

FIRETRAIL ABSOLUTE RETURN FUND

MONTHLY REPORT | MAY 2023

PERFORMANCE (AFTER FEES)¹

	Month	Quarter	1 Year	3 Years p.a.	5 Years p.a.	Fund inception p.a. ³	7 Years p.a.	Strategy inception p.a. ⁵
Fund ²	3.92%	4.13%	(7.30%)	0.45%	0.35%	1.67%	-	-
Strategy composite ⁴	3.92%	4.13%	(7.30%)	0.45%	0.35%	-	3.58%	7.57%
Benchmark	0.32%	0.91%	2.65%	0.97%	1.03%	1.05%	1.18%	1.25%
Excess Return	+3.60%	+3.22%	-9.95%	-0.52%	-0.69%	+0.62%	+2.41%	+6.32%

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 – 31 MAY 2023

Top 3 Overweight Holdings (Alphabetical)
Newcrest Mining Ltd
Origin Energy Ltd
Santos Ltd

FUND DETAILS

Unit Prices	31 May 2023
Application Price	\$1.0725
Redemption Price	\$1.0651
NAV Price	\$1.0688
Fund Details	
APIR Code	WHT5134AU
Benchmark	RBA Cash Rate
Inception Date	14 March 2018
Risk/Return Profile	High
Fund Size	\$296mil
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 – 31 MAY 2023

	Portfolio Exposure
Long Equity	169.3%
Short Equity	-173.3%
Net Equity Exposure	-4.0%

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/>.

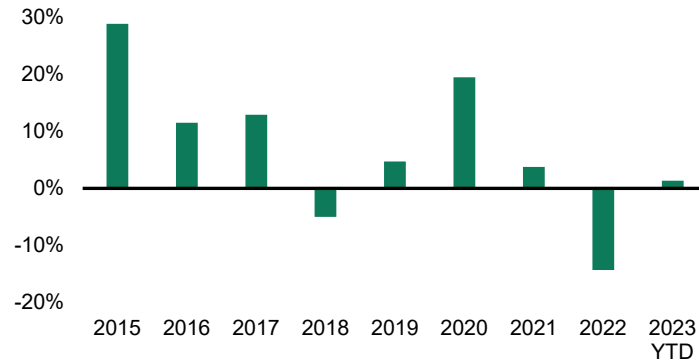
2. Firetrail Absolute Return Fund ('Fund'). Net Fund returns are calculated based on exit price with distributions reinvested, after ongoing fees and expenses but excluding taxation. 3. Fund inception is 14 March 2018. 4. The Fund has been operating since 14 March 2018. To give a longer-term view of 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 3.92% for the month ending 31 May 2023, outperforming the RBA Cash Rate by 3.60%. The S&P/ASX 200 Accumulation Index declined -2.53% during the month.

2022 was a challenging performance year as highlighted in Figure 1 below. But we remain confident in the outlook for the portfolio to deliver meaningful positive returns over the medium-term, irrespective of equity market movements.

Figure 1: Firetrail Absolute Return Strategy composite returns by calendar year (after fees)



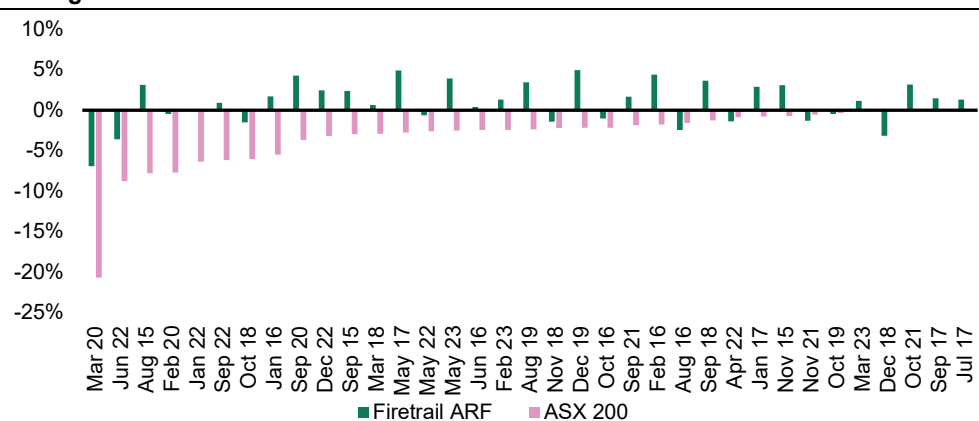
Source: Firetrail, Morningstar, June 2023.

We believe the portfolio has now adapted to the market changes that caused the underperformance in 2022 (particularly between March 2022 to August 2022). Below are a few key reasons that give us confidence in the outlook for the portfolio from here:

- Since September 2022, the Fund has delivered a positive return in all months where the ASX 200 return was negative (September 2022, December 2022, February 2023, March 2023, and May 2023).
- The Fund has reduced net exposure to small companies, which was a contributor to underperformance in 2022, but retained long exposure to our best small cap ideas. This includes companies like Estia Health and Silk Laser Clinics which are delivering meaningful positive returns.
 - In addition, Firetrail are actively allocating to new small cap ideas, including pre-IPO opportunities. But it is a high hurdle for inclusion in the portfolio. We have ensured that our long exposure to small companies is offset by fundamental and risk short positions to retain a net neutral exposure given current market conditions.

Despite the tough 2022 period, Figure 2 below shows that the Fund has delivered uncorrelated, positive returns in 66% of monthly observations where the ASX 200 return has been negative. Providing uncorrelated returns in tough market conditions through time.

Figure 2: Firetrail Absolute Return Strategy performance (after fees) in negative markets since inception (30 June 2015). The Fund delivered a positive return in 66% of negative ASX 200 months



Source: Firetrail, Morningstar, June 2023

Past performance is not a guarantee of future returns.

CONTRIBUTORS TO RETURNS

Positive contributors to monthly returns included long positions in Allkem, Lynas Rare Earths, and James Hardie Industries. Detractors included long positions in Newcrest Mining, oOh!Media, and Ramsay Health Care.

POSITIVE CONTRIBUTORS

Allkem

Allkem and Livent Corporation agreed to an all stock \$11 billion merger in May. The combined group will benefit from larger scale, operating and capital synergies given the proximity of assets in Argentina and Canada. Livent's established position in the US should lead to a higher price multiple on Allkem's assets. The deal is expected to close by end of 2023.

Lynas Rare Earths

Lynas Rare Earths outperformed during the month. The Malaysian Government extended the deadline for Lynas to cease cracking and leaching in the country by six months to 1 January 2024. The extension is significant as it allows Lynas more time to transition to its new facility currently being constructed in Kalgoorlie, WA.

James Hardie Industries

James Hardie outperformed in May after reporting an in-line FY 2023 result and initiating 1Q 2024 profit guidance 10-15% ahead of consensus expectations. Management did not explicitly guide to full-year earnings, but outlined a number of scenarios for North America margins if volumes weaken. The market took comfort from the fact that James Hardie expects to maintain margins above 25% even if volumes fall by 20%.

NEGATIVE CONTRIBUTORS

Newcrest Mining

Newcrest shares underperformed in May. The US 10-year bond yield rose 20 basis points and the US dollar strengthened 3%, both negative for the gold price. On 15th May, Newcrest entered a binding scheme implementation deed with Newmont on previously agreed terms. The shareholder vote will be held in September or October, with scheme completion expected before the end of 2023.

oOh!Media

oOh!Media underperformed in May following a disappointing trading update. oOh!Media lost market share due to the ramp of competitor QMS's newly revamped City of Sydney contract. The company believes market share will recover through the year as the hype of the new contract subsides and advertisers refocus on return on investment. Outdoor advertising continues to outperform other media categories due to the lagged recovery of the sector post-COVID lockdowns.

Ramsay Health Care

Ramsay Health Care's 3Q 2023 update illustrated a continued recovery in surgical volume trends across Australia, the UK and France. However, earnings margins were below expectations due to a slower January than usual and ongoing issues around the availability of labour. The March quarter is a seasonally soft period for profits so we don't believe the margin shortfall should be extrapolated across the rest of 2023.

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 the equity market. The Fund is driven by our best long and short ideas.

The long portfolio can be summarised as:

- 169.3%¹ 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 with attractive cost positions and strong growth, such as Mineral Resources, Allkem and Lynas Rare Earths.
 - 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, Medibank Private and Suncorp.
 - Undervalued companies with defensive attributes including Newcrest and The Lottery Corporation.

¹ Note: We have excluded Origin Energy from the long exposure calculation given an M&A transaction is in progress and the share price is not expected to be correlated to equity markets.

The short portfolio can be summarised as:

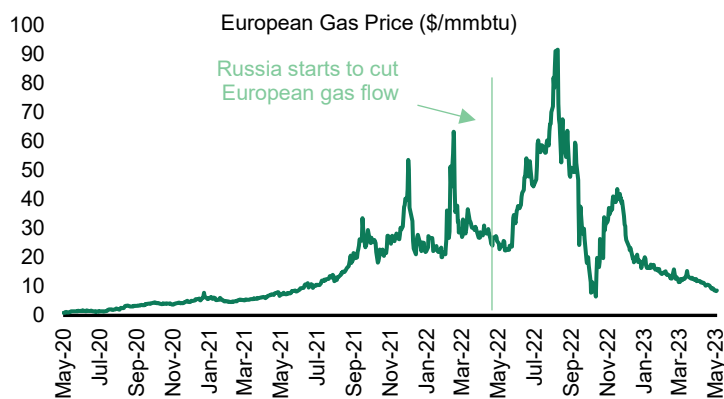
- 173.3% short exposure across a diversified portfolio of earnings shorts and risk-reducing shorts
- Earnings shorts aim to profit from companies that downgrade near term earnings. The current market is creating heightened opportunities as companies deal with rising costs and easing demand at a time 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 banks, large cap iron ore miners and expensive bond proxies where we see material near term earnings risks.

ONE INTERESTING THING THAT HAPPENED THIS MONTH...

Global energy prices soared in 2022, buoyed by the Russia-Ukraine conflict. However, prices have moderated throughout 2023. European gas prices, which were the most impacted by Russia’s decision to cut off pipeline gas in 2022, have fallen 90% from their August 2022 peak. The reasons are well known: 1) a mild European winter meant demand for heating was lower than expected; and 2) soft industrial demand has led to near-full storage levels, resulting in excess supply.

Despite the short-term relief, we maintain the view that Europe’s energy complex remains fragile. With Russian gas supply likely to remain impaired, a near-term demand shock will likely cause another squeeze higher in gas prices.

Figure 3: European gas prices have cooled from their 2022 peaks. However, the market remains vulnerable to further price shocks



Source: Factset, Firetrail

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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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General enquiries 1300 010 311

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