

FIRETRAIL ABSOLUTE RETURN FUND

MONTHLY REPORT | FEBRUARY 2023

PERFORMANCE (AFTER FEES)¹

	Month	Quarter	1 Year	3 Years p.a.	Fund inception p.a. ³	5 Years p.a.	7 Years p.a.	Strategy inception p.a. ⁵
Fund ²	1.32%	(0.30%)	(16.60%)	2.09%	0.93%	-	-	-
Strategy composite ⁴	1.32%	(0.30%)	(16.60%)	2.09%	-	0.92%	4.05%	7.25%
Benchmark	0.25%	0.77%	1.77%	0.69%	0.92%	0.91%	1.12%	1.17%
Excess Return	+1.07%	-1.07%	-18.37%	+1.40%	+0.01%	+0.01%	+2.94%	+6.08%

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 28 FEBRUARY 2023

Top 3 Overweight Holdings (Alphabetical)
CSL Ltd
Newcrest Mining Ltd
Santos Ltd

FUND DETAILS

Unit Prices	28 February 2023
Application Price	\$1.0301
Redemption Price	\$1.0229
NAV Price	\$1.0265
Fund Details	
APIR Code	WHT5134AU
Benchmark	RBA Cash Rate
Inception Date	14 March 2018
Risk/Return Profile	High
Fund Size	\$305mil
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 28 FEBRUARY 2023

	Portfolio Exposure
Long Equity	186.2%
Short Equity	-186.1%
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 1.32% (after fees) for the month ending 28 February 2023, outperforming the RBA Cash Rate by 1.07%.

CONTRIBUTORS TO RETURNS

Positive contributors to monthly returns included long positions in Newcrest Mining, Origin Energy, and The Lottery Corporation. Detractors included long positions in Domino's Pizza Enterprises, Lendlease, and Lynas Rare Earths. We discuss each further in our commentary below.

POSITIVE CONTRIBUTORS

Newcrest Mining

Newcrest Mining outperformed during the month despite a weaker gold price driving a sell-off in gold stocks. Newcrest rejected a takeover bid from Newmont, the world's largest gold producer, early in the month. The market viewed this positively given the possibility of a higher bid. We see material value in Newcrest's low-cost, long-life gold assets and believe significant value can be realised through a Newmont takeover.

Origin Energy

Origin Energy outperformed during the month. After a number of delays to the due diligence process and a government cap on the gas price, the market had begun to heavily discount the chance that the \$9.00 per share non-binding takeover bid from EIG and Brookfield would proceed. However, the EIG/Brookfield consortium returned in late February with only a modestly revised proposal of \$8.90 per share, driving significant outperformance in the Origin share price.

The Lottery Corporation

The Lottery Corporation outperformed after reporting a very strong 1H23 result, with 8% revenue growth and 16% EBITDA growth. Outlook comments were also positive, with future revenue growth expected to be boosted by increases to lottery ticket prices and commissions.

NEGATIVE CONTRIBUTORS

Domino's Pizza Enterprises

Domino's Pizza Enterprises underperformed during February after reporting a weak 1H23 result and providing very subdued comments on the outlook. The pricing changes Domino's has made to offset higher costs appear to have had a greater negative impact on volumes than expected, particularly for delivery customers. The withdrawal of FY23 guidance less than three months after reaffirming it with a capital raising also drew management credibility into question.

Lynas Rare Earths

Lynas Rare Earths shares underperformed as its renewed Malaysian operating licence confirmed that it would still be required to cease cracking and leaching activities by July 2023. While Lynas confirmed that its Kalgoorlie plant remains on track to start up before this date, the market became more cautious on Lynas' ability to execute this transition without curtailing production.

St Barbara

St Barbara underperformed the broader market in sympathy with the gold price which fell by USD \$100 per ounce over the month. In addition, the merger with Genesis Minerals was thrown into doubt after St Barbara disclosed a bad debt provision and the requirement for debt covenants to be waived. On a medium-term view, we see compelling rationale for the merger and expect it to proceed.

PORTFOLIO POSITIONING

The Firetrail Absolute Return Fund is a market neutral portfolio (long/short) with zero net market exposure and beta (+/- 0.1) to ensure Fund performance is uncorrelated to equity market direction. The Fund is driven by our best long and short ideas. Overall, we see the portfolio as follows:

The long portfolio can be summarised as:

- 186.2% long exposure across 40-60 stocks with upside based on our medium-term earnings forecasts.
- Overweights include:
 - Energy companies exposed to commodities where supply is constrained in the medium term, such as Santos and Incitec Pivot.
 - Commodity companies exposed to decarbonisation such as Mineral Resources with attractive cost positions and strong growth.
 - Market leaders including ResMed, SEEK and James Hardie Industries who are well placed to strengthen their competitive position through the cycle.
 - Financials with leverage to interest rate rises including QBE Insurance, ANZ and Virgin Money UK.
 - Undervalued companies with defensive attributes including Newcrest Mining and The Lottery Corporation.

The short portfolio can be summarised as:

- 186.1% short exposure across a diversified portfolio of earnings shorts and risk-reducing shorts
- Earnings shorts aim to profit from companies that downgrade near term earnings. The current market is creating heightened opportunities as companies deal with rising costs and easing demand at a time of peak margins.
- Risk-reducing shorts offset equity market exposure and control portfolio risk such as style, size, sector, and thematic biases to ensure returns are driven by stock specific factors.
- The short portfolio is overweight consumer cyclicals, and expensive bond proxies where we see material near term earnings risks.

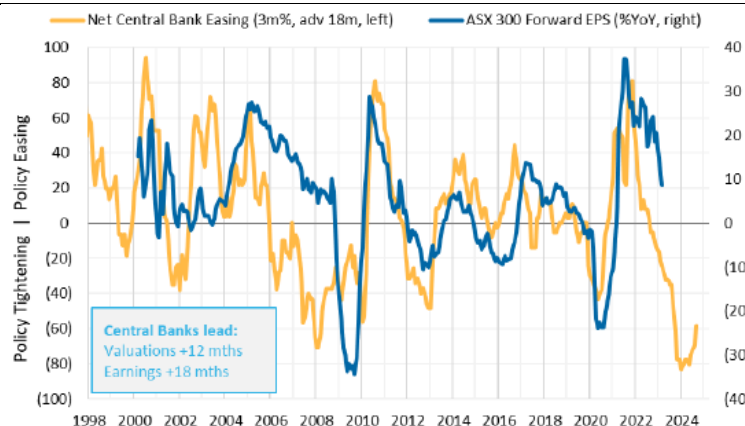
ONE INTERESTING THING THAT HAPPENED THIS MONTH...

We saw another eventful Australian reporting season in February. Overall, downgrades outpaced upgrades by 2.6x. Despite this, earnings expectations for the Australian market fell less than 1%. Consensus still expects 2.5% earnings per share growth in FY23. We remain cautious on the outlook for earnings through CY23 given tighter monetary policy.

Figure 1 shows that ASX earnings downgrades typically follow central bank tightening on an 18-month lag. The more challenging outlook for earnings is being further exacerbated by:

- High inflation is starting to impact corporate margins. ASX earnings are down 7-8% from the FY22 peak despite revenues being higher.
- COVID tailwinds are rolling off. The one-off reopening trade that shielded sectors such as retail and travel is now in the rear view.
- Interest costs are rising for indebted companies. We expect this to continue in FY24.

Figure 1: ASX earnings (blue line) downgrades typically follow central bank tightening (yellow line – lagged 18-months) on an 18-month lag.



Source: Factset, Macquarie Research, March 2023

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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

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