FIRETRAIL AUSTRALIAN HIGH CONVICTION FUND

MONTHLY REPORT | MARCH 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.	10 Years p.a.	Strategy inception p.a.[5]
Fund[2]	(0.56%)	3.71%	(2.99%)	19.07%	5.54%	-	-	-	-
Strategy composite[4]	(0.56%)	3.71%	(2.99%)	19.07%	-	6.09%	8.63%	10.85%	9.19%
Benchmark	(0.16%)	3.46%	0.10%	16.52%	7.97%	8.69%	8.87%	8.97%	7.10%
Excess Return	**-0.40%**	**+0.25%**	**-3.09%**	**+2.55%**	**-2.43%**	**-2.60%**	**-0.24%**	**+1.88%**	**+2.09%**

1. Past performance is not indicative 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.

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 ASX 200 Accumulation Index over the medium to long term (after fees).

FUND DETAILS

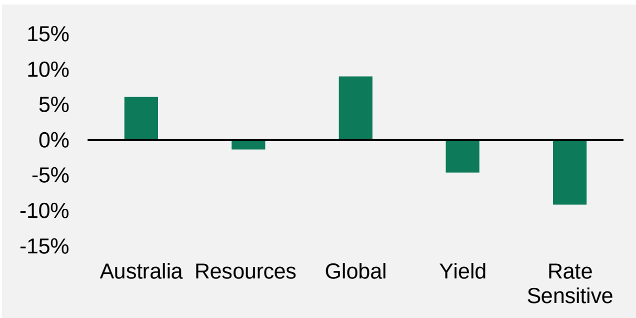
Unit Prices	31 March 2023
Application price	$1.1857
Redemption Price	$1.1821
NAV Price	$1.1839
Fund Details	
APIR Code	WHT3810AU
Benchmark	S&P/ASX 200 Accumulation Index
Inception date	14 March 2018
Risk/Return Profile	High
Number of Holdings	27
Fund size	$657mil
Management fee*	0.90% p.a.
Performance fee*	15% of outperformance above an annual Hurdle

*Please read the Product Disclosure Statement for more details

PORTFOLIO POSITIONING – 31 MAR 2023

Top 3 Overweight Holdings (Alphabetical)
Newcrest Mining Ltd
QBE Insurance Group Ltd
Santos Ltd

THEMATIC POSITIONING – 31 MAR 2023



Source: Firetrail. Relative to the Benchmark

Past performance is not a reliable indicator of future performance.

The Product Disclosure Statement ('PDS') and the Target Market Determination ('TMD') of the Fund is available at www.firetrail.com. Any potential investor should consider the PDS and TMD before deciding whether to acquire, or continue to hold units in, the Fund.

2. 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. 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 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. 5. Strategy inception 29 November 2005.

PORTFOLIO COMMENTARY

The Fund returned negative 0.56% (after fees) for the month ending 31 March 2023, underperforming the ASX 200 Accumulation Index by 0.40%.

For the quarter ending 31 March 2023, the Fund returned 3.71%, outperforming the ASX 200 Accumulation Index Benchmark by 0.25%.

CONTRIBUTORS TO RETURNS

Positive contributors included Newcrest Mining, Origin Energy and Commonwealth Bank of Australia (no holding). Negative contributors included Virgin Money UK, Lynas Rare Earths and BHP (underweight). We discuss each further in our commentary below.

POSITIVE CONTRIBUTORS

Newcrest Mining

Newcrest Mining outperformed as the market became more positive on the prospects for gold. The USD gold price rallied 8% on the view that banking sector disruption would temper the pace of central bank rate tightening. There was no additional formal news on the Newmont takeover offer, however press speculated that early-stage talks have begun.

Origin Energy

Origin Energy outperformed as the company received a binding proposal from the Brookfield/EIG consortium. The price was largely unchanged from the original bid, equating to $9.05 per share at current FX rates (pre the 16.5c dividend). The Origin Board has unanimously recommended shareholders vote in favour of the scheme. Targeted completion is early 2024, with ACCC approval the main hurdle remaining.

Commonwealth Bank of Australia

The Australian major banks underperformed the ASX 200 in March, but mainly for domestic reasons rather than any fallout attached to the banking issues in the US/Europe. Following the CBA CEO's comments that it is currently writing mortgages at below the cost of capital, the Westpac CEO said this was the most competitive mortgage market he has seen in his career. The only Australian bank we hold in the portfolio is ANZ, which is less exposed to mortgages versus its peers.

NEGATIVE CONTRIBUTORS

Virgin Money UK

Virgin Money UK underperformed along with the European bank sector on concerns of liquidity and credit contagion from SVB, Signature Bank and Credit Suisse. While it is still too early to determine if there will be material flow-on impacts, Virgin Money UK is in a strong position with 80% of its loan portfolio in mortgages, a diversified customer base, and substantial excess capital above regulatory minimums and internal targets.

Lynas Rare Earths

Lynas Rare Earths underperformed following Elon Musk's comments that Tesla's next drive unit will not use any rare earth materials. We don't believe this marks a turning point in rare earth demand. Many car manufacturers do not use rare earths in their motors. However, this practice does necessitate trade-offs on performance. The market also became more cautious on Lynas' ability to ramp up its new facility in Kalgoorlie without any meaningful time delays.

BHP (underweight)

Our underweight holding in BHP was a detractor during the period as the shares outperformed on the back of continued positive sentiment around China reopening. While the iron ore price was only up 1%, BHP shares outperformed the ASX 200 by 6%.

Companies mentioned are illustrative only and not a recommendation to buy or sell any particular security

COMPANY AND INDUSTRY NEWS

The broadly flat performance of the ASX 200 in March was a surprising outcome considering the substantial disruption that took place in the banking sector. The collapse of Silicon Valley Bank and Signature Bank raised questions about liquidity, customer concentration, and asset-liability mismatches across banks globally. Only one week later, an exodus of customers and investors from Credit Suisse led to a heavily discounted, Government brokered sale to UBS.

The Chair of the Fed acknowledged that banking turmoil had altered the trajectory of future base rate changes, commenting that “you can think of it as being the equivalent of a rate hike or perhaps more than that”. At the start of March, markets expected the Fed Funds rate to be at 5.3% at the end of the year. By the end of the month, the expected rate was 4.3%. By sector, gold led the way in March with metals and mining also strong. Banks, other financials, and property were the worst performers.

MEDIBANK PRIVATE DEEP DIVE

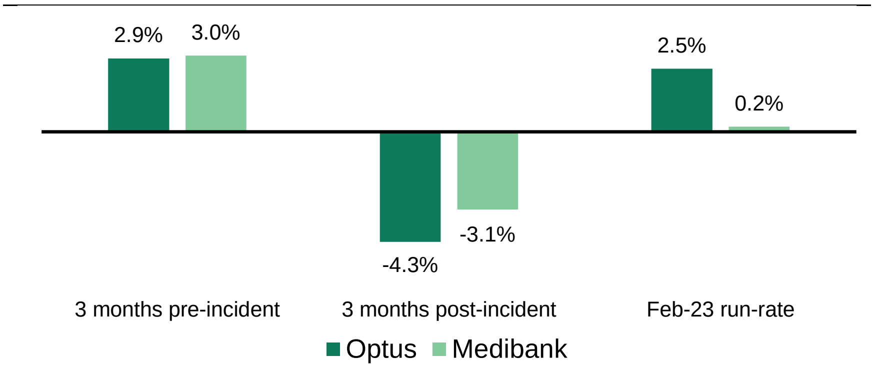
We added Medibank Private to the portfolio during the quarter. We believe the stock offers strong earnings growth with relatively high certainty compared to the rest of the market. The sell off that followed the cyber incident last year provided a compelling opportunity to enter the stock at attractive valuation levels.

Policyholder numbers are growing again

The widely publicised cyber-attack in October 2022 caused substantial disruption to the Medibank business. Apart from damage to the brand, significant resources were directed away from customer acquisition and retention towards dealing with queries relating to the attack.

In evaluating the potential impacts on the brand and customer growth, we referenced the experience of Optus following its own cyber incident. The Optus attack occurred almost a month before Medibank, on 22 September 2022. Over the subsequent three months Optus post-paid customer numbers contracted by 1.1% (4.3% annualised) but have since returned to pre-incident levels of growth. Medibank policy numbers had only returned to modest growth in February, but we expect this will continue to trend higher as we saw with Optus.

Figure 1: Customer growth around cyber events (% annualised)

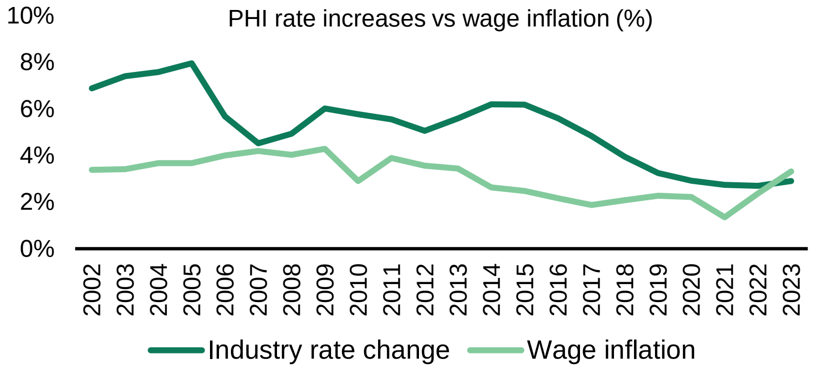


Source: Optus and Medibank data, Firetrail estimates

As shown in Figure 1 above, prior to the cyber-attack Medibank was growing policyholder numbers at ~3% per annum. While we would expect cost of living pressures to have some negative impact on private health insurance take-up, we believe there are a number of offsetting tailwinds that should enable Medibank to continue growing, namely:

1. Low claims activity means the recent pattern of premium refunds and premium increase deferrals is likely to continue (see more detail in next sub-section).
2. Public hospital waiting lists are long and not improving.
3. General consumer focus on health has increased post-COVID.
4. In 2023, premium increases will be below wage inflation for the first time in over 20 years.

Figure 2: In 2023, private health insurance (PHI) premium increases will be below wage inflation for the first time in over 20 years, which is positive for affordability



Source: Australian Government Department of Health and Aged Care, ABS

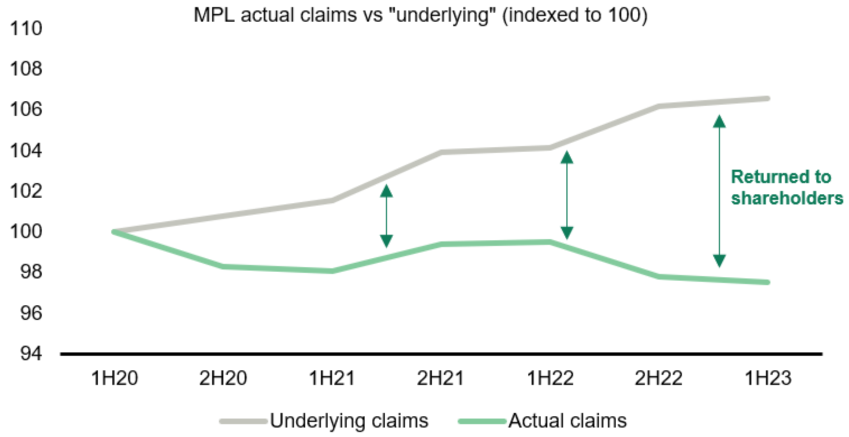
Slow claims recovery supports margins

Following the deferral and cancellation of claims during COVID, private health insurers made a commitment to the Government that they will not retain any excess profits. To the extent that actual claims have been below underlying, policyholders have received:

1. Deferral of premium rate increases; and
2. Cash refunds of previously paid premiums

Since the onset of COVID, Medibank has provided more than $1 billion of financial support to policyholders through the above mechanisms plus financial hardship support. Despite consistent discussion of the claims ‘backlog’, the gap between actual and underlying claims has been progressively widening. For the six months ending December 2022, actual claims were 9% below underlying.

Figure 3: Medibank has provided more than $1 billion of financial support to policyholders through the deferral of rate increases and premium refunds

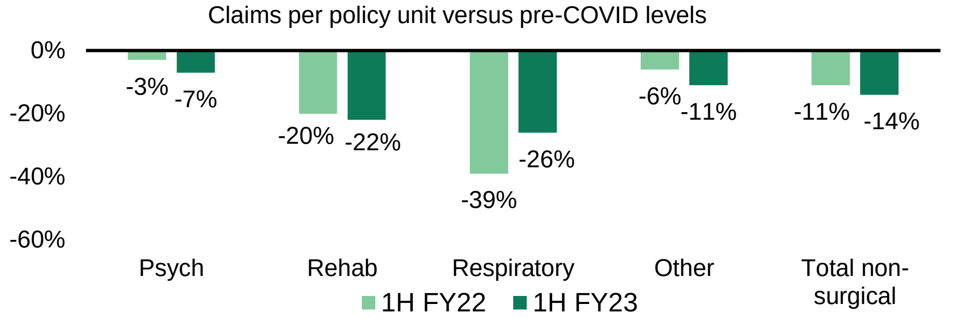


Source: Medibank data

While Medibank expects a reversion back towards underlying trends over time, there are some claims areas such as rehab where claims behaviours may have changed more permanently.

Prior to COVID, Medibank identified rehab in the home as a key focus area to improve customer experience and reduce overall health system costs. COVID naturally forced a lot of post-operative rehab for procedures like knees and hips into the home, which helped Medibank accelerate this shift. As a result, rehab claims now sit more than 20% below pre-COVID levels and may not revert.

Figure 4: It's possible that rehab claims do not revert to pre-COVID levels, resulting in a 7-8% NPAT benefit for Medibank.



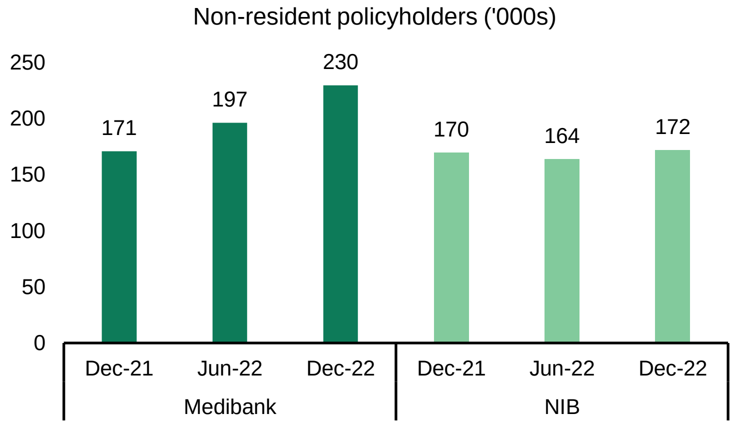
Source: Medibank data, Firetrail

At the February 2023 result, the Medibank CFO stated that "the biggest opportunity for our claims line is on rehab. We're seeing somewhere around 20% lower rehab referral rates. We're assuming they revert … If they don't, that's a $50-60 million claims saving." Note that a $50-60 million claims saving equates to a 7-8% net profit after tax benefit, all else equal.

An earnings kicker from the return of immigration

Medibank's division that insures overseas students and workers has rarely been a focus for investors. However, with the closure and reopening of borders, 'non-resident' business is now a reasonable swing factor. Over the year to December 2022, Medibank grew policyholders in this business by 35% which added 5% to group net profit after tax. Continued strong immigration data so far in 2023 suggests this business can continue to surprise positively over the next twelve months.

Figure 5: Medibank's non-resident policyholders surged in 2022. Strong immigration data in 2023 suggests this will continue



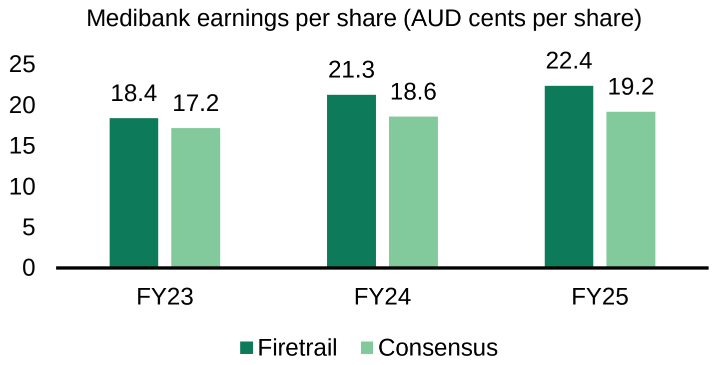
Source: Medibank and NIB data

Valuation remains well below pre-cyber levels

Medibank has now bounced around 20% from its lows relative to the market, however the stock still sits 15% below where it was trading prior to the cyber-attack despite an improved earnings outlook.

Our earnings forecasts for Medibank are 7-15% ahead of consensus and we forecast an earnings per share growth rate of 10% over FY23-25. On a multiple of 16x FY24 earnings per share, we believe Medibank is one of the cheapest defensives in the ASX 200.

Figure 6: Our earnings forecasts for Medibank are 7-15% ahead of consensus over FY23-25



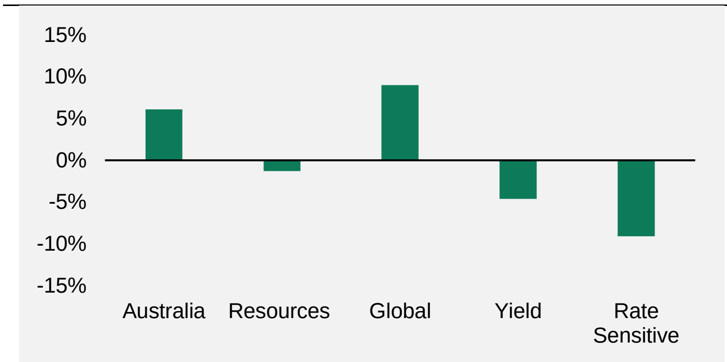
Source: Visible Alpha, Firetrail estimates

PORTFOLIO POSITIONING AND CHANGES

With underweight positions in Yield and Rate Sensitive categories broadly offsetting each other, our main thematic exposure is an overweight holding in global stocks. Our positioning across each category can be summarised as follows:

- **Australia** – overweight cyclicals with strong market positions like Qantas Airways and SEEK, and defensives like The Lottery Corporation. Underweight consumer staples.
- **Resources** – overweight energy and decarbonisation metals through exposure to Santos and Lynas Rare Earths. Underweight iron ore.
- **Global** – holdings in companies that either have robust demand profiles like ResMed and CSL, or businesses that are priced too cheaply for their reality, like James Hardie Industries and Domino's Pizza Enterprises.
- **Yield** – underweight real estate and infrastructure stocks. Overweight gold through our holding in Newcrest Mining.
- **Rate Sensitive** – underweight Aussie banks, overweight QBE Insurance and Virgin Money UK.

Figure 7: Thematic positioning as of 31 March 2023 (relative to benchmark)



Source: Firetrail

The main changes we made to the portfolio over the March quarter were:

- Initiated positions in Medibank Private and Woolworths.
- Increased position sizes in CSL and Incitec Pivot.
- Reduced position sizes in Origin Energy, Virgin Money UK, Qantas Airways, and The Lottery Corporation.

The portfolio remains highly concentrated with 75% active share and 60% stock-specific risk.

ONE INTERESTING THING THAT HAPPENED THIS MONTH…

One of our portfolio managers, Blake Henricks, recently spent two weeks in Europe visiting countries including the UK, Germany, Switzerland, and Norway. As part of his trip, he visited the St Gallen manufacturing plant of Vifor, the pharmaceutical business acquired by CSL last year. Vifor is a market leader in IV iron therapy, which is manufactured from 65% grade iron ore (see photo of the stockpile below). The high prevalence of iron deficiency presents a significant long-term upside opportunity for CSL, with 15% of the population estimated to have iron deficiency anaemia[1].

Figure 8: Iron ore stockpile at CSL Vifor, St Gallen

Source: Firetrail

Footnote 1. *Blood,* 2014 Jan 30;123(5):615-24.

MORE INFORMATION

General enquiries 1300 010 311

Existing client enquiries 1300 360 306

www.firetrail.com