
| Benchmark             | All Ordinaries Accumulation Index          | S&P/ASX 200 Accumulation Index  | S&P/ASX 100 Accumulation Index  | N/A – 10% p.a. absolute return  | S&P/ASX 300 Accumulation Index  |
| Top Holdings          | ARB, Lovisa, CAR group, Hub 24, Nick Scali | Rio Tinto, Resmed, Telstra, CAR group, James Hardie                   | Com Bank, Cochlear, Rio Tinto, Macquarie, QBE Insurance               | Santos, Nexgen, Fraport, Cenovus Energy, Qantas                       | BHP, GQG, Com Bank, Ventia, Zip                                       |
| Lonsec Rating         | Recommended                                | Recommended   | Recommended   | Recommended   | Recommended (Zenith)  |
| Platform Availability | All platforms                              | Hub, BT, Netwealth (No CFS)   | All platforms   | All platforms   | Hub, Netwealth (No CFS or BT)   |

# Long Short Manager Summary

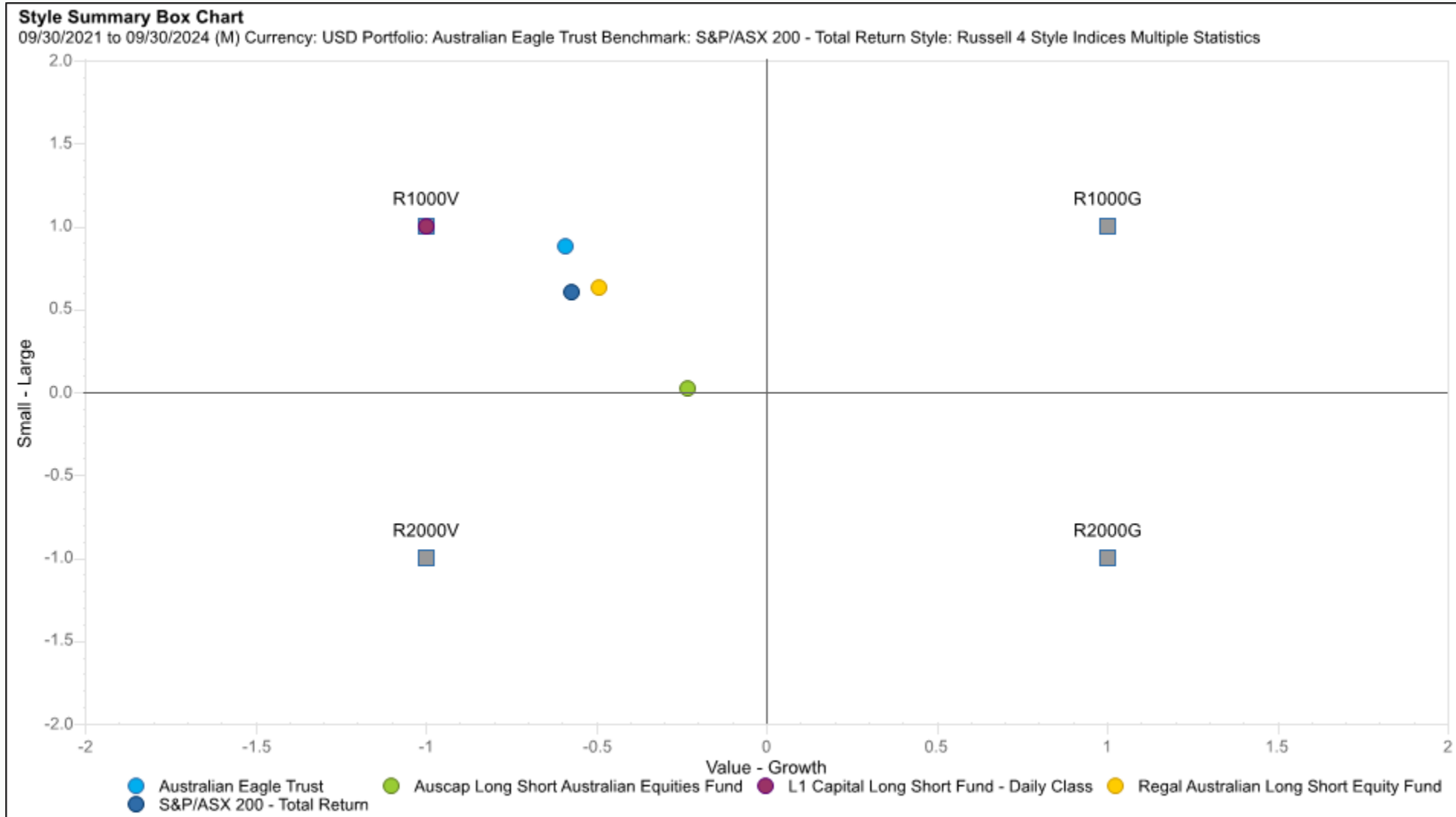
| Auscap Long Short Australian Equities Fund   | Blackwattle Long-Short 130/30 Quality Fund   | Australian Eagle Trust (Long Short Fund)   | L1 Capital Long Short Fund (Daily Class)  | Regal Australian Long Short Equity Fund  |
|--|--|--|---|--|
| <b>Performance:</b> Good<br><b>Fees:</b> High<br><br><b>Management:</b> 1 senior PM + 1 Deputy PM/Analyst.<br><b>Team opinion:</b> Under-resourced<br><br><b>Process:</b> Quality-value with focus on competitive advantage.<br><b>Process opinion:</b> Less structured than peers.<br><br><b>Final Thoughts:</b> Long-only and as such no longer serves intended purpose. For a long-only offering the fee is outsized and process lacks structure. | <b>Performance:</b> Great<br><b>Fees:</b> Medium<br><br><b>Management:</b> 2 senior PM's + 1 dedicated analyst.<br><b>Team opinion:</b> Adequately-resourced<br><br><b>Process:</b> Quality-value oriented with leading proprietary investment tools.<br><b>Process opinion:</b> Highly structured, rules-based investing. Viewed as repeatable.<br><br><b>Final Thoughts:</b> Proprietary investment tools are a standout amongst peers. Long co-tenure of the two PMs managing the strategy at their previous shop. Alpha generative short book is an edge over peers. | <b>Performance:</b> Poor<br><b>Fees:</b> High<br><br><b>Management:</b> 1 CIO, 1 PM + senior analyst.<br><b>Team opinion:</b> Adequately-resourced<br><br><b>Process:</b> Quality value oriented with strong scoring systems.<br><b>Process opinion:</b> Structured with detailed scoring. Time tested since early 2000's.<br><br><b>Final Thoughts:</b> Structured process, although investment universe is seen as highly restrictive (only 130 names). Low-confidence in performance ability. | <b>Performance:</b> Good<br><b>Fees:</b> High<br><br><b>Management:</b> 2 PMs + 7 analysts<br><b>Team opinion:</b> well-resourced<br><br><b>Process:</b> Strong valuation focus with quality assessment.<br><b>Process opinion:</b> Research intensive, however, high workload with AUS and International coverage.<br><br><b>Final Thoughts:</b> Differentiated approach with allocation globally, although means the product is not a pure AUS exposure. Low return target can lead to outsized fees. | <b>Performance:</b> Great<br><b>Fees:</b> Low<br><br><b>Management:</b> 1 CIO/PM, 1 Deputy PM + 2PMs.<br><b>Team opinion:</b> well-resourced<br><br><b>Process:</b> Valuation driven and benchmark aware.<br><b>Process opinion:</b> Pragmatic benchmark aware approach. Each PM manages a sleeve resulting in increased accountability.<br><br><b>Final Thoughts:</b> Process is less focused on shorts and utilises them to leverage the longs. Returns here should be index + gearing alpha. Benchmark aware and diversified in holdings lowers risk. |

# 1 -Year Style & Market Cap Size





# 3 -Year Style & Market Cap Size



# 5 -Year Style & Market Cap Size





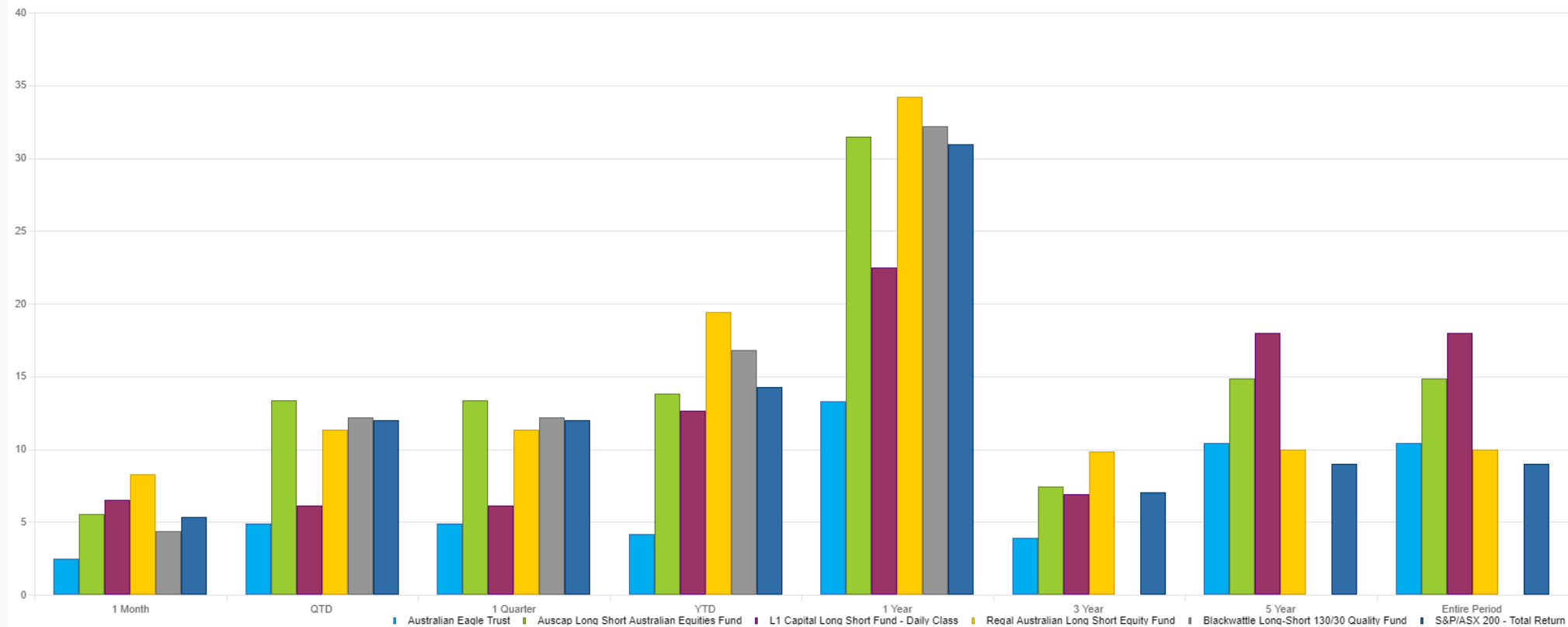
# Australian Long Short Equity Performance Comparison

October 2024

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# Annualised Returns

| Portfolio  | 1m   | 3m   | 6m    | 1yr   | Ann. 3yr | Ann. 5yr | Ann. 10yr |
|--|------|------|-------|-------|----------|----------|-----------|
| Australian Eagle Trust TR in AU                        | 0.17 | 0.98 | -2.37 | 5.35  | 5.3      | 9.76     |           |
| Auscap Long Short Australian Equities TR in AU         | 3.19 | 9.12 | 0.98  | 22.25 | 8.85     | 14.17    | 11.41     |
| Blackwattle Long-Short 130/30 Quality Dis AUD TR in AU | 2.06 | 8.01 | 7.31  | 22.92 |          |          |           |
| L1 Capital Long Short Retail TR in AU                  | 4.14 | 2.13 | 2.83  | 13.92 | 8.36     | 17.73    |           |
| Regal Australian Long Short Equity TR in AU            | 5.87 | 7.17 | 8.79  | 24.81 | 11.32    | 9.31     | 10.63     |
| S&P ASX 200 TR in AU                                   | 2.97 | 7.79 | 6.65  | 21.77 | 8.44     | 8.38     | 8.93      |



# Calendar Year Performance

| Portfolio  | 2024<br>Return | 2023<br>Return | 2022<br>Return | 2021<br>Return | 2020<br>Return | 2019<br>Return | 2018<br>Return | 2017<br>Return |
|--|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Australian Eagle Trust TR in AU                        | 2.85           | 4.44           | 2.38           | 33.46          | 7.29           | 29.42          | 3.31           | 21.25          |
| Auscap Long Short Australian Equities TR in AU         | 8.48           | 18.52          | -12.4          | 43.15          | 10.59          | 18.06          | -18.5          | 17.11          |
| Blackwattle Long-Short 130/30 Quality Dis AUD TR in AU | 14.33          |                |                |                |                |                |                |                |
| L1 Capital Long Short Retail TR in AU                  | 12.68          | 6.64           | 9.63           | 30.35          | 26.53          | 25.87          | -26.59         | 30.52          |
| Regal Australian Long Short Equity TR in AU            | 19.77          | 12.82          | -2.3           | 25.2           | -1.63          | 37.16          | -6.19          | 18.01          |
| S&P ASX 200 TR in AU                                   | 13.01          | 12.42          | -1.08          | 17.23          | 1.4            | 23.4           | -2.84          | 11.8           |

## Calendar Year Performance Rank Per Year

| Portfolio  | 2024<br>Quartile | 2023<br>Quartile | 2022<br>Quartile | 2021<br>Quartile | 2020<br>Quartile | 2019<br>Quartile | 2018<br>Quartile | 2017<br>Quartile |
|--|------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| Australian Eagle Trust TR in AU                        | 4                | 4                | 2                | 2                | 3                | 2                | 1                | 2                |
| Auscap Long Short Australian Equities TR in AU         | 3                | 1                | 4                | 1                | 2                | 4                | 3                | 4                |
| Blackwattle Long-Short 130/30 Quality Dis AUD TR in AU | 1                |                  |                  |                  |                  |                  |                  |                  |
| L1 Capital Long Short Retail TR in AU                  | 2                | 3                | 1                | 3                | 1                | 3                | 4                | 1                |
| Regal Australian Long Short Equity TR in AU            | 1                | 2                | 3                | 4                | 4                | 1                | 2                | 3                |



# Australian Long Short Equity Product Summaries

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# Incumbent Manager – Auscap Long/Short

- The Fund has undergone a significant transition removing the short book. This has triggered a reassessment of the investment case.
- The Fund will now be a long only high conviction fund comprising 40 stocks.
- The Fund was initially selected for a Long/Short exposure and as such no longer serves it's intended purpose.
- The team is led by a capable and experienced individual, Tim Carleton, however, is considered under-resourced when compared to peers in the sub sector.
- The process is viewed as less structured compared to peers and more reliant on the industry experience and company contacts of the team.
- Performance track-record is no longer valid given the change in the composition. Over the one year it has underperformed long only Australian equity peers.
- Atchison no longer believe in the investment case for this fund and suggest alternative options in the Australian equity long/short space.

# Australian Eagle Trust (Long-Short Fund)

- The Fund is lead by a highly capable CIO with support from a long co-tenured investment team. The team is small on a relative basis, however, the universe they cover is considered non-intensive and manageable.
- The process is pragmatic, repeatable and has been tested through time having been used since the early 2000s by its founders.
- An area of concern revolves around the size of the universe to construct a meaningful, alpha generative short book. The investment universe is limited to 130 stocks. Atchison believe this to be highly restrictive when constructing a 50% short book.
- The return in the long run is expected to come from the gearing on the long side and be biased to times where mid-caps will outperform.
- Atchison believe this product is a viable option, however, the universe is too restrictive to have conviction in the manager long term.

# L1 Capital Long Short Fund (Daily Class)

- The Fund is led by capable investors and founders of the business. Supported by a reasonably well-resourced team. However, the team members retain global coverage along with their domestic stocks meaning analysts have a relatively high workload compared to domestic focused peers.
- Capacity was recently revised upwards from \$4bn to \$6bn. This should be a watchpoint going forward regarding how they will soft close and what formal studies they have done to re-affirm this number.
- The process is sound and rooted in a pragmatic quality and valuation discipline. .
- The ability to invest internationally is a competitive advantage and allows them greater flexibility, especially in constructing a meaningful short book compared to domestic managers who are constrained.
- Absolute return target, strong downside protection and low correlation with traditional equity managers means this can be classified as an alternative product.
- Atchison believe this is an attractive offering with the competitive advantage of investing 30% of the portfolio in global stock, increasing the breadth of their universe.
- However, fee load is high with a low outperformance objective of 10% p.a. absolute return resulting in potentially outsized fees. Additional concerns around revised capacity and lack of formal study.

# Blackwattle Long-Short 130/30 Quality Fund

- The Business is a relatively nascent domestic equities manager. A watchpoint going forward is the current low level of FUM at \$160mn across the business. At current time this is not a concern when considering the context of when the business inceptioned, however, if the manager fails to attract FUM there will be questions around business risk.
- Ray David and Joe Koh are seen as highly experienced and capable investors who were running an identical strategy at their previous shop, Schroders. The additional support of a dedicated analyst is viewed positively, although an expansion of the team is expected as FUM is raised.
- The process is founded on a clear philosophy highlighting the importance of quality in the form of sustainable competitive advantage and valuation.
- Proprietary red and green flag tools along with a detailed portfolio construction framework are considered key competitive advantages of the manager. Process is highly structured and repeatable.
- The strategy has outperformed over all assessable time periods to August 2024, with shorting contributing considerable alpha. This stands out against peers who mostly detract on the short side.
- Atchison believes that this fund is one of the most attractive offerings in the Australian equity long/short space.



# Regal Long-Short Fund

- The business has expanded rapidly through M&A. Despite Regal's assertion that King is not directly involved in the company's M&A activities, Atchison believes his role as co-founder ties him to these activities, potentially creating a distraction.
- The portfolio is managed in sleeves by four portfolio managers. Phillip King oversees 60%, while deputy PM Jovita Khilnani manages 20%. Mark Nathan, head of research, and James Sioud, small-cap PM, each manage 10%.
- The investment process is benchmark-aware, with strict constraints limiting active positions to +/- 5%. It focuses on value-driven investments based on intrinsic value, complemented by a macro-overlay.
- Portfolio is highly diversified with roughly 200 positions and well represented across the ASX300 spectrum, effectively mitigating risk.
- Performance outcomes are expected to be heavily driven by the gearing on the long side.
- Atchison considers this fund to be one of the more attractive options in the Australian long/short space, backed by a strong performance track record since 2009. The sleeve-based management structure enhances accountability and helps mitigate key person risk. Furthermore, the fund offers the lowest management and performance fees within its peer group, adding to its appeal.

# Australian Long Short Equity Strategy – Atchison Recommendation

October 2024

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# Regal Australian Equity Long Short Fund

| Pros   | Cons   |
|--|--|
| <ul style="list-style-type: none"><li>• Strong performance outcomes over many years dating back to 2009.</li><li>• Lowest mgmt. fee in the peer group (0.8%) and lowest Performance fee in the peer group (15%)</li><li>• Most diversified with roughly 200 total positions.</li><li>• Diversified across market cap spectrum with holdings across the ASX300.</li></ul> | <ul style="list-style-type: none"><li>• Philip King has competing responsibilities as name portfolio manager on two other strategies.</li><li>• Despite Regal's assertion that King is not directly involved in the company's M&amp;A activities, Atchison believes his role as co-founder ties him to these activities, potentially creating a distraction.</li><li>• Portfolio is managed in sleeves by four portfolio managers potentially diluting some positions.</li><li>• Shorting has detracted since inception.</li></ul> |

# Blackwattle Long-Short 130/30 Quality Fund

| Pros  | Cons  |
|---|---|
| <ul style="list-style-type: none"><li>• Strong performance outcomes since inception.</li><li>• Highly structured approach based on proprietary systems.</li><li>• Co-PMs have long co-tenure managing the strategy.</li><li>• Alpha generative short book – best amongst peers.</li></ul> | <ul style="list-style-type: none"><li>• Low level of FUM in the product at \$28mn.</li><li>• Nascent business with limited track record.</li><li>• Potential distractions for PMs marketing a new business.</li></ul> |



# Atchison Recommendation

- Atchison recommends exiting the Auscap Long Short Fund and reallocating the investment equally between the **Regal Australian Equity Long Short Fund** and the **Blackwattle Long-Short 130/30 Quality Fund**.
- Both funds offer high-octane strategies that merit inclusion.
- The Regal fund offers a more benchmark-aware, diversified portfolio, generating returns through leverage, though with a less effective short book.
- In contrast, Blackwattle delivers a purer long-short approach, featuring a more concentrated portfolio for potentially higher alpha on both sides.
- Atchison believe a blended approach of the two portfolios will mitigate risk and offer the most consistent return profile.

| Fees            | Auscap | 50/50 Blend (Blackwattle and Regal) |
|-----------------|--------|-------------------------------------|
| Management Fee  | 1.54%  | 0.86%                               |
| Performance Fee | 15.38% | 16.47%                              |



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## Recommended Fund Review

### Auscap Long Short Australian Equities Fund APIR: ASX0001AU

#### FUND

The **Auscap Long Short Australian Equities Fund** (the “Fund”) is managed by Auscap and was inceptioned in December 2012. Auscap is a dedicated Australian equities manager with a focus on value and quality. The Long Short Fund is a high conviction portfolio that is typically invested in 30 to 60 securities. The Fund is structured as an open-ended unlisted registered managed investment scheme.

#### INVESTMENT OBJECTIVE

The Fund aims to outperform the All-Ordinaries Accumulation Index (‘the Benchmark’) through the cycle by investing in a portfolio of Australian companies. The Fund’s internal performance objective is to provide an absolute return of 10-15% p.a.

The Fund is a quality, actively managed fund that invests in Australian listed companies. Auscap is focused on generating returns through a focus on fundamental, value-driven long and short positions.

#### GOVERNANCE AND COMPLIANCE

##### Responsible Entity

Auscap (‘the RE’) is the Responsible Entity of the Auscap Long Short Australian Equities Fund. This is not deemed to be a tier one service provider and is a related party RE, which can lead to conflicts of interest. Pleasingly since inception there have been no adverse findings regarding this relationship.

##### Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

#### FUNDS UNDER MANAGEMENT

- ❖ Firmwide - \$375mn
- ❖ Auscap Long Short Australian Equities Fund - \$360mn

Large cap equity focus, thus there is plenty of capacity remaining allowing headroom for growth. Firmwide FUM has been in decline since 2018 where the manager had \$625mn compared to the \$375mn today. Some concerns around continuity of the business, however, the Manager has been pro-active launching an “ex-20” strategy to help broaden its product offering and attract FUM.

#### PRODUCT FEATURES

|   |  |  |  |
|---|--|--|--|
| Fund Type                               | Australian registered managed investment scheme  |  |  |
| Investment Manager & Responsible Entity | Auscap Asset Management Limited<br>ACN 158 929 143 AFSL 428014 ARSN 615 542 213  |  |  |
| Investment Objective                    | The Fund aims to generate strong absolute returns in excess of the Benchmark, being the All Ordinaries Accumulation Index  |  |  |
| Fund Holdings                           | 30 – 60 investments  |  |  |
| Investment Time Horizon                 | 5 years+   |  |  |
| Management Fee                          | 1.5375% p.a. of the NAV of the Fund (GST inclusive net of RITC) [2]. See the <a href="#">Product Disclosure Statement</a> for the Fund for more information on applicable fees and costs.                  |  |  |
| Performance Fee                         | 15.375% of Outperformance over the Benchmark (GST inclusive net of RITC), subject to the performance of the Fund also exceeding that of the Reserve Bank of Australia Cash Rate since the High Water Mark. |  |  |
| Application/Exit Fee                    | Nil  |  |  |
| Commencement Date                       | December 2012  |  |  |

The total fee load is considered high in an absolute sense and high on a peer relative basis. A reduction in the performance or management fee would be considered appropriate.

## INVESTIBLE STATUS

The Fund is open to wholesale and retail investors and is available on platforms. Ample capacity remains available.

## BUSINESS

Auscap Asset Management is a value bias, active Australian equities investment manager established in 2012. The firm is owned and operated by the team and manages \$375mn exclusively sourced from retail investors. Auscap currently operates two strategies: the Auscap Long Short Australian Equities Fund and the recently launched Auscap Ex-20 Australian Equities Fund. In recent years, the firm has been trying to expand its product offering, though a previously launched global equities strategy has since been closed. The launch of the Ex-20 Fund marks the latest effort in this expansion.

A key consideration will be whether Auscap can attract sustainable flows of FUM while maintaining focus on investment performance, given the firm's current emphasis on growth.

A notable strategic shift has also taken place, as Auscap has decided to discontinue short selling. The Auscap Long Short Australian Equities Fund has eliminated its short positions and will soon be renamed the Auscap High Conviction Fund.

## INVESTMENT TEAM

The team is led by Portfolio Manager Tim Carleton who founded the business in 2012. Carleton is highly experienced and was previously an executive director at Goldman Sachs where he was responsible for managing an Australian equities portfolio. Providing support is Deputy Portfolio Manager, Will Mumford. Mumford joined in 2018 with an investment banking background, he is assessed as capable, however, still developing at the portfolio manager level. Gavin Rogers is also listed as part of the team, although his role is "investment specialist" and it is believed he is more involved in distribution and is not involved in the research and portfolio construction process.



Team of two is considered small and under resourced given the additional competing focus on the recently launched Ex-20 Fund. Co-tenure is also lower than peers. Additional resourcing would be viewed positively and help alleviate concerns around workload and competing responsibilities.

### Remuneration and Incentives

Pleasingly the firm is owned and operated by staff and as such they have a share in the profits. Carleton holds a majority stake in the business with Mumford and Rogers becoming equity holders recently in 2023.

### Key Person Risk

A departure of Carleton would be a considerable loss for the Fund and would trigger a re-assessment of the investment case.

## INVESTMENT PHILOSOPHY AND PROCESS

### Investable Universe

The Fund will seek ideas from Australian listed equities across the market-cap spectrum, however, will generally invest at the larger end of the market. Benchmark unaware in the Long Short strategy, although the ex-20 strategy is benchmark aware and thus positions are guided by benchmark weights.

### Philosophy

The Manager is a quality biased focussing on buying high quality, growing businesses with a sensible valuation filter. The managers philosophy can be best described as quality at the right price (QARP).

### Idea Generation

The Manager utilises several quantitative screens to initially filter the universe to uncover high quality companies. In addition to screens the team travel extensively providing an additional source of ideas. It is understood that a reasonable proportion of idea generation lies with Carleton's experience in the markets.

### Research Process

The Fund's investment process begins by identifying companies with competitive advantages that enable them to generate superior returns. The team emphasise return on invested capital (ROIC) and cash flow generation as key indicators of these advantages. After assessing a company's competitive edge, the focus shifts to identifying growth opportunities. The portfolio manager actively travels to meet with management teams and observe areas for potential expansion.

Given the team's size, there is some reliance on sell-side analysts for certain research. However, the manager also conducts in-depth valuation analysis, adapting methodologies based on industry and company specifics to ensure a tailored approach.

A recent strategic shift has seen the removal of the short book, significantly altering the manager's research focus. With no need to research for short positions, the manager now concentrates exclusively on long positions.

The process is viewed as less structured compared to peers and more reliant on the industry experience and company contacts of the team.

### Portfolio Construction

Positioning is based on the team's conviction and the bottom-up fundamental research. Carleton retains ultimate discretion over portfolio composition and the sizing.

The final portfolio will consist of approximately 40 long positions, following the removal of the short book. The Manager is rebranding the fund as the Auscap High Conviction Fund, positioning it as a more concentrated and dynamic offering. However, upon review, the top 20 stocks will represent 80% of the portfolio, while the remaining 20% will be allocated to the bottom 20 stocks. A portfolio with such a large and diluted tail is not considered truly high conviction. Atchison recommends the manager reconsider this structure.

Given the team's size and competing responsibilities, eliminating the tail of stocks would not only reduce the research burden but also deliver a more focused and impactful portfolio.

## Risk Management

The manager has entirely removed the short book and thus risk profile of the Fund has changed dramatically. The Fund is no longer prone to the risks associated with short positions. On the long side the risk is primarily managed through their bottom-up research assessment with a focus on good management, strong balance sheets and liquidity.

## PORTFOLIO CHARACTERISTICS

### Portfolio Turnover

The portfolio turnover is low and expected to be 25-40%.

### Liquidity

The Fund invests in large-mid cap Australian equities and as such liquidity is not considered to be a concern.

### Leverage

Given the removal of the short book the Fund is no longer able to employ leverage and is a long only Australian equities offering.

## PERFORMANCE – As at 31/08/24

| Performance to<br>31 August 2024    | 1 year       | 3 year<br>p.a. | 5 year<br>p.a. | 10 year<br>p.a. | Inception<br>p.a. |
|-------------------------------------|--------------|----------------|----------------|-----------------|-------------------|
| ALSAEF (gross of fees)              | 13.9%        | 8.8%           | 16.4%          | 13.6%           | 19.1%             |
| ALSAEF (net of fees)                | 11.6%        | 6.5%           | 13.9%          | 10.8%           | 15.2%             |
| All Ordinaries Accumulation Index   | 14.7%        | 6.3%           | 8.4%           | 8.2%            | 9.6%              |
| <b>Relative Performance (gross)</b> | <b>-0.8%</b> | <b>+2.5%</b>   | <b>+8.0%</b>   | <b>+5.4%</b>    | <b>+9.5%</b>      |
| <b>Relative Performance (net)</b>   | <b>-3.2%</b> | <b>+0.2%</b>   | <b>+5.6%</b>   | <b>+2.6%</b>    | <b>+5.6%</b>      |

## Performance Opinion

The Fund has underperformed over the past year. Due to recent changes in strategy, including the removal of the short book, its long-term track record is no longer relevant. The absence of leverage and reduced flexibility in long exposure means the Fund's strategy no longer aligns with what Atchison seeks in the long/short bucket.

Consequently, it should now be compared to long-only Australian equity managers, where it has also underperformed its peers over the past year.

## CONCLUSION

- The Fund has undergone a significant transition removing the short book. Given this Fund was initially selected for a Long/Short exposure it no longer serves its intended purpose.
- The team is led by a capable and experienced individual, Tim Carleton. However, the team is considered under-resourced when compared to peers in the sub sector especially when considering the added burden of the ex-20 strategy.
- The process is viewed as less structured compared to peers and more reliant on the industry experience and company contacts of the team.
- Performance track-record is no longer valid given the change in the composition. Over the one year it has underperformed long only Australian equity peers.
- Atchison no longer believe in the investment case for this fund and suggest alternative options in the Australian equity long/short space.

## Recommended Fund Review

### **L1 Capital Long Short Fund (Daily Class)** **APIR: ETL0490AU**

#### FUND

The **L1 Capital Long Short Fund** (the “Fund”) is managed by L1 Capital and was inceptioned in September 2014. L1 is a large cap Australian equities manager with a focus on quality and value.

It employs a long-short, portfolio with roughly 60 longs and 20 shorts. The Fund is structured as an open-ended unlisted registered managed investment scheme. The Fund is offered in daily or monthly liquidity classes.

#### INVESTMENT OBJECTIVE

The Fund aims for strong positive risk adjusted returns whilst preserving capital in falling markets. The Fund has an absolute return objective of 10% p.a.

The Fund is a quality/value, actively managed fund that invests in Australian and international listed companies. L1 Capital is focused on generating returns through differentiated insights into the fundamentals of a stock coupled with a valuation-overlay. The Fund is typically 30-100% net long (typically) and is expected to average 60-70% over the cycle.

#### GOVERNANCE AND COMPLIANCE

##### Responsible Entity

Equity Trustees (‘the RE’) is the Responsible Entity and custodian of the L1 Capital Long Short Fund. Pleasingly the RE is not a related party.

##### Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

#### FUNDS UNDER MANAGEMENT

- ❖ Firm-wide - \$7.2bn
- ❖ Long Short Fund - \$4.2bn
  - LIC – \$1.9bn
  - Unlisted (daily and monthly classes) – \$2.3bn

Capacity was set at \$4bn in 2018, however, a capacity study was conducted in 2020 and determined \$6bn as the new target. Given the international exposure and large cap bias of the Fund this is considered reasonable.

## PRODUCT FEATURES

|  |  |
|--|--|
| <b>Geography</b>                           | Australia, with up to 30% international (gross)  |
| <b>Net/gross exposure</b>                  | 30-100% net long (typically). Expect to average 60-70% over the cycle.   |
| <b>Structure / Currency</b>                | Australian Unit Trust / AUD  |
| <b>Vehicle</b>                             | Australian Unit Trust  |
| <b>Minimum investment</b>                  | A\$25,000  |
| <b>Fees</b>                                | <ul style="list-style-type: none"><li>• Management fee 1.54% p.a.</li><li>• Performance fee 20.5%</li><li>• High watermark Yes</li></ul> |
| <b>Buy / Sell Spread</b>                   | 15bps / 15bps  |
| <b>APIR / ISIN</b>                         | ETL0490AU / AU60ETL04909   |
| <b>Subscription / Redemption frequency</b> | Daily  |

The Fee is considered high in an absolute sense and high on a peer relative basis. A reduction in the performance or management fee would be considered appropriate. Ability to invest up to 30% internationally is seen as a differentiating factor.

## INVESTIBLE STATUS

The Fund is open to wholesale and retail investors, with a minimum investment of \$25,000 and is available on platforms. Capacity was revised up to \$6bn, will be watch point going forward how they manage and soft close.

## BUSINESS

L1 Capital was founded in 2007 by Raphael Lamm and Mark Landau with a focus on managing Australian equities. L1 is 100% employee owned with a reasonable share of equity amongst the key team members. The Manager offers a variety of strategies including Australian equities, international equities and property funds with a focus on quality and value investing.

## INVESTMENT TEAM

The team is co-lead by founders and co-CIOs Raphael Lamm and Mark Landau. The two have a long co-tenure working together and are highly capable investors. Whilst they are highly experienced, they do have competing CIO responsibilities that can be a distraction from the Fund give the depth of products on offer. Supporting Lamm and Landau are seven analysts and two dedicated dealers. Analysts are sector specialists and are responsible for domestic and international equity coverage.



## Remuneration and Incentives

Pleasing both Lamm and Landau are equity holders in the business and have a profit share arrangement. In addition to this they are both significantly co-invested in the Fund. Analysts are remunerated based on the performance of their ideas. These are kept separate to the portfolio and are independent of whether they get into the portfolio or not. The team is considered highly aligned with investors.

## Key Person Risk

A departure of Lamm or Landau would be a considerable loss for the Fund and would trigger a re-assessment of the investment case.

# INVESTMENT PHILOSOPHY AND PROCESS

## Investable Universe

The Fund will seek ideas from Australian listed companies and look at internationally listed competitors with the ability to invest 30% into global equities. The Fund has no benchmark and is agnostic although for performance purposes it is benchmarked against the S&P/ASX 200 Accumulation Index (AUD).

## Philosophy

The core investment philosophy of L1 Capital is that both valuation and qualitative factors are the ultimate determinant of share price performance. The Manager seeks to buy quality companies at an attractive valuation and sell short companies that are declining in quality or overvalued. The manager aims to hold those investments until their competitive advantages are materialised and reflected in returns.

## Idea Generation

The Manager utilises quality and valuation screens to narrow the global and domestic equity universe to a more manageable level. Analysts are sector specialists and will take responsibility for their sectors and idea generation. Lamm and Landau at time have input into the direction they would like analysts to look in if they have perceptions about the market. The manager has an extensive travel budget where analysts are encouraged to go out and look for ideas and meet with company management.

## Research Process

Process is quality biased with a valuation discipline. The team will conduct numerous visits with company management, listed and unlisted competitors, customers, suppliers, consultants and any other stakeholders. L1 believe that identifying stock and industry opportunities through contact with companies is the most fruitful. Once analysts have identified names of interest, they conduct a deep fundamental quality analysis and a valuation analysis. The valuation includes constructing DCFs forecasting out 3-5 years out. DCFs are cross-checked with peer and historical multiples such as P/E, EV/EBITDA and P/B. The analyst will then conduct scenario analysis to assess the spread of risk and reward.

Following the valuation assessment the analyst will conduct a qualitative analysis. The main areas of focus for L1 are management quality, industry and company structure and business trends. The analyst will score each segment which feeds into an overall "quality" score of the business.

Analysts are responsible for coming up with long and short ideas. On the short side the names will typically be high P/E business that have a low "quality" score. The long book will be made up of high-quality score businesses trading at low multiples. The freedom to go internationally to construct the short book is a competitive advantage and allows the manager to construct a more meaningful portfolio compared to constrained Australian equity managers. However, Atchison is aware this reduces performance comparability with domestic Australian managers.

## Portfolio Construction

The final portfolio will consist of roughly 60 long positions and 20 short positions. The portfolio construction process is conviction based with some guideline weights for long and shorts. Longs will be between 1-5% with shorts being between 1-3%.

The Manager's portfolio construction process is less rules based than peers although does have sufficient guidelines.

## Risk Management

The Manager does not use stop loss on its short positions which is a potential cause for concern. However, the Manager does have a set review process when a short falls below a certain level. There are few risk constraints, although this is in line with peers.

# PORTFOLIO CHARACTERISTICS

## Portfolio Turnover

The portfolio turnover will be between 100-150% although name turnover is much lower. The manager is highly active in adding to and trimming positions.

## Liquidity

The Fund invests in large cap Australian and international equities and as such liquidity is not considered to be a concern.

## Leverage

L1 Capital is permitted to borrow on behalf of the Fund. There will be a maximum net exposure: 1.5X and a maximum gross exposure: 3X. The Fund may also borrow by short selling securities. The portfolio is typically 30-100% Net long.

## PERFORMANCE – As at 31/08/24

### Fund returns (Net)<sup>1</sup> (%)

|                      | L1 Capital Long Short Fund | S&P/ASX 200 AI | Out-performance |
|----------------------|----------------------------|----------------|-----------------|
| 1 month              | (3.4)                      | 0.5            | (3.9)           |
| 3 months             | (6.9)                      | 5.7            | (12.6)          |
| 1 year               | 10.4                       | 14.9           | (4.5)           |
| 2 years p.a.         | 11.2                       | 12.2           | (1.1)           |
| 3 years p.a.         | 8.5                        | 6.7            | +1.8            |
| 5 years p.a.         | 17.3                       | 8.1            | +9.2            |
| 7 years p.a.         | 10.9                       | 9.3            | +1.6            |
| 10 years p.a.        | 18.3                       | 8.0            | +10.3           |
| Since Inception p.a. | 18.3                       | 8.0            | +10.3           |

Figures may not sum exactly due to rounding.

### Returns since inception (Net)<sup>1</sup> (%)

|   | Cumulative return | Annualised return p.a. |
|---|-------------------|------------------------|
| L1 Capital Long Short Fund              | 438.6             | 18.3                   |
| S&P/ASX 200 Accumulation Index          | 116.2             | 8.0                    |
| MSCI World Net Total Return Index (USD) | 149.5             | 9.6                    |

## Performance Opinion

The Fund will at times lag in up markets due to the nature of the strategy, however, does well in down markets protecting client capital. A long, short strategy in theory should provide returns irrespective of market direction, therefore there is conviction in the managers ability to achieve its 10% p.a. objective. The Manager has returned 19% p.a. since inception.

The Fund provides downside protection and aims to generate absolute returns of 10% p.a. and as such can be classified as an alternative strategy. This makes it a more appealing investment given the return profile vs traditional equity and alternatives. This is an attractive portfolio that will provide low correlation with traditional equity managers.

## CONCLUSION

- The Fund is led by capable investors and founders of the business. Supported by a reasonably well-resourced team. However, global coverage along with their domestic stocks means analysts have a relatively high workload compared to domestic focused peers.
- Capacity was recently revised upwards from \$4bn to \$6bn. This should be a watchpoint going forward to assess how they will soft close and what studies they have done to re-affirm this number.
- The process is sound and rooted in a pragmatic quality and valuation discipline. The ability to invest internationally is a competitive advantage and allows them greater flexibility, especially in constructing a meaningful short book compared to domestic managers who are constrained.
- Absolute return target, strong downside protection and low correlation with traditional equity managers means this can be classified as an “alternatives” product.
- Atchison believe this is an attractive offering with the competitive advantage of investing 30% of the portfolio in global stock, increasing the breadth of their universe.
- However, fee load is high with a low outperformance objective of 10% p.a. absolute return resulting in potentially outsized fees. Additional concerns around revised capacity limit.



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## Fund Review

### **Blackwattle Long-Short 130/30 Quality Fund** **APIR: ETL3029AU**

#### FUND

The **Blackwattle Long-Short Fund** (the “Fund”) is managed by Blackwattle (‘the Manager’) and was inception in August 2023. Blackwattle is a domestic Australian equities asset manager.

The Fund is an actively managed, long-short Australian equities portfolio, typically consisting of 35-55 long positions and 15-25 short positions. As a 130/30 strategy, the Fund maintains 130% exposure on the long side and 30% on the short side, resulting in a net equity exposure of 100%. The Fund is structured as an open-ended unlisted registered managed investment scheme.

#### INVESTMENT OBJECTIVE

The Fund aims to outperform the S&P/ASX 200 Accumulation Index (‘the Benchmark’) (after fees and before taxes) over the long term. The Fund’s internal return objective is to outperform the benchmark by 3-5% over the long term.

Quality companies at low or reasonable valuations underpin overweight positions while poor quality companies with high valuations facing near-term pressures underpin short positions.

#### GOVERNANCE AND COMPLIANCE

##### Responsible Entity

Equity Trustees (‘the RE’) is the Responsible Entity of the Blackwattle Long-Short 130/30 Fund. Pleasingly this is not a related party RE.

##### Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

#### FUNDS UNDER MANAGEMENT

- ❖ Blackwattle AUM = \$160mn
- ❖ Blackwattle Long-Short 130/30 Fund FUM = \$28mn

Blackwattle is a recently established domestic Australian equities manager and as such is still in the process of building up AUM. At current time the manager is responsible for a relatively small amount of AUM and as such the Fund’s growth is a watchpoint going forward. Currently there are no wind-up concerns given the nascency of the product, however, if the Manager fails to attract FUM it will elevate concerns.

The Manager has been conservative with its capacity limit, currently set at \$1bn. The core large cap equity strategy is set at \$5bn.



## PRODUCT FEATURES

### Key Information

|                                   |                                |
|-----------------------------------|--------------------------------|
| Benchmark                         | S&P/ASX 200 Accumulation Index |
| Recommended investment period     | 3-5 years                      |
| Number of holdings                | 35-55 Long, 15-25 short        |
| Management fee                    | 0.92%*                         |
| Performance fee                   | 17.94%*                        |
| Buy sell spread                   | +0.25%/-0.25%                  |
| Frequency of distributions        | Semi Annually                  |
| APIR Code                         | ETL3029AU                      |
| Application/ redemption frequency | Daily                          |
| Cash limits                       | 30% (typically +10% to -10%)   |
| Inception date                    | 8 <sup>th</sup> August 2023    |
| Zenith Rating                     | Recommended                    |

\*Inclusive of Goods and Services Tax (GST) and net of any Reduced Input Tax Credits (RITC).

The Fund is open to investors and available on platforms with ample capacity for investment. The total fee load of the Fund is considered high in an absolute sense, however, at the lower end of the long/short peer group.

## BUSINESS

Blackwattle is a domestic Australian equities manager founded in November 2022. The business has strong employee ownership with all staff holding equity. Portfolio Managers were all required to put down a minimum of \$1mn into the business. The manager offers a variety of strategies across large and small cap equities with core and long-short products. The manager also has an international equity offering with a dedicated global team.

## INVESTMENT TEAM

The Blackwattle Long-Short team is led by Ray David and Joe Koh. David and Koh were both co-PMs at Schrodgers running an identical strategy before they came over to Blackwattle. Pleasingly they have a long co-tenure managing the strategy together. Both David and Koh are considered highly experienced and capable investors. Providing support is one dedicated analyst who also worked with the pair at Schrodgers. Additionally, the team has access to a quant analyst, although Atchison notes this is a shared resource amongst the Blackwattle teams. Rounding out the broader investment team are five portfolio managers and five analysts as well as CIO Michael Skinner.

The team is considered adequately resourced and has the ability to leverage off other highly skilled investment professionals for information. All team members are generalists which helps facilitate the sharing of information and ideas as well as more insightful debates.

### Key Person Risk

A departure of either David or Koh would be a considerable loss for the Fund and would trigger a reassessment of the investment case. Given the nascency of the product and the equity holding of the PMs these concerns are muted.

### Remuneration and Incentives

Pleasing both David and Koh are equity holders in the business and have a profit share arrangement, however, the firm is not yet profitable. In addition to this they are both significantly co-invested in the Fund. Analysts also hold equity and are remunerated based on their performance and contributions to the Fund. Additionally, all staff at Blackwattle are restricted from making personal investments outside of Blackwattle, thus promoting a strong buy in across the team.

## INVESTMENT PHILOSOPHY AND PROCESS

### Investable Universe

The Fund will seek ideas from Australian listed companies and can go down the market cap spectrum across the ASX300. However, it is expected that the manager remains largely in the ASX200.

### Philosophy

The Manager prescribes to the philosophy that quality companies will consistently outperform the market over the medium term, as their competitive advantages allow for compounding shareholder returns through market cycles. In addition to owning quality companies, they believe investor returns are also determined by the price you pay for a company, "Price is what you pay, value is what you get".

### Idea Generation

The Manager has a highly structured idea generation framework on both the long and the short side. The team utilise a proprietary screen across the investment universe. This is a green flag (for longs) and red flag (for shorts) indicator based on 45 accounting "quality" metrics. These screens are run weekly with new names forming the basis for the research process.

### Research Process

The investment process is grounded in a quality-focused, valuation-disciplined approach, commonly referred to as Quality at a Reasonable Price (QARP). Analysts use a "red and green flag" system to guide their evaluations, conducting deep fundamental analysis with an emphasis on three pillars of quality.

First, the analyst seeks to identify companies with a sustainable competitive advantage, underpinned by recurring earnings and clear growth drivers. Second, they look for firms that hold dominant market positions. Third, there is a focus on management teams and boards that are aligned with shareholder interests.

Following this quality assessment, the analyst undertakes a rigorous valuation analysis, primarily using sum-of-the-parts methods and assessing through-the-cycle earnings. This ensures consistency across the portfolio companies and research universe.

Importantly, the manager recognises the complexity of shorting and goes beyond just targeting poor quality or overvaluation. They also look for key indicators such as industry shifts, business changes, peak-cycle risk, and signs of financial distress when identifying short positions.

The process is considered highly structured and repeatable, with a disciplined focus on quality and value. The red and green flag system is viewed as a competitive advantage, enabling a consistent pipeline of investment ideas. Moreover, the manager's thorough approach to shorting adds a distinct edge over peers in the market.

## Process - Red Flags System



| Momentum last update               |                        | 14/05/2024 |             | Redflag fundamental update |                    | 14/05/2024 |       | Median |       | 8.0   |       |
|------------------------------------|------------------------|------------|-------------|----------------------------|--------------------|------------|-------|--------|-------|-------|-------|
| company name                       | GICS                   | MA Cap \$M | Fiscal Year | Total Flag Count           | Total Flag Count % | Count      | Count | Count  | Count | Count | Count |
| Pure Resources Ltd                 | Materials              | 228        | 30/06/2023  | 100%                       | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| NEOTEC Ltd                         | Information Technology | 11,080     | 30/06/2023  | 100%                       | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| 20Materials Ltd                    | Materials              | 331        | 31/12/2023  | 99%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Synk Resources Ltd                 | Materials              | 416        | 31/12/2023  | 99%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Evolution Mining Ltd               | Materials              | 7,399      | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Corona Power Ltd                   | Utilities              | 369        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| ICI Minerals Ltd                   | Materials              | 660        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Copper Energy Ltd                  | Energy                 | 543        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Preston Ltd                        | Materials              | 532        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Tourism Holdings Ltd               | Industrials            | 391        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Nature Energy Resources Ltd        | Materials              | 856        | 31/12/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Global Data Centre Investment Fund | IT                     | 234        | 30/06/2023  | 99%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Merall Resources Ltd               | Materials              | 12,418     | 30/06/2023  | 97%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Peninsula Energy Ltd               | Energy                 | 300        | 30/06/2023  | 97%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Raynor Mining Ltd                  | Materials              | 382        | 30/06/2023  | 97%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Sealed Harbours Ltd                | Consumer Staples       | 423        | 30/06/2023  | 97%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Woodside Energy Group Ltd          | Energy                 | 52,212     | 31/12/2023  | 97%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| ICMHealth Ltd                      | Health Care            | 250        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Alpha HPA Ltd                      | Materials              | 828        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Breanna Solutions Ltd              | Information Technology | 452        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Develop Global Ltd                 | Materials              | 517        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Energy Resources Of Australia Ltd  | Energy                 | 880        | 31/12/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| ProFit Metals Ltd                  | Materials              | 336        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Naka Resources Ltd                 | Materials              | 2,868      | 31/12/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Naka Mining Ltd                    | Materials              | 288        | 31/12/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Pyrgo Resources Ltd                | Materials              | 1,351      | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Rural Funds Group                  | Real Estate            | 784        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Sanfield Resources Ltd             | Materials              | 3,913      | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Spencer Resources Ltd              | Materials              | 937        | 30/06/2023  | 94%                        | 2                  | 2          | 1     | 0      | 0     | 1     | 1     |
| Auriferum Rare Earths Ltd          | Materials              | 384        | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Beech Energy Ltd                   | Energy                 | 3,700      | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Chalton Mining Ltd                 | Materials              | 549        | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| PRECOS Corporation Holdings PLC    | Information Technology | 553        | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Proctor Building Ltd               | Industrials            | 2,190      | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Intell Ltd                         | Health Care            | 8,343      | 31/12/2024  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Lynas Rare Earths Ltd              | Materials              | 5,887      | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Myer Pharma Group Ltd              | Health Care            | 363        | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| NOVONK Ltd                         | Information Technology | 319        | 31/12/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Seven West Media Ltd               | Communication Services | 283        | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Site Systems Ltd                   | Industrials            | 1,292      | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| Spidy Entertainment Group Ltd      | Consumer Discretionary | 1,063      | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |
| South2 Ltd                         | Materials              | 16,566     | 30/06/2023  | 91%                        | 3                  | 3          | 1     | 0      | 0     | 1     | 1     |

### Red Flag Check List

- Accruals
- ROA Trends
- Free Cashflow
- Aggressive
- Accounting
- Insider selling
- Governance score

## Portfolio Construction

The portfolio construction process is guided by a detailed framework that determines position weights based on multiple factors. Stocks are plotted on a two-dimensional matrix, with the x-axis representing a combined quality and risk score. This score reflects the outcome of the research process, incorporating both the quality assessment and a volatility-based risk ranking. The y-axis ranks stocks according to their absolute return potential, measured by an absolute upside vs downside assessment.

The Fund will generally hold 35-55 long positions and 15-30 short positions. Long positions typically range from 0.5% to 5%, while short positions are sized between -0.5% and -5%. This structured approach to portfolio construction is considered a key competitive advantage, reinforcing the manager's buy/sell discipline and providing clarity in position sizing. The manager places particular emphasis on the upside/downside potential of each stock, which is seen as a crucial edge in maintaining disciplined risk management and return generation.

### Long-Short 130/30 Quality

## Process - Portfolio Construction

|                                |              | Quality/Risk Score (1 = Low Risk, 7 = High Risk) |               |                         |                    |  |                              |   |                              |              |
|--------------------------------|--------------|--|---------------|-------------------------|--------------------|--|------------------------------|---|------------------------------|--------------|
|                                |              | 1  | 2             | 3                       | 4                  | 5  | 6                            | 7   |                              |              |
| Overweight Positions           | > 18%        | 1  |               |                         | LNW                | RHC, TWE, LIC, EVY                               | RIO, STO, JMS, NHC, IFL, CRM | MIN, WHC, APE                               | > 30%                        |              |
|                                | 8% to 18%    | 2  | TLC, NWS      | TLS, CNL, DR            | RGN, SPK           | ORG, SVW   | SOR, DMP, 3PL, RIC           | WDS, RIO, MTS, NEC, HVN, NEU                | FBU, SKC                     | 15% to 30%   |
|                                | -7% to 8%    | 3  | CSL, CAR      | TCL, BXB, JHX, IEL, PMV | SUN                | QBE, SEK, ORL, WOR, FLT                          | BHP                          | S32, BBL, NGR, IPL, MAC, CIA, SUL, CKF, CGF | FMG, LLC, ORA, PGH, PTM, NCK | 5% to 15%    |
|                                | -17% to -7%  | 4  | WOW, RMD      | REH, MND                | COL, CHC, BWP, DHG | MPL, GPT, DKS, ALX, REG, VCK, ALD, SDF, AGL, CWY | SHL, IGO, CTD, TPG           | AMC, AZJ, CGF, DDR                          | NUF, PRN, AZM                | -5% to 5%    |
|                                | -27% to -17% | 5  | COH, REA      | ASX, ARB                | ALL, PLS, ALQ      | NAB, WBC, MOG, IAG, JBN, NSR, CIP                | LTR, SGP, LYC, LTR, ELD      | CPU, SGM, AX1, SSG                          | AMP                          | -15% to -5%  |
|                                | -42% to -27% | 6  | XRO, TNE, NWL | BRG, HLS                | WES, IRE           | CBA, EDV, ANN, LOV                               | ANZ, SGO, BOQ, CSR, ABC      | QAN, BEN, MTR, SGR, EBO                     | EVN                          | -30% to -15% |
| Underweight or Short Positions | < -42%       | 7  | PME, HUB, SIG | GMG, WTC, NXT, FPH      | SGZ, GYG           | WBT, CTT   | AWC, KGN                     | NEM, NST, RSG, TAH, RDD                     |                              | > -30%       |
|                                |              |  | 1             | 2                       | 3                  | 4  | 5                            | 6   | 7                            |              |
|                                |              | Quality/Risk Score (1 = Low Risk, 7 = High Risk) |               |                         |                    |  |                              |   |                              |              |

Larger Portfolio Weights

Smaller Portfolio Weights

### Portfolio Construction Framework

- Long weights scale on risk -5% > to +5%
- Typical Shorts -0.5% > to < -1.5%
- Buy/Sell discipline based on stock upside/downside
- GICS sector limits and consideration
- Liquidity considerations

Matrix risk and return are based on a live share price as at 29/3/24 and is subject to analyst valuation inputs.

|           |   | Risk (Volatility) Rank |        |        |        |        |        |        |
|-----------|---|------------------------|--------|--------|--------|--------|--------|--------|
|           |   | 1                      | 2      | 3      | 4      | 5      | 6      | 7      |
| Valuation | 1 | 4.50%                  | 3.50%  | 3.00%  | 2.50%  | 2.00%  | 1.50%  | 1.00%  |
|           | 2 | 3.50%                  | 2.75%  | 2.25%  | 1.75%  | 1.50%  | 1.00%  | 0.75%  |
|           | 3 | 2.00%                  | 1.75%  | 1.50%  | 1.25%  | 1.00%  | 0.75%  | 0.50%  |
|           | 4 | 0.00%                  | 0.00%  | 0.00%  | 0.00%  | 0.00%  | 0.00%  | 0.00%  |
|           | 5 | -1.00%                 | -0.85% | -0.70% | -0.55% | -0.45% | -0.35% | -0.25% |
|           | 6 | -2.00%                 | -1.75% | -1.50% | -1.25% | -1.00% | -0.75% | -0.50% |
|           | 7 | -3.00%                 | -2.50% | -2.00% | -1.50% | -1.25% | -1.00% | -0.75% |



## Risk Management

The manager's primary approach to risk management is embedded in their thorough bottom-up assessment. Atchison highlights that throughout this process, the manager places significant emphasis on identifying red flags, such as accounting irregularities, valuation concerns, liquidity risks, and volatility. These red flags play a critical role in mitigating potential downside. Additionally, the portfolio construction framework is designed to ensure that no single stock disproportionately impacts the overall risk, maintaining a balanced and well-diversified portfolio.

## PORTFOLIO CHARACTERISTICS

### Portfolio Turnover

The long book is expected to have a low turnover of approximately 45%, with positions typically held for over three years. In contrast, the short book is anticipated to exhibit higher turnover, with an average holding period of 7 to 10 months. This is pragmatic and reflects the manager's longer-term conviction in long positions, while shorts are more actively managed to capitalise on shorter-term opportunities and manage risk.

### Liquidity

The portfolio invests on the larger end of the Australian equities market cap spectrum and as such liquidity is not considered to be a concern.

### Leverage

The Fund is structured in a 130/30 manner meaning the fund employs leverage through short selling. The gross exposure is intended to be 160% whilst net exposure remains at 100%.

## PERFORMANCE – As at 31/08/2024

| Performance Blended Strategy             | 1 months     | 3 months     | 6 months     | 1 Year (p.a)  | 3 Years (p.a) | Inception <sup>2</sup> |
|--|--------------|--------------|--------------|---------------|---------------|------------------------|
| <b>Strategy</b>                          | <b>1.19%</b> | <b>6.41%</b> | <b>9.21%</b> | <b>19.26%</b> | <b>10.56%</b> | <b>15.39%</b>          |
| Index (S&P / ASX 200 Accumulation Index) | 0.47%        | 5.74%        | 6.97%        | 14.90%        | 6.73%         | 11.45%                 |
| <b>Value Added (net)</b>                 | <b>0.72%</b> | <b>0.67%</b> | <b>2.24%</b> | <b>4.35%</b>  | <b>3.83%</b>  | <b>3.94%</b>           |

Blended Strategy

| Performance (Net)                        | 1 months      | 3 months      | 6 months     | 1 year        | Inception (p.a) <sup>1</sup> |
|--|---------------|---------------|--------------|---------------|------------------------------|
| <b>Fund</b>                              | <b>0.32%</b>  | <b>5.31%</b>  | <b>7.27%</b> | <b>15.54%</b> | <b>14.53%</b>                |
| Index (S&P / ASX 200 Accumulation Index) | 0.47%         | 5.74%         | 6.97%        | 14.90%        | 14.57%                       |
| <b>Value Added</b>                       | <b>-0.15%</b> | <b>-0.43%</b> | <b>0.30%</b> | <b>0.64%</b>  | <b>-0.03%</b>                |

31 August 2024

| Cumulative Performance – August 2024 | Inception <sup>2</sup> |
|--------------------------------------|------------------------|
| Fund - Long Alpha                    | -1.04%                 |
| Fund - Short Alpha                   | 5.90%                  |
| <b>Value Added (gross)</b>           | <b>4.86%</b>           |

Inception 8 August 2023

## Performance Opinion

Although the fund was officially launched at Blackwattle in August 2023, the co-portfolio managers have been executing the same strategy previously at Schroders. Importantly, the strategy's performance track record has been carried over, with a three-month transition period where the portfolio's returns matched the index. The strategy has consistently outperformed its benchmark over all measured time periods. Notably, the fund has generated substantial alpha from its short positions, setting it apart from many other long-short peers.

A long-short manager offers diversification benefits from both a risk and return perspective. By capitalizing on opportunities in rising and falling markets, the manager can deliver downside protection and a smoother return profile through different market conditions. Incorporating a long-short Australian equities manager into a multi-manager portfolio can enhance risk-adjusted returns, reduce downside exposure, and offer diversified performance drivers.

## CONCLUSION

- The Business is a relatively nascent domestic equities manager, although has been able to attract significant talent and resources in its brief history. A watchpoint going forward is the current low level of FUM at \$160mn across the business. At current time this is not a concern when considering the context of when the business inceptioned, however, if the manager fails to attract FUM there will be questions around business risk.
- Ray David and Joe Koh are seen as highly experienced and capable investors who were running an identical strategy at their previous shop, Schroders. The additional support of a dedicated analyst is viewed positively, although an expansion of the team is expected as FUM is raised.
- The process is founded on a clear philosophy highlighting the importance of quality in the form of sustainable competitive advantage and valuation.
- Proprietary red and green flag tools along with a detailed portfolio construction framework are considered key competitive advantages of the manager.
- The strategy has outperformed over all assessable time periods to August 2024, with shorting contributing considerable alpha. This is impressive when compared to peers in the long-short space who often struggle with shorting.
- Atchison believes that this fund is an attractive offering and when placed into a multi-manager portfolio can enhance risk-adjusted returns, reduce downside exposure, and offer diversified performance drivers.



# Atchison

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## Recommended Fund Review

### Australian Eagle Trust (Long-Short Fund) APIR: ALR2783AU

#### FUND

The **Australian Eagle Trust (Long-Short Fund)** (the “Fund”) is managed by Australian Eagle and was inceptioned in July 2016. Australian Eagle is a large cap Australian equities manager with a focus on quality.

It employs a long-short, low turnover, portfolio with 25-35 longs and 12-25 shorts. The Fund is structured as an open-ended unlisted registered managed investment scheme.

#### INVESTMENT OBJECTIVE

The Fund aims to outperform the S&P/ASX 100 Accumulation Index (‘the Benchmark’) over a rolling five-year period by investing in a portfolio of Australian companies.

The Fund is a quality, actively managed fund that invests in Australian listed companies. Australian Eagle is focused on generating returns through differentiated insights into the fundamentals of a stock coupled with a valuation-overlay. The Fund is typically 150% long and 50% short resulting in a net 100% long exposure.

#### GOVERNANCE AND COMPLIANCE

##### Responsible Entity

The Trust Company (‘Perpetual’, ‘the RE’) is the Responsible Entity of the Australian Eagle Long Short Fund. Pleasingly the RE is a tier one service provider and not a related party.

##### Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

#### FUNDS UNDER MANAGEMENT

- ❖ Firmwide - \$1.1bn
- ❖ Australian Eagle Trust (L/S Fund) - \$450mn

Large cap equity focus, thus there is plenty of capacity remaining allowing headroom for growth. Business has been growing with Australian Eagle taking on the Montgomery Long only FUM.

## PRODUCT FEATURES

|                                  |   |
|----------------------------------|---|
| Fund Type                        | Australian Equity Long-Short Fund   |
| Inception date                   | 1 July 2016   |
| Investment Platform Availability | BT Panorama, Macquarie Wrap, Netwealth, HUB24, Mason Stevens, Praemium, Colonial First State, DASH, AMP North                     |
| Min. Initial Investment          | A\$20,000   |
| Benchmark                        | S&P/ASX 100 Accumulation Index  |
| Management Fee                   | 1.23% p.a. (inclusive of GST net of RITC)   |
| Performance Fee                  | 20.5% (inclusive of GST) of excess performance above benchmark with outperformance high watermark (accrued daily, paid quarterly) |
| Recoverable Expenses             | 0.1568% p.a. (inclusive of GST)   |
| Distribution Frequency           | Annual  |
| Applications/Withdrawals         | Daily   |
| Buy/Sell Spread                  | ± 0.30%   |

The Fee is considered high in an absolute sense and high on a peer relative basis. A reduction in the performance or management fee would be considered appropriate.

## INVESTIBLE STATUS

The Fund is open to wholesale and retail investors, with a minimum investment of \$25,000 and is available on platforms.

## BUSINESS

Australian Eagle was established in Sydney in 2004 and specialises in Australian equities. The firm is owned and operated by the team and manages in excess of \$1.1bn through a domestic long only strategy and the Australian Eagle Long Short Fund. In 2022 Australian Eagle partnered with Montgomery and took on the FUM from their Large cap long only strategy. Montgomery provides distribution and back-office support in exchange. A potential concern is the distribution focus of Montgomery, given their existing FUM has shifted into the Australian Eagle Long Only strategy. Their focus may be on distributing that fund over the long-short. However, the Australian Eagle Long Short Fund is the only Long Short manager in Montgomery's suite and thus tempers concern to a degree. The distribution focus will be a watchpoint going forward.

## INVESTMENT TEAM

The team is led by CIO, Sean Sequeira, who has been at Australian Eagle since 2004. Sequeira is assessed as being experienced and a highly capable leader of the investment team. Alan Kwan is the named portfolio manager on the Fund, however, Sequeira has ultimate decision-making authority, veto rights and the key figure head. Providing support are two additional analysts as well as an investment committee that includes a risk manager and Albert Hung. Hung was the architect of the strategy when it was being first built out. The manager has indicated that Hung is stepping back his involvement and acting more as a mentor.

The team is considered to be adequately resourced given the narrowness of the investment universe and the length of time they have been working together. On a peer relative basis track-record and co-tenure is high.

### Remuneration and Incentives

Pleasing both Sean and Alan are equity holders in the business and have a profit share arrangement. In addition to this they are both significantly co-invested in the Fund. Whilst there is no direct performance bonus based on the outperformance of the Fund, the equity structure and co-investment are seen as sufficient and the co-PMs are considered to be adequately aligned with investors.

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### Key Person Risk

A departure of Sequeira would be a considerable loss for the Fund and would trigger a re-assessment of the investment case.

## INVESTMENT PHILOSOPHY AND PROCESS

### Investable Universe

The Fund will seek ideas from the ASX100 although has the freedom to go outside and maintains a research list of 130 names. The 130 names include all the ASX100, plus 30 names that they see of interest. The Fund is benchmarked against the S&P/ASX 100 Accumulation Index.

### Philosophy

The manager seeks to buy quality companies with long term competitive advantages and a sensible risk buffer. The manager aims to hold those investments until their competitive advantages are materialised and reflected in returns.

### Idea Generation

The manager believes a focus on quality, valuation and identifying a catalyst to trigger a re-rating upwards will enhance returns. Idea generation is constrained given the size of the universe. The team will cover the ASX100 in detail and analysts are free to choose any other stocks to make up the remaining 30. The manager does not believe meeting with company management adds value to the process at this end of the market.

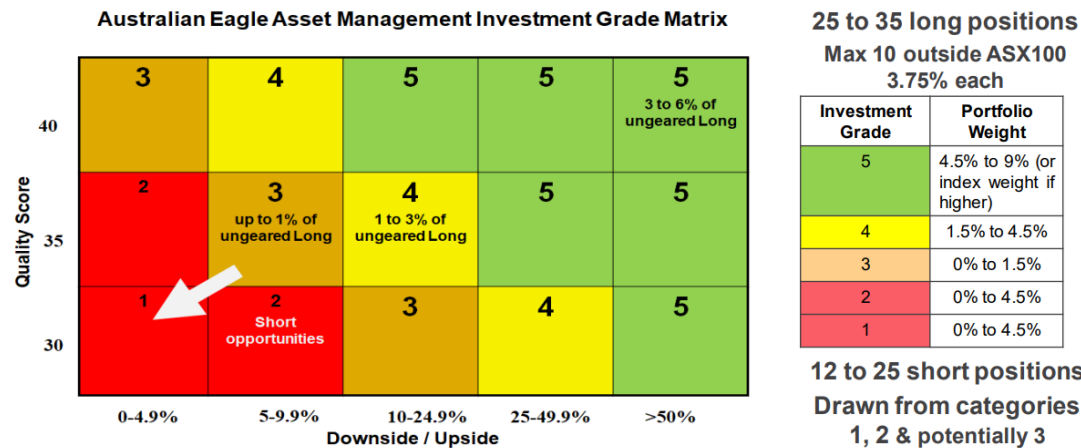
### Research Process

Process is quality biased and has been implemented in the long only portfolio since the early 2000s. This score is driven by 10 sub-components comprising of variables such as industry and company growth, management quality, capital management and shareholder returns. Each of the 10 sub-components is rated from 1 to 5 and accumulated. Only companies with a Quality Score equal to or greater than 30 are considered investible for the long side of the portfolio. The quality score is re-tested every six months and whenever significant news comes out to ensure accuracy.

In addition to this the manager will conduct a valuation analysis to rank stocks based on their “valuation gap”. Analysts will use valuation methods depending on the industry and competitive factors. The manager pairs the quality score with the valuation gap which creates a rubric that determines position size.

In relation to the Fund’s shorting program, the same methodology of security analysis is employed with short candidates tending to arise from lower quality stocks that likely have pronounced negative Growth.

Atchison believe the manager’s process is highly structured and rules based. This ultimately enhances the repeatability and consistency of the process.



## Portfolio Construction

The final portfolio will consist of roughly 25-35 long positions and 12-25 short positions. The portfolio construction process is rules based and driven primarily from the scoring rubric. Clear and pre-determined weights for each score based on the intersection of the quality score and the valuation score.

The Manager has a set guide for position sizing based on the assessment of quality and valuation upside. This is seen as a strength compared to some less structured peers. Sell decisions are based on a deterioration of quality or when valuation has extended beyond the team's assessment.

## Risk Management

They do have the ability to wind down the short exposure when they see times of stress which is a positive. The Manager is relatively unconstrained in terms of positioning and managing the Fund. There are few risk limits in place, however, this is consistent with the high conviction design. Shorts have a maximum holding period of one year, which is seen as long and potentially hurtful to alpha.

# PORTFOLIO CHARACTERISTICS

## Portfolio Turnover

The manager is active in adding and trimming names; however, actual name turnover is low. Long positions are typically held for 3 years while short positions are held for up to or less than a year.

## Liquidity

The Fund invests in large-mid cap Australian equities and as such liquidity is not considered to be a concern.

## Leverage

The Fund does employ leverage utilising a 150/50 portfolio maintaining a 200% gross exposure. The Fund takes 150% of its NAV long and 50% of its NAV short. Leverage magnifies both gains and losses and as such should be treated with precaution.



## Performance – 31 July 2024

|                | 1 month | 3 months | 6 months | 1 year | 3 years (p.a.) | 5 years (p.a.) | 7 years (p.a.) | Since inception (p.a.) |
|----------------|---------|----------|----------|--------|----------------|----------------|----------------|------------------------|
| Fund           | 3.40%   | 4.09%    | 3.63%    | 8.49%  | 6.56%          | 9.69%          | 13.62%         | 14.51%                 |
| Benchmark      | 4.21%   | 6.47%    | 7.51%    | 13.75% | 8.15%          | 7.97%          | 9.64%          | 10.13%                 |
| Outperformance | -0.80%  | -2.39%   | -3.88%   | -5.27% | -1.59%         | +1.71%         | +3.98%         | +4.38%                 |

SOURCE: AUSTRALIAN EAGLE, AS AT 31 JULY 2024.  
FOR THE AUSTRALIAN EAGLE TRUST, PERFORMANCE IS NET OF FEES, BENCHMARK S&P/ASX 100 ACCUMULATION INDEX, INCEPTION DATE 30<sup>TH</sup> JUNE 2016

## Performance Opinion

The Fund's performance has faced considerable pressure, underperforming the benchmark by 5.3% over the 12 months to July 2024. This underperformance has been largely driven by the short side, which contributed over 6% in negative attribution. The Manager's relatively small investment universe has limited their ability to effectively construct a meaningful short book.

In theory, a long/short strategy should generate returns across market cycles, regardless of market direction. However, recent performance has exposed weaknesses in the strategy, particularly the Manager's constrained stock selection universe and the difficulty in swiftly exiting poorly performing short positions. This inability to adapt and rotate out of losing shorts has magnified the strategy's downside during periods of volatility, raising concerns about its resilience in dynamic market environments.

## CONCLUSION

- The Fund is led by a highly capable CIO with support from a long co-tenured investment team. The team is small on a relative basis, however, the universe they cover is considered non-intensive and manageable.
- The process is pragmatic, repeatable and has been tested through time having been used since the early 2000s by its founders.
- An area of concern revolves around the size of the universe to construct a meaningful, alpha generative short book. Only 130 stocks to construct a 50% short book is considered challenging.
- The return here in the long run is going to come from the gearing on the long side and be biased to times where mid-caps will outperform.
- In future Atchison will need to assess the growth in FUM of the Long only book vs the growth of the L/S book. This will shed light on how Montgomery is pushing the two products – Atchison believe Montgomery will place an emphasis on distributing the Long only given it has their original client FUM.



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## Fund Review

### Regal Australian Long Short Equity Fund APIR: RGL0002AU

#### FUND

The **Regal Australian Long Short Equity Fund** (the “Fund”) is managed by Regal (‘the Manager’) and was inceptioned in August 2009. The Manager covers a broad range of asset classes with a number of alternative investment management subsidiaries.

The Long/Short equity Fund is an actively managed, diversified offering holding roughly 40-100 long positions and 0-40 short positions. The Fund is expected to maintain a net exposure between 90-110% with a gross exposure of 90-200%.

#### INVESTMENT OBJECTIVE

The Fund aims to outperform the S&P/ASX 300 Accumulation Index (‘the Benchmark’) (net of fees) over rolling five-year periods. The Fund has a risk objective to maintain tracking error in the range of 4-8% p.a.

The Fund is a quality, actively managed fund that invests in Australian listed companies. The Fund is typically 150% long and 50% short, resulting in a net 100% long exposure.

#### GOVERNANCE AND COMPLIANCE

##### Responsible Entity

The Trust Company (‘Perpetual’, ‘the RE’) is the Responsible Entity of the Regal Australian Long Short Equity Fund. Pleasingly the RE is a tier one service provider and not a related party.

##### Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

#### FUNDS UNDER MANAGEMENT

- ❖ Regal Firmwide FUM = \$17.2bn
- ❖ Regal Australian Long/Short Equity Fund = \$560mn

The Manager oversees a significant amount of FUM, driven largely by recent acquisitions of private market and alternative asset managers. The Long/Short Fund exclusively serves wholesale and institutional investors, aligning with Regal’s focus on these markets. Atchison has no concerns regarding the current FUM levels or the fund’s inflows.

## PRODUCT FEATURES

| FUND INFORMATION   |   |
|--------------------|---|
| Name               | Regal Australian Long Short Equity Fund |
| Structure          | Australian Unit Trust                   |
| Inception          | August 2009                             |
| Management Fee     | 0.8%                                    |
| Benchmark          | S&P/ASX 300 Accumulation Index          |
| Performance Fee    | 15% above Benchmark                     |
| High Water Mark    | Yes                                     |
| APIR Code          | RGL0002AU                               |
| Fund Size          | A\$104m                                 |
| Minimum Investment | A\$100,000                              |
| Subscriptions      | Daily                                   |
| Redemptions        | Daily                                   |
| Registry           | Boardroom Pty Ltd                       |
| Auditor            | Ernst & Young                           |
| Custodian          | JPM/UBS/BofA                            |
| Unit Price         | \$1.41                                  |

The Fund is open to investors and available on platforms with a minimum investment amount of \$100,000. There is no set capacity limit although it is estimated to be around \$1bn. Atchison would prefer to see a more structured/formal process around capacity.

## BUSINESS

Regal Partners Limited is an ASX-listed (ASX: RPL), specialist alternative investment manager with a market cap of \$1.3bn. Regal Partners Limited was formed in June 2022 following the merger of privately owned Regal Funds Management (founded 2002) with ASX listed VGI Partners (founded 2008). The Group manages a broad range of investment strategies covering long/short equities, private markets, real & natural assets and credit & royalties on behalf of institutions, family offices, charitable groups and private investors.

The Manager has been growing through acquisitions in recent times with a focus on acquiring alternative asset managers. Atchison have some concerns around the strategic focus of the business and potential distractions it may cause to the investment team.

## INVESTMENT TEAM

The investment team is led by Philip King, CIO and co-founder of Regal, who also serves as the portfolio manager for the Regal Australian Long Short Equity Fund. While Atchison regards King as highly capable, there are concerns about his competing responsibilities, as he manages three additional funds at Regal. Furthermore, despite Regal's assertion that King is not directly involved in the company's M&A activities, Atchison believes his role as co-founder and one of the largest shareholders inevitably ties him to these activities, potentially creating a distraction.

Supporting King on the Long Short Fund is Jovita Khilnani, who serves as the deputy portfolio manager. Regal's broader investment team consists of 25 professionals across their equity products, working collaboratively and sharing insights. Analysts are sector and geographical specialists. Additionally, Mark Nathan, Head of Research, offers overarching support across all of Regal's funds.

The portfolio is managed in sleeves by four portfolio managers. Phillip King oversees 60%, while deputy PM Jovita Khilnani manages 20%. Mark Nathan, head of research, and James Sioud, small-cap PM, each manage 10%. Analysts present ideas weekly to the portfolio management team and it is up to the PM's discretion to make

decisions for their sleeve. Atchison believe this promotes accountability, however, can also result in diluted positions flowing through to the final portfolio.

## Key Person Risk

A departure of King would trigger a reassessment of the investment case. Given his role as CIO and co-founder, with a significant equity stake in the business, a sudden departure is seen as unlikely.

## INVESTMENT PHILOSOPHY AND PROCESS

### Investable Universe

The Fund will seek ideas from Australian listed companies and can go down the market cap spectrum across the ASX300.

### Philosophy

The Manager's investment philosophy is based on the belief that the market is broadly correct in valuing companies. However, due to a range of factors, such as human emotion and temporary supply/demand imbalances, the market can misprice companies. Regal seeks to identify this mispricing and the factors driving the market's view capitalising on both the long and short side.

### Idea Generation & Research Process

Analysts, as sector specialists, are tasked with generating investment ideas across the ASX300. Atchison views this broad coverage as a relative strength, enhancing the Fund's return potential by offering a wider opportunity set. However, Atchison also notes that the idea generation process is less structured compared to peers, who tend to rely more on systematic screens and a formalised research agenda.

Analyst research follows a methodical four-step process. The first step involves conducting a comprehensive fundamental and valuation analysis, including setting price expectations, to identify companies that are either undervalued or overvalued relative to their intrinsic value. This forms the foundation for both long and short positions. Analysts have the discretion to select the most appropriate valuation method depending on the business. Typically, for short positions, the stock must be overvalued by at least 30% above its intrinsic value, whereas long positions are assessed with greater flexibility. Atchison views this restriction positively.

After the valuation step, the analyst conducts a macro analysis, leveraging third-party brokered macro research to identify broader economic factors that could influence the company's path to its intrinsic value.

The third stage focuses on identifying a catalyst that could trigger a re-rating of the stock. Lastly, the analyst highlights where Regal's unique perspective or competitive edge lies in their assessment of the stock.

Analysts present their findings during weekly stock meetings, where portfolio managers utilise this research to inform their core long and short positions. While Atchison acknowledges the thoroughness of the research process, they also highlight the dependence on portfolio managers' judgment. However, Atchison views this discretion as a positive feature, promoting both accountability and active decision-making within the investment process.





## Portfolio Construction

The Portfolio typically consists of around 200 stocks and is constructed with a benchmark-aware approach. Individual positions are capped at a maximum active weight of +/-5%. Portfolio managers hold core ASX300 constituents while leveraging analyst research to selectively take long and short positions. Generally, the Portfolio will feature 40 key long positions and 30 key short positions, with the remainder built to align with the benchmark.

While the sleeve-based investment approach promotes accountability, it can occasionally lead to the inclusion of diluted positions. Atchison is mindful that this may result in a tail of holdings that contribute little to overall returns.



## Risk Management

The risk management process is primarily driven by bottom-up, stock-specific analysis. However, Philip King can implement portfolio-level hedges when necessary. The manager does not employ stop-losses on short positions nor impose time limits on them. While this approach may seem less risk-controlled compared to peers, Atchison believes it has been effectively managed historically.

Atchison also notes that Regal's six prime broker relationships help mitigate risk on both the broker and short sides. This diversification is considered a relative strength, reflecting the advantages of being part of a large and growing firm.

## PORTFOLIO CHARACTERISTICS

### Portfolio Turnover

The Portfolio follows a high-turnover strategy, with frequent trading. This is expected given its benchmark-aware approach and the need to continuously adjust positions in response to market movements.

### Liquidity

The Portfolio invests across the full market-cap spectrum, including some names that might be classified as small-cap. While Atchison remains cautious about the potential liquidity challenges in this segment of the market, they believe Regal effectively manages position sizes and overall capacity to mitigate these risks.

### Leverage

The Fund does employ leverage utilising a 150/50 portfolio maintaining a 200% gross exposure. The Fund takes 150% of its NAV long and 50% of its NAV short. Leverage magnifies both gains and losses and as such should be treated with precaution.

## PERFORMANCE – 31/08/2024

|  |
|--|
| Correlation:<br>S&P/ASX300 0.87  |
| Average 5-Yr Exposure:<br>Gross Exposure: +195%<br>Net Exposure: +101% |

PERFORMANCE SINCE INCEPTION

|  | 1 yr   | 3 yr (p.a.) | 5 yr (p.a.) | 7 yr (p.a.) | 10 yr (p.a.) | Since inception (p.a.) |
|--|--------|-------------|-------------|-------------|--------------|------------------------|
| Regal Australian Long Short Equity Fund <sup>1</sup> | +16.7% | +10.2%      | +8.0%       | +12.6%      | 9.6%         | +13.8% p.a.            |
| Benchmark <sup>2</sup>                               | +13.3% | +7.1%       | +7.5%       | +9.3%       | +8.0%        | +8.8% p.a.             |
| Active   | +3.4%  | +3.1%       | +0.5%       | +3.3%       | +1.6%        | +5.0%                  |

## Performance Opinion

The Fund has consistently outperformed its benchmark across all time periods up to August 2024. Atchison understands that the manager employs shorting primarily to maintain the earnings profile, with less emphasis on alpha generation, thereby allowing the Fund to increase exposure on the long side through gearing. While short positions have detracted 2.5% per annum since inception, this has been more than offset by the amplified returns from the geared long positions.

Atchison has strong conviction in the manager's ability to deliver both index-plus returns and additional alpha, thanks to the strategic use of shorts to enable gearing on the long side.

## CONCLUSION

- The business has expanded rapidly through M&A. Despite Regal's assertion that King is not directly involved in the company's M&A activities, Atchison believes his role as co-founder ties him to these activities, potentially creating a distraction.
- The portfolio is managed in sleeves by four portfolio managers. Phillip King oversees 60%, while deputy PM Jovita Khilnani manages 20%. Mark Nathan, head of research, and James Sioud, small-cap PM, each manage 10%.
- The investment process is benchmark-aware, with strict constraints limiting active positions to +/- 5%. It focuses on value-driven investments based on intrinsic value, complemented by a macro-overlay.
- Portfolio is highly diversified with roughly 200 positions and well represented across the ASX300 spectrum, effectively mitigating risk.
- Performance outcomes are expected to be heavily driven by the gearing on the long side.
- Atchison considers this fund to be one of the more attractive options in the Australian long/short space, backed by a strong performance track record since 2009. The sleeve-based management structure enhances accountability and helps mitigate key person risk. Furthermore, the fund offers the lowest management and performance fees within its peer group, adding to its appeal.

# Atchison

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