FIRETRAIL AUSTRALIAN HIGH CONVICTION FUND

MONTHLY REPORT | SEPTEMBER 2021

PERFORMANCE (AFTER FEES)

	Month	Quarter	6 Months	1 Year	2 Years p.a.	3 Years p.a.	Fund inception p.a.[2]	5 Years p.a.	7 Years p.a.	10 Years p.a.	Strategy inception p.a.[4]
Fund[1]	-1.49%	3.22%	8.40%	37.89%	11.78%	7.95%	7.73%	-	-	-	-
Strategy composite[3]	-1.49%	3.22%	8.40%	37.89%	11.78%	7.95%	-	11.50%	12.19%	10.81%	10.07%
Benchmark	-1.85%	1.71%	10.14%	30.56%	8.27%	9.65%	10.15%	11.41%	8.97%	9.39%	7.51%
Excess Return	**+0.37%**	**+1.51%**	**-1.75%**	**+7.33%**	**+3.50%**	**-1.70%**	**-2.42%**	**+0.09%**	**+3.22%**	**+1.42%**	**+2.56%**

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.

AUSTRALIAN HIGH CONVICTION FUND

The Australian High Conviction Fund (“Fund”) is a concentrated portfolio (approx. 25 companies) of our most compelling equity ideas. 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 ASX200 Accumulation Index over the medium to long term.

PORTFOLIO POSITIONING 30 SEPTEMBER 2021

Top 3 Overweight Holdings (Alphabetical)
Newcrest Mining
Oil Search
Virgin Money UK

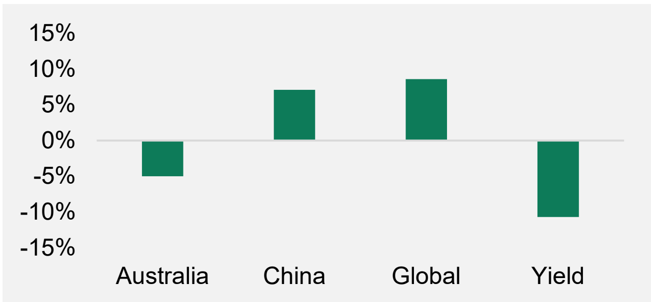
FUND DETAILS

Unit Prices	30 September 2021
Application price	$ 1.2438
Redemption Price	$ 1.2400
NAV Price	$ 1.2419
Fund Details	
APIR Code	WHT3810AU
Benchmark	S&P/ASX 200 Accumulation Index
Inception date	14 March 2018
Number of Holdings	27
Fund size	$622mil
Management fee*	0.90% p.a.
Performance fee*	15% of outperformance above an annual Hurdle

*Please read the Product Disclosure Statement for more details

THEMATIC POSITIONING 30 SEPTEMBER 2021

Relative to the Benchmark



Past performance is not a reliable indicator of future performance.

1. Firetrail Australian High Conviction Fund (‘Fund’). Net Fund returns are calculated based on exit price with distributions reinvested, after ongoing fees and expenses but excluding taxation. 2. Fund inception is 14 March 2018. 3. 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 Australian High Conviction Strategy Composite (‘Strategy’) which has been operating since 29 November 2005. 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 High Conviction Fund (after fees) between 29 November 2005 to 23 November 2017. The Fund employs the same strategy as was used by the same investment team that managed the Macquarie High Conviction Fund as at 23 November 2017. Firetrail has records that document and support the performance achieved as the Macquarie High Conviction Fund. The composite returns for the Strategy and the S&P/ASX 200 Accumulation Index (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. 4. Strategy inception 29 November 2005.

PORTFOLIO COMMENTARY

The Fund returned 3.22% for the quarter ending 30 September 2021, outperforming the ASX200 Accumulation Index by 1.51%. For the month of September, the Fund returned -1.49% outperforming the benchmark by 0.37%.

COMPANY & INDUSTRY NEWS

The Australian equity market finished flat over the quarter, with a modest rally in July and August unwinding in September. Key themes were the effectiveness of vaccination in combating the delta variant, the extent of China's growth slowdown, and progressively more hawkish central banks. Australian and US 10-year yields declined 30-40bps over July and August but recovered back to June levels by the end of September. Resource stocks were the key underperformers, largely driven by a slowdown in China's growth and fears of knock-on effects from the distressed property developer Evergrande, one of China's biggest borrowers.

Positive contributors to the Fund's performance included Oil Search, Qantas and Nufarm. Detractors included Bluescope, Newcrest and Resmed. We discuss each further in our commentary below.

CONTRIBUTORS

Oil Search

Energy stocks were strong performers during the month due to an improved global demand outlook and a continued rational approach to supply from OPEC. Following a period of exclusive due diligence, the Boards of Oil Search and Santos agreed to a merger on previously disclosed terms. Confirmed cost synergies of $90-115m were in line with consensus expectations.

Qantas

Qantas outperformed along with global airlines as the reopening thematic regained momentum. The capacity roadmap that Qantas outlined at its results in August was also supported by the timelines and vaccinations milestones outlined by the Premiers of NSW and Victoria in September.

Nufarm

The demand outlook for Nufarm's products has improved over recent months, supported by higher soft commodity prices and improved weather conditions across most of Nufarm's key regions.

DETRACTORS

Bluescope

Bluescope's share price was impacted by China growth concerns and planned capacity additions announced by two competitors. New capacity is never good news but appears manageable in the context of the global demand recovery and an expectation of steel price moderation.

Newcrest

A weaker gold price and a more hawkish outlook from the Fed drove Newcrest's underperformance during the month. The results from pre-feasibility studies at Lihir and Red Chris were pushed back but are expected in early-mid October.

Resmed

Australian healthcare stocks underperformed the index by ~3% in September as markets priced in higher inflation. Resmed also highlighted that global supply chain shortages are having some short-term impacts on production but are expected to be remedied by the end of 2021.

QBE INSURANCE DEEP DIVE

QBE is a position we established during April/May 2021 and is now one of the top five holdings in the Fund. There are three key reasons why we believe QBE is an attractive investment:

1) The global insurance pricing environment is the most rational it has been in over a decade;
2) QBE has made substantial improvements to its underlying business over recent years; and
3) Balance Sheet and reserves are now in a much stronger position.

The hard pricing cycle continues to roll on

Prices for business insurance have been increasing by at least high single-digits for the past three years across most major regions. Higher pricing has been driven by:

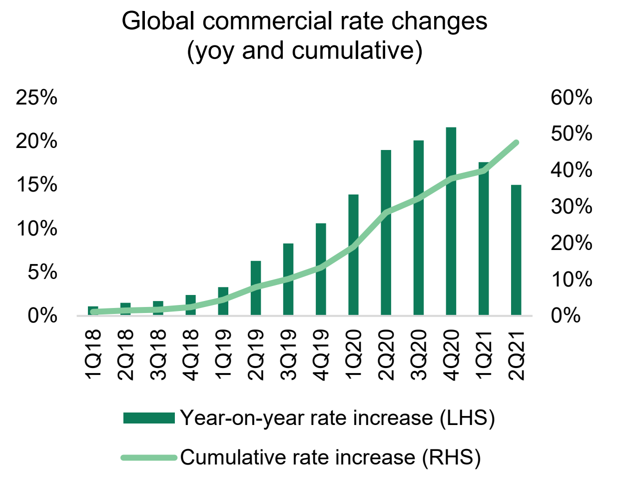
- The need to recover losses from substantial catastrophes and COVID;
- Less buffers in reserves held against prior year claims;
- Falling interest rates reducing income earned on assets backing reserves; and
- Withdrawal of capacity from the market.

We believe the withdrawal of capacity has been a key driver because it has taken multiple forms. Insurers have pulled back from classes of business that are not delivering adequate returns, third party capital has declined due to large incurred losses, and markets such as Lloyd's in the UK have been restricting the growth of insurers that are not profitable.

While there has been some moderation in the pace of year-on-year increases, we believe pricing is still increasing above inflation in the US, Europe and Australia. As illustrated by Figure 1, cumulative price increases over the past three years are now approaching 50%.

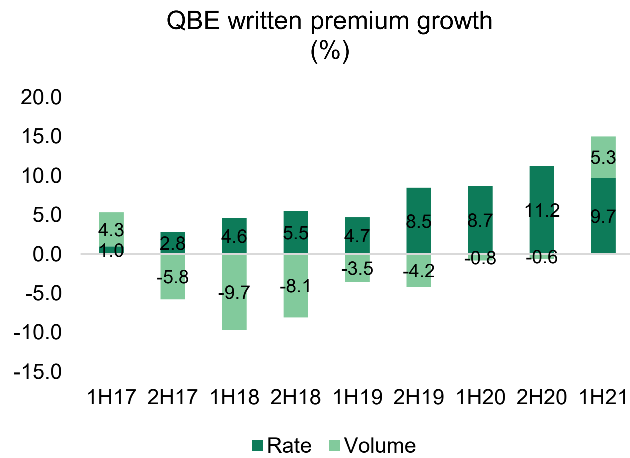
QBE has been a beneficiary of the rising price environment. As seen in Figure 2, QBE has reported average rate increases of 9.5% pa over the past two years, and a return to volume growth in the most recent half.

Figure 1. Cumulative price increases over the past three years are now approaching 50%



Source: Marsh Global Insurance Market Index, Firetrail, September 2021

Figure 2. QBE has been a beneficiary of the increasing rate environment



Source: MBS, Firetrail, September 2021

QBE's underlying performance continues to improve

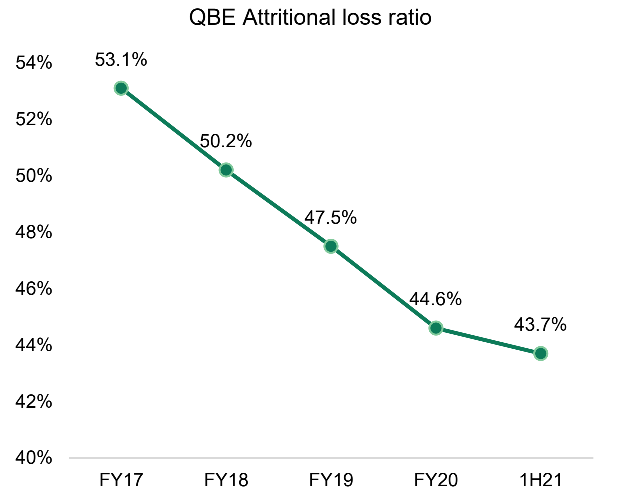
Over the past five years, QBE has been focused on integrating granularity and accountability into its pricing process, selling problem portfolios, and simplifying its operating model.

Combined with the upwards pricing cycle outlined above, QBE's self-help efforts have driven consistent improvements in underlying profitability. The "attritional loss ratio", which measures day-to-day claims as a percentage of premium (i.e. lower is better), has steadily declined since FY17 as seen in Figure 3.

Due to the lagged nature of how written premium is earned through the P&L, we expect further margin improvement to emerge over the short-medium term as the price increases of 2019-21 take effect. We estimate this will help QBE achieve a double-digit ROE in FY22 and sustain mid-teens EPS growth for the next couple of years.

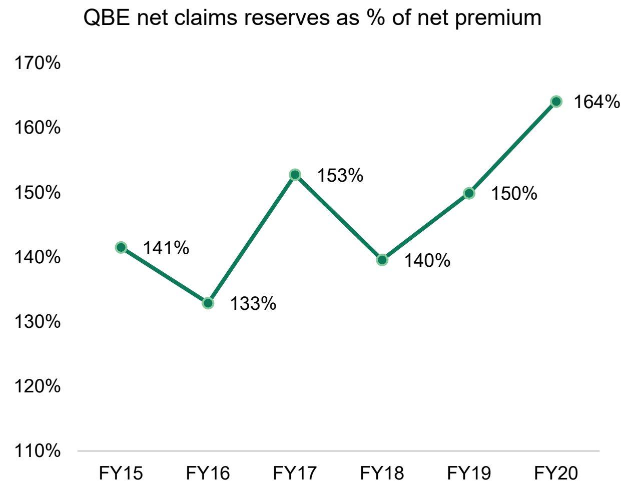
Another area of improvement for QBE has been the strength of the reserves it holds on its balance sheet. While the numbers in Figure 4 are a rather crude measure, it shows QBE's claims reserves as a percentage of premium are at their highest point in over five years.

Figure 3. Attritional loss ratio has steadily declined since FY17



Source: Marsh Global Insurance Market Index, Firetrail September 2021

Figure 4. QBE's claims reserves as a percentage of premium are at the highest point in over five years



Source: MBS, Firetrail, September 2021

What are the risks? Insurance is an unpredictable business, and as such there are always risks with an investment like QBE. Front of mind for us includes:

1. The potential negative impact of inflation on claims reserves;
2. Rebasing risk associated with the new CEO who commenced on 1 September; and
3. Higher losses from 2021 catastrophes, namely Hurricane Ida.

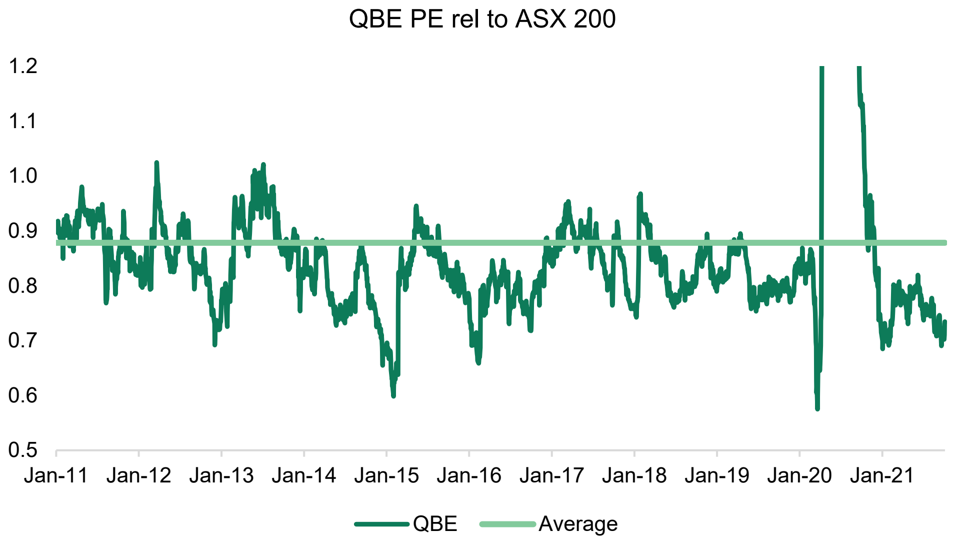
Insurers are negatively impacted by unexpected increases in inflation on the liability side of the balance sheet. This can be offset by the significant positive leverage insurers have to interest rate increases on their asset portfolios which are largely invested in fixed income. However, there are risks of a mismatch if inflation runs well ahead of interest rate rises. This dynamic is one of the reasons why the higher inflation / higher interest rate thematic has benefitted stocks like Computershare in recent months but has left QBE behind. We continue to closely monitor macro data and industry feedback for signs of breakouts of claims inflation, but currently believe it can be adequately offset by higher interest rates and the impact of multi-year price increases.

More conservative balance sheet and P&L setting are always a consideration when a new CEO commences but given the significant remediation and reserve strengthening that has occurred in recent years, we expect any rebasing from the new CEO to be manageable. While 2021 looks likely to be another poor year for catastrophe losses, we don't think this should be completely capitalised into the share price.

Valuation

QBE is currently trading at a 27% discount to the ASX200 on a 12-month forward basis, 16% below its ten-year average. For the majority of the past decade, commercial insurance pricing has been falling and QBE has been managing a number of company-specific issues. We believe the current valuation presents significant value when considered in the context of a far more supportive industry backdrop and a greatly simplified business.

Figure 5. QBE is currently trading at a 27% discount to the ASX200 on a 12-month forward basis, 16% below its ten-year average



Source: Factset, Firetrail September 2021

PORTFOLIO POSITIONING AND CHANGES

Material changes made to the portfolio over the September quarter include:

- Initiated a position in Woodside due to increased conviction in the outlook for energy stocks and an improved business risk profile post the merger with BHP's petroleum business.
- Initiated a below-index position in BHP to reduce our iron ore underweight exposure.
- Increased our holdings in Aristocrat, Xero and QBE to capitalise on short-term underperformance.
- Trimmed Virgin Money UK and Resmed following recent outperformance.
- Exited IAG following the August result as it appears that the profitability turnaround will take longer than we originally anticipated.

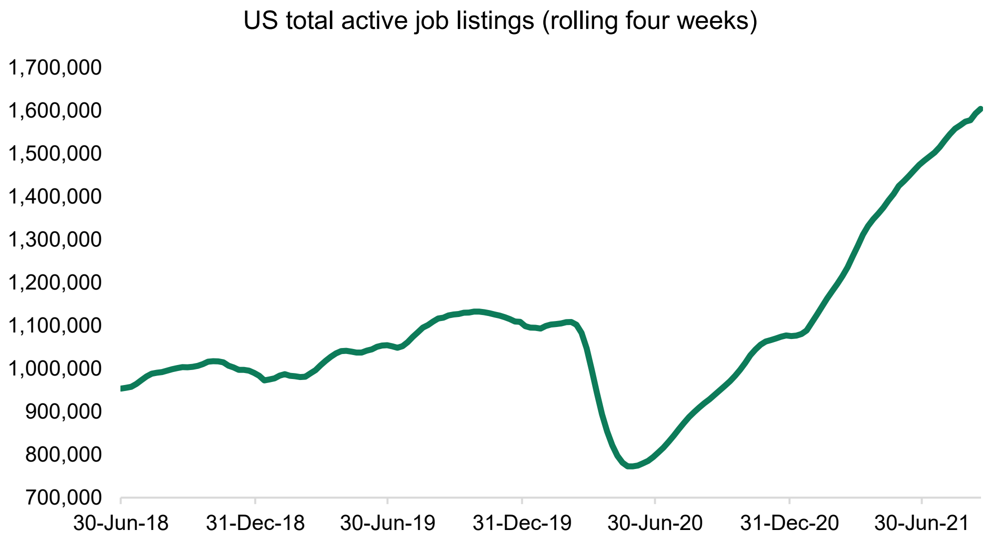
Current portfolio positioning can be summarised as follows:

- Highly concentrated with an 80% active share
- Overweight
  - Re-opening trades like Qantas, Aristocrat and the energy sector, where competitive dynamics have improved post COVID.
  - Base metal and EV materials where supply won't be able to keep up with demand over the medium-term.
  - Housing plays like Bluescope and James Hardie who are benefitting from strong demand while taking market share in their categories.
  - Non-bank financials including QBE and Medibank.
  - Undervalued defensive companies including Newcrest, Telstra and Crown.
- No holding in Australian banks and underweight iron ore where we don't see compelling opportunities.

ONE INTERESTING THING THAT HAPPENED THIS MONTH

The evidence that Australia is about to enter one of the tightest jobs markets it has ever seen is mounting. The US is leading the world out of COVID, and job trends continue to strengthen. During September, US job listings were 40% above pre-COVID levels. We heard a broad range of companies including Vale Resorts, Fedex and Delta Airlines speak about an inability to find staff and refer to ~20% pay increases for entry level roles. During the month, we added to our Seek position to increase our exposure to this thematic in Australia.

Figure 6. During September, US job listings were 40% above pre-COVID levels



Source: Factset, Firetrail, September 2021

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General enquiries 1300 010 311

Existing client enquiries 1300 360 306

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