L1 Capital Catalyst Fund

Quarterly Report | JUNE 2022

- **During the June quarter, the L1 Capital Catalyst Fund returned -9.0% (net)[1] (ASX200AI -11.9%).**
- **Since inception on July 1, 2021, the L1 Capital Catalyst Fund has returned 10.7% (net)[1] (ASX200AI -6.5%).**
- **Performance during the June quarter was impacted by rising inflation and increasing concerns over central bank policy tightening and the possibility of a U.S. recession. This impacted performance of Materials and Energy stocks.**

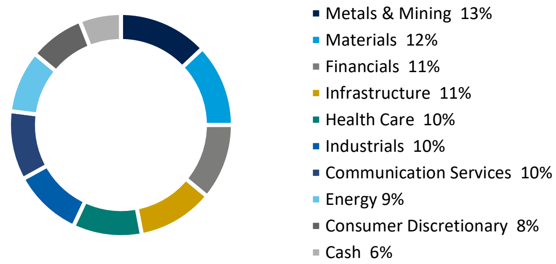
Global equity markets were weak during the June quarter, heavily impacted by higher than expected inflation and rising interest rates. The S&P/ASX200AI returned -11.9%, however outperformed most major developed markets (MSCI World ex Australia -16.1%, S&P 500 -16.1% and NASDAQ -22.3%) due largely to its relatively lower Technology sector exposure.

In the U.S., inflation reached 8.6% in May, its highest level in 41 years. In response to this, the U.S. Federal Reserve hiked interest rates by 75bps, its first three-quarter-point hike in 28 years. It was a similar story in Australia with inflation tracking above consensus expectations. As a result, the RBA increased the cash rate by 75bps during the June quarter and stated it expects inflation to peak at 7% by the end of 2022 vs. its February forecast of a 3.75% peak in June.

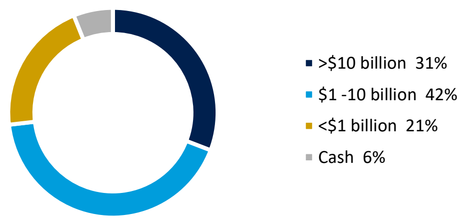
For the June quarter, 8.8% of the 11.9% decline in the S&P/ASX2000 AI occurred during the month of June. The strongest sector performance over the quarter was from Utilities (+1.7%), Energy (+1.5%) and Industrials (-1.4%), whilst the worst sector performance was from Information Technology (-27.2%), Property (-17.7%) and Materials (-16.1%).

Returns (Net)[1] (%)	Catalyst Fund	S&P ASX 200 AI	Out-performance
3 months	(9.0)	(11.9)	+2.9
6 months	(5.1)	(9.9)	+4.8
12 months	10.7	(6.5)	+17.2
Since Inception	**10.7**	**(6.5)**	**+17.2**

Sector exposure (%)



Market cap exposure (%)



Portfolio exposures by catalyst as at 30 June 2022

	Strategic	Financial	Operational	Governance
Stock 1	✓			
Stock 2				✓
Stock 3			✓	
Stock 4	✓			
Stock 5				✓
Stock 6			✓	
Stock 7		✓		
Stock 8		✓		
Stock 9	✓			
Stock 10		✓		

1. All performance numbers are quoted net of fees. Figures may not sum exactly due to rounding. Inception date: 1 Jul 2021. Past performance should not be taken as an indicator of future performance. NOTE: Fund returns and Australian indices are shown in A$. Returns of U.S. and global indices are shown in US$.

Portfolio commentary

During the June quarter, the Catalyst Fund outperformed the ASX200AI by 2.9%. The portfolio's outperformance relative to the market was driven by:

1. **Continued M&A and corporate restructurings**: M&A and corporate restructurings continue to have a positive impact on portfolio performance. One example is Ramsay Health Care ('RHC') (which we discussed during the **March 2022 Quarterly Report**). On 20 April 2022, RHC responded to media speculation and announced that it had received a conditional, non-binding, indicative proposal from a consortium of financial investors led by KKR[2]. The indicative offer price was $88 per share, less any ordinary or special dividends paid after the date of the proposal, and RHC would also be permitted to pay a fully franked special dividend to distribute all available franking credits to shareholders (worth an additional $3.40 to Australian shareholders). RHC benefited from the strong share price rally post the announcement of the KKR approach.
2. **Improved balance sheet strength:** Broadly across the Catalyst Fund portfolio, company balance sheets are strong. Several portfolio companies successfully strengthened their balance sheets early in the June quarter via debt re-financings completed at favourable interest rates, particularly considering the rise in interest rates during the latter part of the June quarter.
3. **Positive trading updates**: A number of portfolio companies released positive trading updates during the June quarter. As discussed in the **March 2022 Quarterly Report**, given the concentrated nature of the Catalyst Fund, detailed bottom-up stock picking remains the Catalyst Fund's focus and a key driver of performance.

During the June quarter, the Catalyst Fund was negatively impacted by fears about a macro-economic slowdown driven by growing concern of a 'hard landing' following a shift in central banks' monetary policy globally to combat high inflation. Specifically, this has resulted in:

1. **Declines in commodity prices**: The Bloomberg commodity price index declined 5.7% during the June quarter on the back of a softening macro-economic environment. This impacted select holdings in the Catalyst Fund that were beneficiaries of elevated commodity prices in prior quarters.
2. **Fears about a pull-back of consumer spend**: While employment for the time being remains strong, worsening economic sentiment and consumer confidence are expected to translate to lower spend across consumer discretionary categories. In addition, rising interest rates are expected to place pressure on Australian residential house prices and mortgage repayments which impact household wealth and savings. This has negatively impacted a couple of portfolio companies that have exposure to the consumer sector.

2. It has been confirmed that the consortium includes HESTA (the Health Employees Superannuation Trust Australia) and is also rumoured to include Abu Dhabi Investment Authority (ADIA, Middle Eastern sovereign wealth fund) and Government of Singapore Investment Corporation (GIC, Singapore's sovereign wealth fund)

Activism by prominent Australians

One interesting theme that has emerged recently in the Australian public markets landscape has been the involvement of prominent Australians in shareholder activism. Examples include:

Market Cap: A$5.6b
EV: A$8.4b

Mike Cannon-Brookes and AGL

On 30 March 2021, AGL announced its intention to separate its coal-focused power generation business (Accel Energy) from its Australian retail business (AGL Energy). Mike Cannon-Brookes campaigned against the demerger, arguing that the demerger would not reduce emissions and address climate change. A consortium led by Brookfield Asset Management, including Mike Cannon-Brookes[3], subsequently put forward two proposals to acquire AGL on 21 February 2022 and 7 March 2022 for A$7.9b and A$8.4b respectively[4]. These offers were rejected by AGL. Mike Cannon-Brookes then acquired c.11% of AGL in order to seek to stop its demerger plans. The demerger was ultimately withdrawn, resulting in the Chair, the CEO and numerous director resignations.

More broadly, through Grok Ventures, Cannon-Brookes has personally committed A$1.5b of capital to climate change philanthropy and green investments over the next decade.

Market Cap: ~A$425m
EV: ~A$550m

Andrew Forrest and Huon Aquaculture Group ("Huon Aquaculture")

Andrew and Nicola Forrest, through their holding company, Tattarang, announced on 21 June 2021 that it had purchased 7.3% of Huon Aquaculture, a Tasmanian salmon farming business. Tattarang were also rumoured to have bid for the company. On 6 August 2021, it was subsequently announced that Huon Aquaculture had entered into a Scheme Implementation Deed with JBS, a Brazilian meat processing giant, to acquire 100% of Huon Aquaculture shares. Tattarang subsequently increased its stake in Huon Aquaculture (to 18.5%) and challenged JBS to declare its unequivocal commitment to animal welfare and environmental sustainability, otherwise it would vote its shareholding against the Scheme. JBS stated its global commitment to sustainability and animal welfare, and Huon Aquaculture was subsequently purchased by JBS, in November 2021 for ~A$550m.

Some of the major themes emerging in Australian listed markets are:

1. **Campaigns have become particularly influenced by ESG agendas, with these individuals driving companies to pursue more progressive policies.** On environmental grounds, Mike Cannon-Brookes stated, *"We have purchased this substantial interest in the company because we fundamentally believe there can be a better future for AGL… A future that accelerates the transition to net-zero."* Similarly, Andrew Forrest stated, *"[our investment in Huon Aquaculture is] to see if we could turn salmon farming away from its current very poor reputation which in many cases is deserved and in some cases is not."*
2. **Very public campaigns run in the media.** These prominent Australian investors have run big media campaigns, using a broad range of media channels. Mike Cannon-Brooks ran a very public campaign against the AGL demerger, using social media (e.g. Twitter), and television (e.g. appearing on the 7.30 Report), to apply pressure on the AGL board. Andrew Forrest similarly ran a very public campaign, launching a national media blitz and taking out a full-page advertisement in The Australian Financial Review, publicly challenging JBS to commit to better animal welfare standards.
3. **Increased collaboration between prominent investors, institutional investors and superannuation/pension funds.** Grok Ventures engaged with a variety of investors in its campaign against AGL. In its initial bid for AGL, Grok Ventures was part of a consortium led by Brookfield Asset Management, a Canadian-based investment firm with over US$725b of assets under management. Subsequent to acquiring an 11% stake in AGL, Grok won the support of the A$68b Australian superannuation fund HESTA (the Health Employees Superannuation Trust Australia) to vote against the proposed demerger of AGL. HESTA stated it was *"unconvinced"* the plan to split AGL would *"sufficiently accelerate decarbonisation to meet Paris-aligned targets"* or *"manage the risk of stranded assets."* Grok ventures also directly engaged with AGL's major institutional shareholders to discuss the proposed demerger. On 30 June, it was announced Brookfield now own a 2.6% interest in AGL.

3. The AGL acquisition was led by Brookfield Asset Management Inc and included Grok Ventures (Mike and Annie Cannon-Brookes' investment vehicle). The Brookfield Consortium proposed to acquire 100% of the shares in AGL Energy.
4. The offer prices of A$7.9b and A$8.4b represent the implied Enterprise Values based on the offer price

Positive tailwind for Activist investors in Australia

We believe increased activism from prominent Australians will result in:

1. **Increased engagement with shareholders by ASX listed corporates and their Boards.** As a result of the failed AGL demerger, Chairman Peter Botten announced his resignation from the Board and Graeme Hunt announced he would step down as CEO and Managing Director. Increased engagement from boards and management teams will ultimately lead to faster execution of value creating catalysts, leading to greater shareholder returns. This is to the benefit and long-term interests of all shareholders.
2. **Support for M&A activity increasing the universe of potential bidders for companies.** Increased involvement of prominent Australians in public markets activism can help to drive potential takeover activity. A healthy M&A market provides one possible channel to hold listed companies accountable to execute on value creation strategies, as well as providing a pathway for businesses to realise proceeds from non-core assets.
3. **Adoption of more progressive ESG policies from companies due to activism.** Companies are expected to be more progressive with their ESG policies as shareholder expectations become more explicit and public. According to research by Guerdon Associates, currently about 88% of ASX 100 companies have executive pay incentives linked to ESG metrics. However, shareholders are now *"looking at companies more closely and… they'll want to see particular measures that are quantifiable."*
4. **More integrated media plans and use of social media channels to communicate with shareholders.** As seen in the AGL and Huon Aquaculture examples, broader media campaigns, including the use of social media, have been effective in communicating with a wide range of shareholders. Companies will need to counter this with their own media campaigns, including the use of social media, to ensure their messaging reaches all of their shareholders.

Team update | Appointment of Mihali Stamatis, Investment Analyst

Mihali Stamatis
Investment Analyst

B.Com (Finance and Economics)

Mihali Stamatis joined the L1 Capital Catalyst Team as an Investment Analyst in June 2022. Prior to joining L1, Mihali worked in public equities for Ontario Teachers' Pension Plan in London and in the Investment Banking Group of Goldman Sachs in the Consumer, Retail & Healthcare team in London and the Natural Resources team in Perth. He holds a Bachelor of Commerce, Finance and Economics, from the University of Western Australia.

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Fund information

Fund / Class Name	L1 Capital Catalyst Fund – Retail Class
Currency	AUD
Investment approach	The Investment Manager seeks to deliver private equity-style returns with listed market liquidity by taking a hands-on 'owner's mindset' to each investment in a tightly focused portfolio of up to 10 companies.
Investment objective	To deliver strong positive risk adjusted returns over the long term.
Benchmark	S&P/ASX 200 Accumulation Index
Minimum investment	$25,000
Management fee	1.28% p.a.
Performance fees	20.5% over benchmark, subject to any underperformance being recouped
Vehicle	Australian Unit Trust
Launch date	1 July 2021
Platform availability	BT Panorama, CFS FirstWrap, HSBC, Hub24, Macquarie Wrap, Mason Stevens, Netwealth, Praemium

Research house ratings

Zenith Rating[5]

Zenith notes: "We draw confidence from the high calibre of personnel and longstanding investment process that will be leveraged for the management of the Fund. We note that the holdings in the Fund will typically be a highly concentrated subset of L1 Capital's strategies, which have strong longer-term track records."

Lonsec Rating[6]

Lonsec notes: "The Fund seeks to deliver private equity-style returns with listed market liquidity by taking a hands-on 'owners mind-set' approach to each investment. The owners mind-set is anchored in constructive engagement with companies, driving the realisation of positive change by bringing strategic options, new ideas and thinking to company boards and management."

5. The Zenith Investment Partners (ABN 27 103 132 672, AFS Licence 226872) ("Zenith") rating (ETL1293AU, June 2022) referred to in this document is limited to "General Advice" (s766B Corporations Act 2001) for Wholesale clients only. This advice has been prepared without taking into account the objectives, financial situation or needs of any individual and is subject to change at any time without prior notice. It is not a specific recommendation to purchase, sell or hold the relevant product(s). Investors should seek independent financial advice before making an investment decision and should consider the appropriateness of this advice in light of their own objectives, financial situation and needs. Investors should obtain a copy of and consider the PDS or offer document before making any decision and refer to the full Zenith Product Assessment available on the Zenith website. Past performance is not an indication of future performance. Zenith usually charges the product issuer, fund manager or related party to conduct Product Assessments. Full details regarding Zenith's methodology, ratings definitions and regulatory compliance are available on our Product Assessments and at http://www.zenithpartners.com.au/RegulatoryGuidelines

6.The rating issued October 2021 is published by Lonsec Research Pty Ltd ABN 11 151 658 561 AFSL 421 445 (Lonsec). Ratings are general advice only and have been prepared without taking account of your objectives, financial situation or needs. Consider your personal circumstances, read the product disclosure statement and seek independent financial advice before investing. The rating is not a recommendation to purchase, sell or hold any product. Past performance information is not indicative of future performance. Ratings are subject to change without notice and Lonsec assumes no obligation to update. Lonsec uses objective criteria and receives a fee from the Fund Manager. Visit lonsec.com.au for ratings information and to access the full report. © 2020 Lonsec. All rights reserved.

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L1 Capital | Overview

L1 Capital is a global investment manager with offices in Melbourne, Sydney, Miami and London. The business was established in 2007 and is 100% owned by its senior staff, led by founders Raphael Lamm and Mark Landau. The team is committed to offering clients best of breed investment products through strategies that include long short Australian equities, international equities, activist equities, a global multi-strategy hedge fund and U.K. residential property. The firm has built a reputation for investment excellence, with all L1 Capital's strategies delivering strong returns since inception versus both benchmarks and peers. The team remains dedicated to delivering on that strong reputation through providing market-leading performance via differentiated investment approaches with outstanding client service, transparency and integrity. L1 Capital's clients include large superannuation funds, pension funds, asset consultants, financial planning groups, family offices, high net worth individuals and retail investors.

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Key service providers for the Fund are: Responsible Entity – Equity Trustees Limited, Fund Administrator and Fund Custodian – Mainstream Fund Services, Fund Auditor – EY, Legal Advisor – Hall & Wilcox. There have been no changes to key service providers since the last report.