

# FIRETRAIL ABSOLUTE RETURN FUND

MONTHLY REPORT | SEPTEMBER 2022

## PERFORMANCE (AFTER FEES)<sup>1</sup>

	Month	Quarter	6 Months	1 Year	2 Years p.a.	3 Years p.a.	Fund inception p.a. <sup>3</sup>	5 Years p.a.	Strategy inception p.a. <sup>5</sup>
Fund <sup>2</sup>	1.16%	(5.96%)	(11.14%)	(15.26%)	(4.72%)	3.38%	1.43%	-	-
Strategy composite <sup>4</sup>	1.16%	(5.96%)	(11.14%)	(15.26%)	(4.72%)	3.38%	-	1.21%	7.98%
Benchmark	0.18%	0.44%	0.54%	0.59%	0.35%	0.39%	0.74%	0.79%	1.06%
Excess Return	<b>+0.98%</b>	<b>-6.40%</b>	<b>-11.68%</b>	<b>-15.85%</b>	<b>-5.07%</b>	<b>+2.99%</b>	<b>+0.69%</b>	<b>+0.42%</b>	<b>+6.92%</b>

1. Past performance is not a reliable indicator of future performance.

## ABOUT FIRETRAIL

Firetrail is an investment management boutique which is majority owned by the Firetrail investment team. Additionally, the investment team is invested alongside clients in the investment strategies.

## ABSOLUTE RETURN FUND

The Absolute Return Fund ("Fund") is a market neutral strategy with minimal correlation to equity market direction. It aims to generate positive returns in all market environments. The strategy is built on fundamental, deep dive research guided by the philosophy that 'every company has a price'.

## INVESTMENT OBJECTIVE

The Fund aims to outperform the RBA Cash Rate over the medium to long term (after fees).

## PORTFOLIO POSITIONING

30 SEPTEMBER 2022

Top 3 Overweight Holdings (Alphabetical)
Australia & New Zealand Banking Group Ltd
Newcrest Mining Ltd
Santos Ltd

## FUND DETAILS

Unit Prices	30 September 2022
Application Price	\$ 1.0496
Redemption Price	\$ 1.0422
NAV Price	\$ 1.0459
Fund Details	
APIR Code	WHT5134AU
Benchmark	RBA Cash Rate
Inception Date	14 March 2018
Risk/Return Profile	High
Fund Size	\$328mil
Management Fee*	1.28% p.a.
Performance Fee*	20% of outperformance above an annual Hurdle

\*Please read the Product Disclosure Statement for more details

## FUND EXPOSURE

30 SEPTEMBER 2022

	Portfolio Exposure
Long Equity	169.1%
Short Equity	-169.0%
Net Equity Exposure	0.1%

Past performance is not a reliable indicator of future performance.

The Product Disclosure Statement ('PDS') and Target Market Determination ('TMD') of the Fund are available at <https://firetrail.com/firetrail-absolute-return-fund/>.

2. Firetrail Absolute Return Fund ('Fund'). Net Fund returns are calculated based on exit price with distributions reinvested, after ongoing fees and expenses but excluding taxation. 3. Fund inception is 14 March 2018. 4. The Fund has been operating since 14 March 2018. To give a longer-term view of our performance for this asset class, we have also shown returns for the Firetrail Absolute Return Strategy Composite ('Strategy') which has been operating since 30 June 2015. Strategy performance has been calculated using the monthly returns (after fees) of the Fund from 14 March 2018 to current date, as well as the monthly returns of the Macquarie Pure Alpha Fund (after fees) between 30 June 2015 to 23 November 2017. The Fund employs the same strategy as was used by the same investment team that managed the Macquarie Pure Alpha Fund as at 23 November 2017. Firetrail has records that document and support the performance achieved as the Macquarie Pure Alpha Fund. The composite returns for the Strategy and the RBA Cash Rate (Benchmark) exclude returns between 24 November 2017 and 13 March 2018. During this period the investment team did not manage the Strategy. As such, the annualised performance periods stated are inclusive of the combined composite monthly returns, and do not include the period when the team were not managing the Strategy. For example, the annualised return over 3 years for the Strategy and benchmark are inclusive of 36 monthly performance periods available in the composite return period, excluding the period between 23 November 2017 and 13 March 2018. For additional information regarding the performance please contact us through the link on our website. Net Fund returns are in AUD terms. Net Fund returns are calculated based on exit price with distributions reinvested, after ongoing fees and expenses but excluding taxation. Past performance is for illustrative purposes only and is not indicative of future performance. 5. Strategy inception 30 June 2015.

## PORTFOLIO COMMENTARY

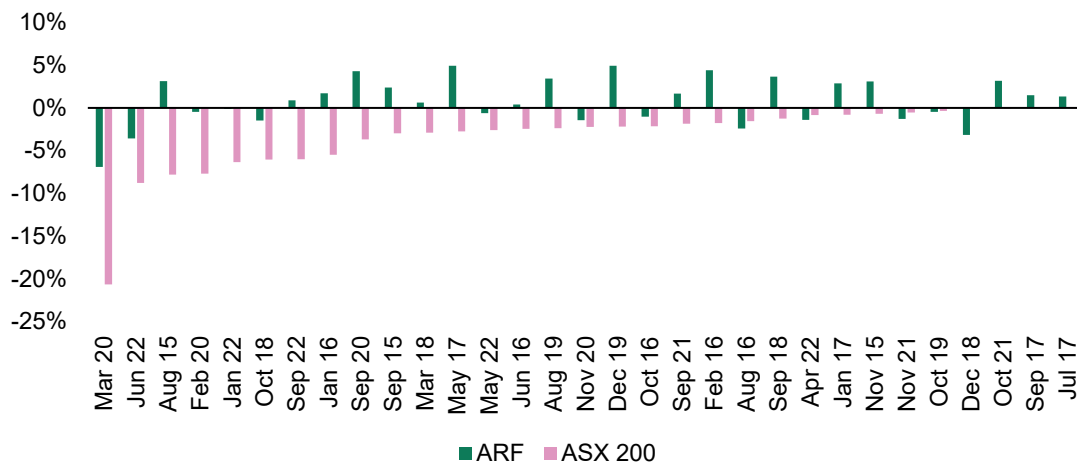
The Fund returned 1.16% (after fees) for September, outperforming the RBA Cash Rate by 0.98% and the ASX 200 which had a negative return of -6.17% for the month.

The past 9-months have been a challenging performance period for the Fund. It was pleasing that the Fund provided uncorrelated returns in September, a tough performance month for equities.

Historically, the strategy has provided good diversification from negative monthly equity market returns. Figure 1 below shows every negative ASX 200 market return since Strategy inception in 2015 in pink, from largest to smallest drawdown. The bars in green show the corresponding return of the Firetrail Absolute Return Strategy.

Historically, when the ASX 200 monthly return was negative, the Firetrail Absolute Return Strategy has delivered a positive return 58% of the time. On average, the Strategy delivered a positive return of +0.78% vs the ASX 200 average monthly drawdown of -3.38%, providing good diversification during monthly market drawdowns.

**Figure 1: Firetrail Absolute Return Strategy performance (after fees) in negative markets since inception (30 June 2015). The Fund delivered a positive return in 58% of negative ASX 200 months**



Source: Firetrail, Morningstar

*Past performance is not a guarantee of future returns.*

The Firetrail team have been very active over the past 6-months, positioning the portfolio to generate positive returns over the medium-term irrespective of equity market direction. Whilst we are disappointed in performance over the past 12-months, we are very excited by the long and short opportunities that have been made available in the recent market volatility. Below we provide more detail on contributors and detractors for the month, portfolio positioning and outlook.

## CONTRIBUTORS TO RETURNS<sup>1</sup>

The short portfolio contributed strongly to portfolio returns during September. Key contributors included short positions in travel, REITs and Technology stocks.

The long portfolio detracted from returns during the month. Key contributors included long positions in ResMed and Australia and New Zealand Banking Group (ANZ). Long positions in Santos, Origin Energy, and Virgin Money UK detracted from portfolio returns during the month.

### ResMed

ResMed outperformed as management continued to guide to a gradual easing of supply chain pressures. In addition, ResMed’s main competitor Philips was the subject of another product recall initiated by the US Food and Drug Administration. Roughly 17 million masks manufactured by Philips were found to have magnets that did not meet FDA safety standards.

1. Illustrative only and not a recommendation to buy or sell any particular security

### Origin Energy and Santos

Origin Energy and Santos underperformed as increased fears of a global recession led to a selloff in oil during September. The Brent crude price fell 9% to US\$88 per barrel. Origin underperformed as the cash flows from its Asia-Pacific LNG project are linked to the oil price. Origin's Energy Markets division is also negatively leveraged to lower energy prices due to fixed price contracts for gas and renewable inputs.

Santos confirmed that the PNG Government has submitted an offer to acquire an additional 5% interest in PNG LNG from Santos for an asset value of US\$1.4 billion. Santos has until 31 December 2022 to accept the offer, which would reduce its ownership interest to 37.5%.

## PORTFOLIO POSITIONING

The Firetrail Absolute Return Fund is a long/short portfolio of our best stock ideas. The portfolio is designed as a market-neutral alternative that provides low to no correlation with traditional equity and bond market exposures.

Overall portfolio positioning can be summarised as:

- Zero net equity market exposure and Beta (+/-0.1)
- 338% gross equity exposure evenly split across:
  - o 169% long exposure across 60 stocks that are undervalued with material earnings upside based on Firetrail's medium-term forecasts (3-year investment horizon).
  - o 169% short exposure across 147 stocks that Firetrail either expect to downgrade earnings versus market expectations, or to mitigate and hedge equity risk exposure.
- The portfolio is currently long:
  - o Value versus Growth
  - o Energy, Gold, Rate-Sensitive Financials, and high-quality Growth companies that we believe have been oversold in recent market volatility
- The portfolio is currently short:
  - o Bond Proxies, Consumer Staples, and Consumer Cyclical where we see material earnings risks and elevated expectations.
  - o A diverse number of stocks that aim to reduce macroeconomic risk exposures within the portfolio and hedge equity risk exposure to ensure uncorrelated returns.

The portfolio is expected to be driven by long and short stock selection over the medium-term, as opposed to equity market direction.

## PORTFOLIO CHANGES AND OUTLOOK

Key portfolio changes over the past quarter include:

- Increased exposure to companies that we believe have been oversold in recent market volatility and represent exceptional medium-term opportunities. These include companies in the Energy, Gold, Insurance and Healthcare sectors.
- Decreased exposure to unprofitable Growth or Technology companies that we believe require additional capital to fund future growth. Which has funded an increase in portfolio exposure to high-quality profitable Growth companies that have been sold-off in the recent market volatility.
- Decreased net exposure to smaller companies, predominantly by increasing our short positions in smaller companies. Firetrail have maintained or increased our long exposures to smaller companies that we believe have been materially oversold in recent market conditions – such as Megaport and Estia Health.

The portfolio remains well balanced across style, sector and thematic exposures. We have high conviction in the outlook for our long and short positions to generate meaningfully positive returns over the next 12 to 24 months.

Whilst the recent macroeconomic volatility has been challenging for fundamental stock pickers like Firetrail, we believe it has created a material opportunity to increase our stock specific risk in the portfolio to drive future outperformance.

## ONE INTERESTING THING THAT HAPPENED THIS MONTH...

The UK dominated headlines in September after new Prime Minister Liz Truss’s government demonstrated a willingness to do ‘whatever it takes’ to kickstart economic growth.

The government released a ‘mini-budget’ which included policies such as scrapping the highest income tax rate, cuts to stamp duty, support for household energy bills, and much more.

Out of fears the government would have to raise significant amounts of debt to fund the proposed policies, the UK government bond (also known as ‘gilts’) market and the Pound sold off heavily. Yields on UK 10-year gilts spiked a remarkable 1% to over 4.5% after the announcement.

The turmoil was more reflective of an emerging market rather than a developed powerhouse which was once the world’s financial centre. The IMF even warned that the spending was irresponsible, given the high levels of inflation we are seeing in the UK and the rest of the world at the moment.

**Figure 1:** UK government bond yields spiked sharply after Prime Minister Liz Truss announced a ‘mini-budget’ heavy on government spending and tax cuts (10-year UK gilts spot yields)



Source: Firetrail, FactSet

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Links to the Product Disclosure Statement: [WHT5134AU](#)

Links to the Target Market Determination: [WHT5134AU](#)

For historic TMD's please contact Pinnacle client service Phone 1300 010 311 or Email [service@pinnacleinvestment.com](mailto:service@pinnacleinvestment.com)

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General enquiries 1300 010 311

Existing client enquiries 1300 360 306

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