



# *High conviction investment insights*

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Blake Henricks

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# *Important Information*

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## *Agenda*

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**01** Introduction to Firetrail

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**02** The M&A cycle is heating up

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**03** Great companies, bad investments

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**04** Summary

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ABOUT FIRETRAIL

## *High conviction investment experts*

Focused approach

1

Unconstrained

2

An experienced  
team

3

*Specialists in Australian and market-neutral equities*

## ABOUT FIRETRAIL

# Who are Firetrail?



**Patrick Hodgens**  
*MD, Portfolio Manager*  
33 yrs exp. Accounting and Finance background



**James Miller**  
*Portfolio Manager*  
11 yrs exp. Civil engineer turned investment analyst



**Scott Olsson**  
*Analyst*  
13 yrs exp. Experienced actuary & financials analyst



**Eleanor Swanson**  
*Analyst*  
3 yrs exp. JP Morgan grad with a degree in Health Science



**Kyle Macintyre**  
*Investment Specialist*  
7 yrs exp. MBA with extensive product management experience



**Annabelle Bamford**  
*Business and Marketing Exec.*  
2 yrs exp. Commerce and marketing double degree



**Blake Henricks**  
*Deputy MD, Portfolio Manager*  
15 yrs exp. Maths background, experience in multiple industries



**Matthew Fist**  
*Portfolio Manager*  
8 yrs exp. 4 years at BHP as a Geo-scientist



**Ramoun Lazar**  
*Analyst*  
15 yrs exp. Finance background, #1 rated sell-side analyst



**Justin Gray**  
*Analyst (Risk/Execution)*  
15 yrs exp. Highly experienced actuary, risk and quant manager



**Kathryn Koutouzis**  
*Head of Dealing (18 June Start)*  
5 yrs exp. Commerce degree with a double major in Finance and International business

- A passionate team with a strong track record
- Deep history working together at Macquarie
- Why we started a boutique?

1. **Team stability** – All investment team members are equity owners in the firm
2. **Culture** – Focus on performance and idea meritocracy
3. **Alignment** – A common mission to ‘**generate outstanding performance for our clients**’

*High conviction investing experts*

## ABOUT FIRETRAIL

# Key Strategies

	<i>Australian High Conviction</i>	<i>Absolute Return</i>
Investment style	Concentrated	Market Neutral Equities
Benchmark	S&P/ASX 200 Accumulation Index	RBA Cash Rate
Experience managing strategy	November 2005	July 2015
Excess return objective	+5% per annum (pre-fee, medium term)	+7% per annum (pre-fee, medium term)
Expected risk objective	Tracking error 5-6%	Volatility 9-12%
Typical market exposure	Generally 100%	Generally 0-10%

Performance History	Macquarie High Conviction Fund <sup>1</sup>	Macquarie Pure Alpha Fund <sup>2</sup>
Excess return - 1 year (post-fee %)	<b>+8.9%</b>	<b>+9.5%</b>
Excess return - 2 years (post-fee % pa)	<b>+5.5%</b>	<b>+12.4%</b>
Excess return - 3 years (post-fee % pa)	<b>+10.4%</b>	
Inception (post-fee % pa)	<b>+3.9%</b>	<b>+16.9%</b>

## High conviction investment strategies

Past Performance is not a reliable indicator of future returns

1. Macquarie High Conviction Fund Post-Fee Outperformance of the S&P/ASX 200 Accumulation Index to 31 October 2017. Inception 30 Nov 2005 Source: Mercer

2. Macquarie Pure Alpha Fund Post-Fee Outperformance of the RBA Cash Rate to 31 October 2017. Inception 30 Jun 15 Source: Mercer

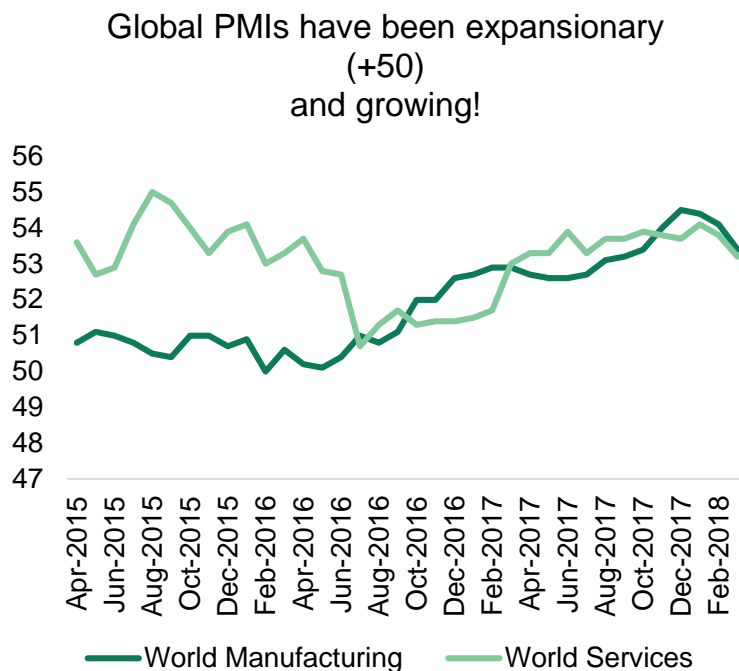
# 02

*The M&A cycle is heating  
up*

THE M&A CYCLE IS HEATING UP

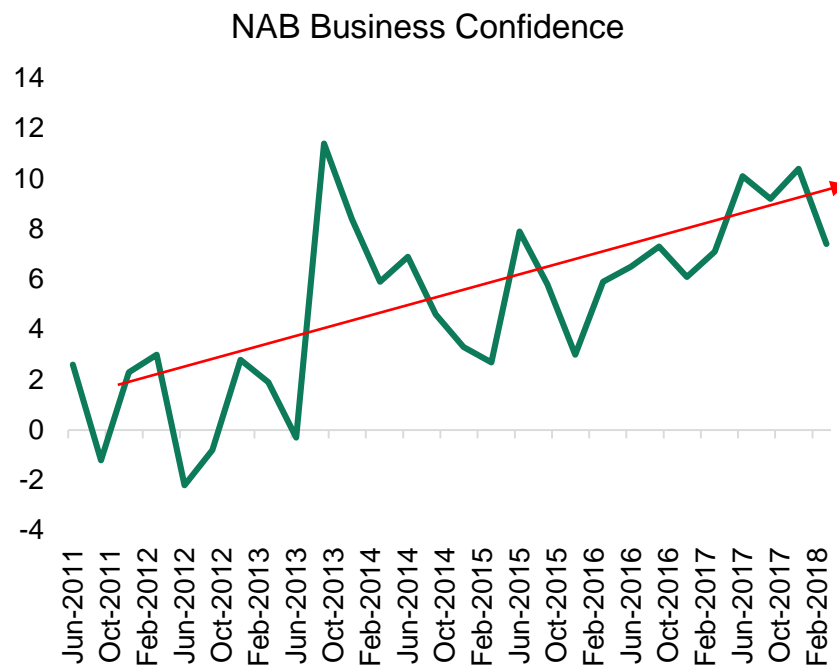
# Business confidence is up

Global PMI's at expansionary levels



Source: Bloomberg

Continued improvement in business confidence over the past 7 years



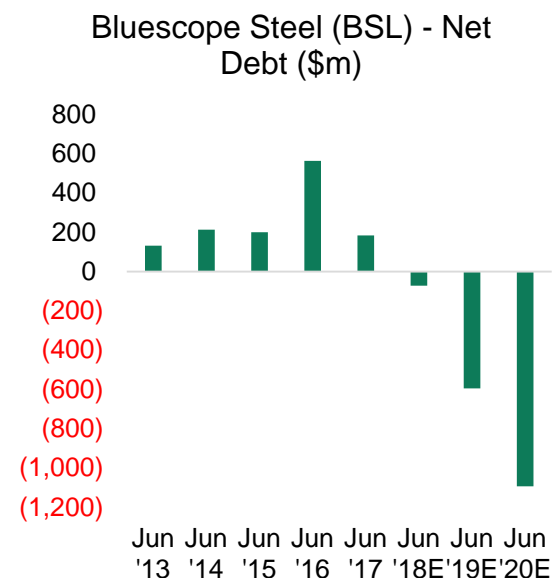
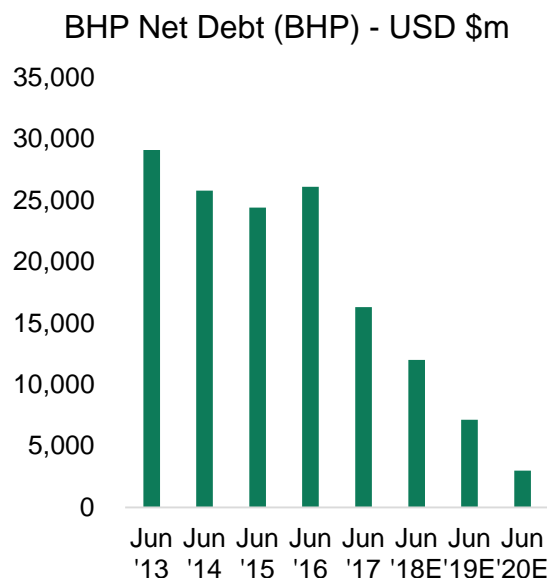
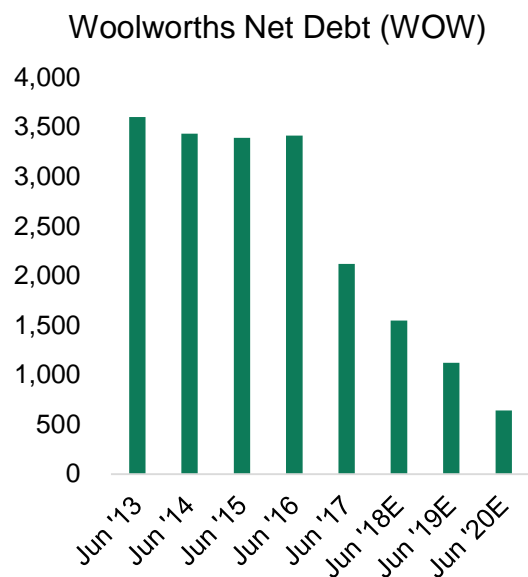
Driven by improving global conditions



THE M&A CYCLE IS HEATING UP

# Stronger balance sheets

Australia's best known companies set to rapidly reduce debt over next 3 years



Source: Firetrail, Factset

*Bluescope steel could be holding \$1bn net cash in two years!*

THE M&A CYCLE IS HEATING UP

# Implications for investors

## Recent acquisitions in Australia



October 2014 Acquisition: **+288%**



October 2015 Acquisition: **+162%**



August 2016 Acquisition: **+52%**

**JB HI-FI**

September 2016 Acquisition: **-9%**



March 2015 Acquisition: **-99%**

- High confidence + increased balance sheet firepower = increased focus on growth
- Build vs Buy economics
  - Build growth organically: 5+ year horizon
  - Buying growth: Accelerated benefits through inorganic growth
- Increased M&A activity a likely outcome

*Increased M&A will create opportunity (& risks) for investors*

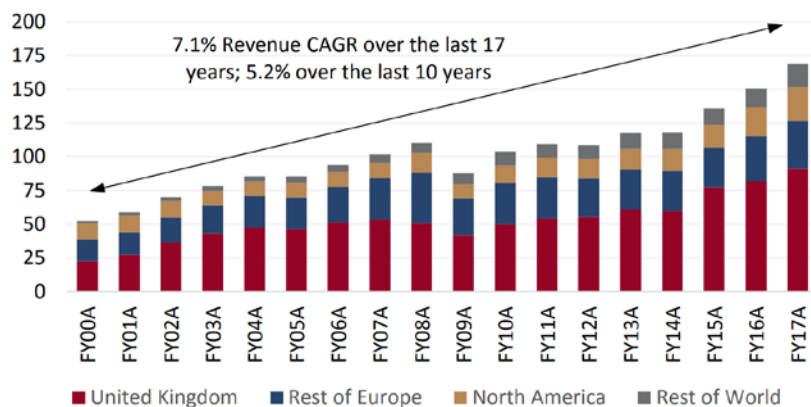
THE M&A CYCLE IS HEATING UP

# Reliance Worldwide

## John Guest Acquisition: May 2018

**Figure 3: John Guest Historical Revenue Profile**

Source: Companies House, EAP Research.



- Reliance is the global market leader in innovative plumbing solutions
- Announced acquisition of John Guest in May 2018
  - Acquired for \$1.2bn - increasing RWC revenue by 50%
- Rationale:
  - Family seller = great price
  - Product complimentary to existing suite – Brass vs plastic
  - Geographically complimentary offering synergies
- Conservatively funded

*The John Guest acquisition is M&A done right!*

# 03

*Great companies,  
bad investments*

## GREAT COMPANIES, BAD INVESTMENTS

# Telstra

### Telstra earnings estimates lowered 30% from September 2015 to March 2018

Telstra 2018 Earnings Per Share Broker Forecast Consensus



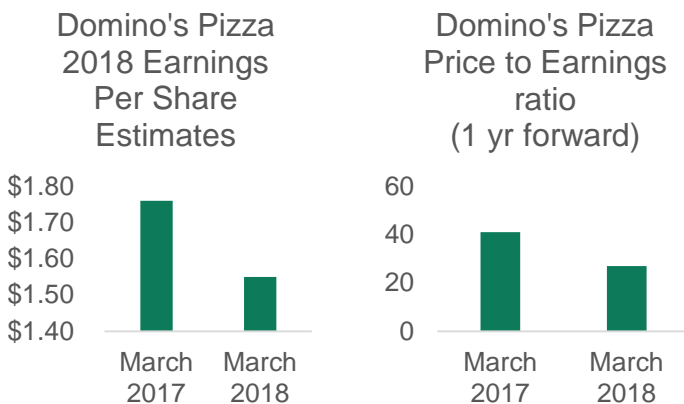
Source: Factset

- In 2015, Telstra was the darling of the Australian market
  - Key rivals had been underinvesting in their mobile networks
  - Negotiated a favourable deal on the NBN
  - Share price was at the highest point since the tech boom in 2000
- Fast forward to 2018, Telstra's share price is half of its 2015 peak
  - Competitors have reinvested in their networks
  - The NBN is a headwind
  - Dividends have been cut by a third

*Company's at the top of their game can turn out to be a bad investment*

# Beware 'market darlings'

## Domino's Pizza earnings estimates and valuation multiples have reduced



## Domino's Pizza

- Until 2017, Domino's was an ASX 200 'market darling'
- When expectations for 'market darlings' are lowered, the valuation multiple (P/E) generally falls
- Domino's has both its earnings estimates and valuation multiple reduce
  - Faced competition from online food order services
  - Franchisee wage audits
  - Slowing international sales growth
  - Earnings still forecast to grow at 20% per year
- Valuation multiple has fallen from 41x to 27x
- The Domino's share price has fallen - **47%** from its 2016 peak

*Market darlings can fall significantly when earnings expectations fall*

# Great investments, bad companies...

## Some great investments in Australia

Considered 'bad companies' at the time



### Bluescope in 2015

- **Market view:** A high cost steel producer
- **Reality:** Steel supply reductions in China & a major cost-out program
- **Share price:** +326%



### Qantas in 2014

- **Market view:** An airline price war with virgin
- **Reality:** Both airlines reduced capacity & increased profitability
- **Share price:** +410%

- Our belief is that *'every company has a price'*
- Our experience shows that *'down & out'* companies can make great investments
- When expectations for *'down & out'* companies change, two things typically occur
  1. **Earnings expectations increase** - the market gains conviction in a turnaround
  2. **Valuation multiples increase** – the market re-rates the *'cheap'* company's share price upwards
- Once these two things occur, it can result in significant positive share price performance

*In our experience, 'bad companies' can be great investments*

# 04

## *Summary*



## AUSTRALIAN HIGH CONVICTION FUND

# Performance is key

### Macquarie High Conviction Fund\*

Post-fee to 31 October 2017

Period to 31/10/17	Strategy <sup>1</sup>	ASX 200	Excess
3 years (% pa)	<b>17.3%</b>	6.9%	<b>+10.4%</b>
5 years (% pa)	<b>17.2%</b>	10.3%	<b>+6.9%</b>
Inception (% pa)	<b>10.6%</b>	6.7%	<b>+3.9%</b>

- Strong performance over more than a decade
- Outstanding upside / downside capture
- **Zenith 'Highly Recommended' – May 2018**
- Highly awarded team prior to Firetrail:

- ✓ Lonsac Manager of the Year 2016
- ✓ Zenith Manager of the Year 2017
- ✓ Canstar, SMSF manager of the year 2017
- ✓ FundSource Manager of the Year 2017 (NZ)

### Upside / downside ratio

Period to 31/10/17	Upside Capture	Downside Protection
5 years (% pa)	142.9%	82.7%

### Firetrail Australian High Conviction Fund\*

Post-fee to 29 May 2018

Actual performance <sup>2</sup>	Fund	ASX 200	Excess
Inception (%)	<b>3.76%</b>	2.00%	<b>+1.76%</b>

#### Past Performance is not a reliable indicator of future returns

\*The Firetrail Australian High Conviction Fund will employ the same strategy as was used by the same investment team that managed the Macquarie High Conviction Fund as at 24<sup>th</sup> October 2017.

1. Macquarie High Conviction Fund Post-Fee Outperformance of the S&P/ASX 200 Accumulation Index to 31 October 2017. Inception 30 Nov 2005 Source: Mercer

2. Firetrail Australian High Conviction Fund Post-Fee Performance since inception on 14 March 2018.

*Strong performance over the long-term*

## ABSOLUTE RETURN FUND

# Uncorrelated returns

### Macquarie Pure Alpha Fund

Post fee to 31 October 2017

Period to 31/10/17	Strategy <sup>1</sup>	RBA Cash	Excess
1 year (%)	<b>11.0%</b>	1.5%	<b>+9.5%</b>
2 years (% pa)	<b>14.1%</b>	1.7%	<b>+12.4%</b>
Inception (% pa)	<b>18.7%</b>	1.8%	<b>+16.9%</b>

### Firetrail Absolute Return Fund

Post fee to 29 May 2018

Actual performance <sup>2</sup>	Fund	RBA Cash	Excess
Inception (% nom)	<b>6.35%</b>	0.31%	<b>+6.04%</b>

Past Performance is not a reliable indicator of future returns

1. Macquarie Pure Alpha Fund Post-Fee Outperformance of RBA Cash Rate to 31 October 2017. Inception July 2016. Source: Mercer.

\*The Firetrail Absolute Return Fund employs the same investment approach as was used by the same investment team that managed the Macquarie Pure Alpha Fund as at 24<sup>th</sup> October 2017. 2. Firetrail Absolute Return Fund Post-Fee Performance since inception on 14 March 2018 to 31 March 2018.

- Aims to generate positive returns above RBA cash over the medium term
- **Zenith 'Recommended' rating – May 18**
- Proven track record of alpha
- Highly awarded prior to Firetrail:
  - ✓ Hedge Fund Rocks:
    - Australian Alternative Investment Fund of the Year 2017
    - Best Market Neutral Fund 2017
  - ✓ Australian Fund Manager Awards
    - Best Absolute Return Fund 2016

*Aiming to achieve positive absolute returns over the long-term*

## SUMMARY

# *High conviction investment experts*

Specialists in high  
conviction investing

1

Market themes  
creating investment  
opportunities

2

An experienced  
team with a proven  
track record

3

*Focused, unconstrained, experienced*