Monthly Class

# L1 Capital Long Short Fund

Monthly Report | SEPTEMBER 2022

Fund NAV: $743m

- **The L1 Capital Long Short Fund returned -7.8%[1] in September (ASX200AI -6.2%).**
- **The Fund has returned 18.1%[1] p.a. over the past 3 years (ASX200AI 2.7% p.a.).**
- **Global equity markets suffered their largest sell-off since March 2020, due to increasing concerns over central bank policy tightening and the possibility of a U.S. recession.**
- **We invite you to join Mark Landau for a LSF investor webinar where he will discuss portfolio positioning and the outlook for equity markets at 11am AEDT on Thursday 10 November. Please register here.**

Global equity markets fell sharply in September (MSCI World -9.3%, S&P500 -9.2%, Nasdaq -10.4%) as the Fed maintained an aggressive stance on tackling high inflation through continued policy tightening, despite rising recession fears. U.S. markets sold off significantly over the month, with the Nasdaq and S&P500 falling below their June 2022 lows. The Fed has now increased interest rates by ~300bps since March 2022, the fastest rise since the early 1980s, with consensus expectations for a further 125bps increase by year-end. At the start of this year, U.S. markets were pricing in only 75bps of rate increases for the entire calendar year.

The S&P/ASX 200 Accumulation Index returned -6.2% in September with all sectors coming under pressure. Despite being negative, the strongest sectors were Materials (-2.3%), Energy (-3.8%) and Healthcare (-4.4%) while Utilities (-13.8%), Property (-13.6%) and Information Technology (-10.6%) were the weakest sectors.

Portfolio performance was impacted by the broad-based market sell-off over the month with limited stock-specific news flow driving share price performance. We believe the recent sell-off is presenting some exceptional opportunities, with our median portfolio long position now trading on only 9.7x FY23 P/E.

While these periods of heightened market volatility can be unnerving, we continue to believe that taking a 2 year view and focusing on enduring investment fundamentals (cashflows, industry structure, management, operating trends and balance sheet) will deliver strong absolute and relative returns to our investors.

**We believe equity markets are entering a more difficult and uncertain period due to a combination of aggressive central bank policy tightening, deteriorating leading economic indicators in the U.S, worsening geopolitical tensions and continued war in the Ukraine, along with an energy crisis. As a result, we have significantly reduced our net market exposure. We continue to find both safety and value in low P/E stocks with undergeared balance sheets and strong cashflow generation. In contrast, we believe high P/E stocks and 'expensive defensives' look crowded, risky and unappealing.**

| Fund Returns (Net)[1] (%) | L1 Long Short Fund | S&P ASX 200 AI | Out-performance |
|---|---|---|---|
| 1 year | (8.7) | (7.7) | (1.0) |
| 2 years p.a. | 27.6 | 9.8 | +17.8 |
| 3 years p.a. | 18.1 | 2.7 | +15.4 |
| 5 years p.a. | 9.1 | 6.8 | +2.3 |
| 7 years p.a. | 17.1 | 8.0 | +9.1 |
| Since inception p.a. | 19.2 | 6.1 | +13.1 |
| Since inception cumulative | 314.2 | 61.2 | +253.0 |

| Returns Since Inception (Net)[1] (%) | Cumulative Return | Annualised Return p.a. |
|---|---|---|
| L1 Capital Long Short Fund | 314.2 | 19.2 |
| S&P ASX 200 Accumulation Index | 61.2 | 6.1 |
| MSCI World Net Total Return Index (USD) | 57.3 | 5.8 |
| HFRX Global Hedge Fund Index | 9.3 | 1.1 |

Key detractors from portfolio performance in September included:

**BlueScope Steel (Long -9%)** shares weakened over the month, along with most offshore steel-making companies as U.S. and Asian steel spreads declined. U.S. steel spreads have fallen from record levels but remain healthy and are starting to stabilise as the arbitrage on importing steel has now largely been eroded.

BlueScope continues to focus on growing its U.S. operations with a 850ktpa capacity expansion at the North Star facility in Ohio, the acquisition of the U.S.'s second largest metal coating/painting company in Coil Coatings, and the establishment of BlueScope Recycling from its acquisition of the MetalX recycling business. Given its strong net cash balance sheet, we expect BlueScope to continue its significant on-market share buyback program alongside further investment in its U.S. and Australian businesses. Currently trading on just ~4.0x consensus FY23 EV/EBIT and ~6.0x consensus FY23 PE, we continue to believe the market significantly undervalues BlueScope's unique and strategic asset base.

*1. All performance numbers are quoted net of fees. Figures may not sum exactly due to rounding. Past performance should not be taken as an indicator of future performance. Strategy performance and exposure history is for the L1 Capital Long Short Fund – Monthly Class. NOTE: Fund returns and Australian indices are shown in A$. Returns of U.S. indices are shown in US$. Returns are on a total return basis unless otherwise specified.*

**James Hardie (Long -8%)** shares declined over the month on an expected sharp correction in U.S. housing demand as 30 year fixed mortgage rates lifted by 100bps to nearly 7% and fears of a U.S. recession increased. James Hardie is the market leader in fibre cement siding with a history of market share growth in the U.S. over more than 20 years. The business mix has evolved considerably since the GFC, with ~65% of group revenues currently driven by repair and remodel exposure and ~35% from new housing. We attended the company's investor day in New York in September (and also had several meetings with James Hardie senior management and board members) and came away confident in James Hardie's ability to continue to grow market share for many years to come as well as the resilience and flexibility of the business to manage through a period of softer new housing demand.

We believe the market correction has provided us the opportunity to invest in a very high-quality company with a decade of structural growth ahead of it at a very attractive valuation. James Hardie currently trades on a FY23 consensus P/E of only ~13x relative to its long-term average of 20-25x. While we expect U.S. housing starts to be negatively impacted by the steep rise in interest rates, at this valuation, we believe the market is implicitly assuming a ~40% decline in James Hardie earnings. This would be a similar impact to what the company suffered during the GFC, however, the business mix at that time was much more cyclical, with a ~60-65% skew to new housing.

**Ramsay Health Care (Long -20%)** shares fell during September following the company ceasing discussions with the KKR consortium on its non-binding indicative proposal, originally valued at $88 cash per share. Ramsay is the largest private hospital operator in Australia with over 70 hospitals and day surgery units nation-wide and a well-established global footprint that includes Australia, the United Kingdom, France, the Nordics and South-East Asia. The collapse of the takeover offer is disappointing as we viewed it as a near-term realisation of some of the catalysts that exist in the business, including portfolio simplification, unlocking value from its Australian property portfolio and capital management opportunities. We believe these value unlock opportunities continue to exist and that Ramsay management and board still have a range of alternative options that can maximise value for shareholders.

**Sandfire Resources (Long -19%)** shares declined in September due to copper prices remaining under pressure in the face of a weaker global economic backdrop. The physical copper market continues to remain tight, with supply continuing to be impacted by production challenges in Chile – the number one global producer. Sandfire completed the transformational US$1.865b (A$2.850b) acquisition of the MATSA mine in Southern Spain in February this year and is currently developing the Motheo Copper Mine in Botswana. We believe the commencement of Motheo production in FY24 will deliver a step-change in free cash flow for the company as capex declines and the operating cash flow from the mine expands. We see compelling value upside in Sandfire with the company currently trading at a discount to the acquisition price of MATSA alone, before factoring in any value for its other mining assets, including Motheo.

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Monthly Class

# L1 Capital Long Short Fund

Monthly Report | SEPTEMBER 2022

## Fund Returns (Net)[2] (%)

| | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | Year |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2014** | – | – | – | – | – | – | – | – | (2.42) | 3.03 | 2.85 | 1.61 | **5.07** |
| **2015** | 0.59 | 9.14 | 2.42 | 1.71 | 3.73 | (0.86) | 3.30 | 2.06 | 5.51 | 8.49 | 8.11 | 4.61 | **60.52** |
| **2016** | 5.81 | 0.59 | 5.47 | 2.46 | 2.78 | (0.89) | 3.22 | 3.92 | 0.46 | (0.13) | 0.55 | 2.22 | **29.61** |
| **2017** | 2.51 | 1.87 | 3.15 | 1.03 | 4.18 | 1.70 | 2.62 | 1.69 | 1.93 | 2.54 | 0.89 | 3.56 | **31.40** |
| **2018** | 0.56 | (0.47) | (1.64) | 1.62 | (3.76) | (6.29) | 0.82 | (5.92) | (2.12) | (3.98) | (2.60) | (6.06) | **(26.40)** |
| **2019** | 4.35 | 5.15 | 0.22 | 2.84 | (2.78) | 3.85 | 1.18 | 0.44 | 2.61 | 3.37 | 0.32 | 2.22 | **26.20** |
| **2020** | (7.81) | (7.10) | (23.02) | 22.96 | 10.97 | (2.20) | (1.93) | 9.98 | 0.52 | (2.62) | 32.28 | 4.16 | **28.01** |
| **2021** | (0.10) | 9.06 | (0.13) | 4.99 | 4.11 | (0.55) | 1.83 | 5.24 | 4.81 | 2.30 | (7.21) | 3.59 | **30.62** |
| **2022** | 2.74 | 7.00 | 1.47 | 3.29 | 0.12 | (13.39) | (4.63) | 5.70 | (7.80) | | | | **(7.14)** |

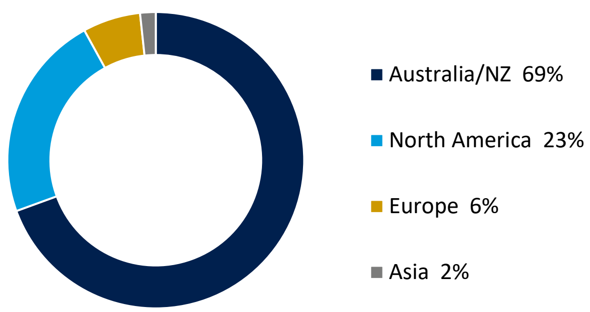
## Portfolio Positions

| Portfolio Positions | Current | Avg. Since Inception |
|---|---|---|
| Number of total positions | 82 | 81 |
| Number of long positions | 55 | 56 |
| Number of short positions | 27 | 25 |
| Number of international positions | 27 | 25 |

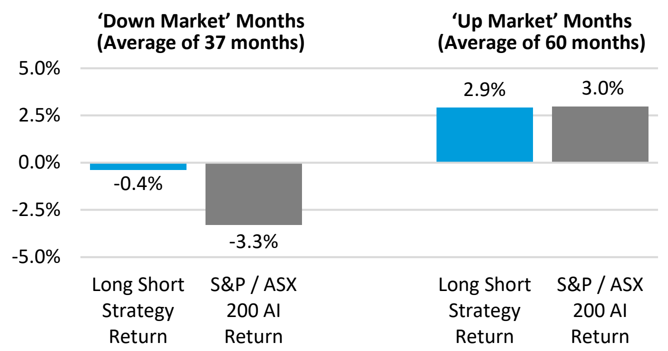
## Net & Gross Exposure by Region[2] (%)

| Geography | Gross Long | Gross Short | Net Exposure |
|---|---|---|---|
| Australia / NZ | 91 | 69 | 22 |
| North America | 37 | 15 | 22 |
| Europe | 14 | 0 | 14 |
| Asia | 4 | 0 | 4 |
| **Total** | **146** | **84** | **62** |

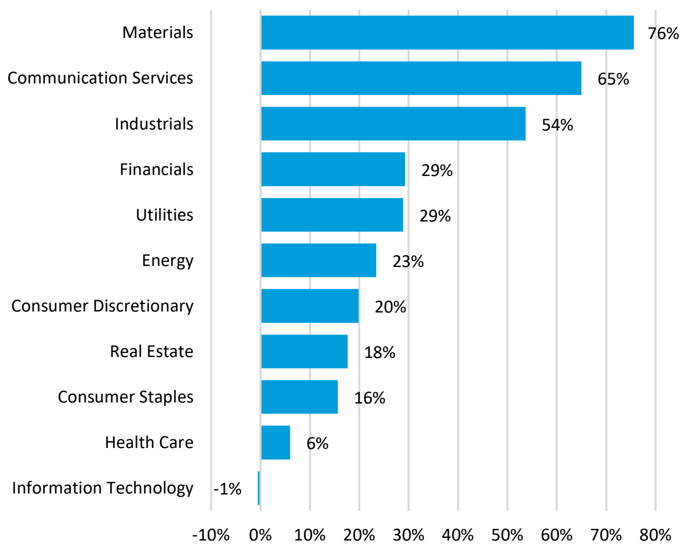
## Gross Exposure as a % of Total Exposure[2]




## Performance in Rising & Falling Markets[2] (Net)




## Sector Contribution Since Strategy Inception[2] (Net)

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## Fund Information – Monthly Class

| | |
|---|---|
| **Class Name** | L1 Capital Long Short Fund – Monthly Class |
| **Structure / Currency** | Australian Unit Trust / AUD |
| **Inception** | 1 September 2014 |
| **Management Fee** | 1.28% p.a. inclusive of GST and RITC |
| **Performance Fee** | 20.50% inclusive of GST and RITC[3] |
| **High Watermark** | Yes |
| **Buy / Sell Spread** | 25bps / 25bps |
| **APIR / ISIN** | ETL4912AU / AU60ETL49128 |
| **Minimum Investment** | A$500,000 |
| **Subscription / Redemption Frequency** | Monthly |
| **Platform Availability** | HUB24, Netwealth, PowerWrap |

## Contact us


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## L1 Capital (Investment Manager) Overview

L1 Capital is a global investment manager with offices in Melbourne, Sydney, Miami and London. The business was established in 2007 and is 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. 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.


L1 CAPITAL

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**Key service providers** for the Fund are: Responsible Entity – Equity Trustees Limited, Prime Brokers – Morgan Stanley, Merrill Lynch and Goldman Sachs, Fund Administrator – Apex Fund Services Ltd (formerly known as Mainstream Fund Services), Fund Auditor – EY, Legal Advisor – Hall & Wilcox. Since the last report, Credit Suisse has ceased to be prime broker of the Fund.

[3] The performance fee is equal to the stated percentage (inclusive of GST and net of RITC) of any increase in the NAV over any Performance Period (adjusted for applications and redemptions and before the payment of any distribution after the payment of the management fee and expenses) above the high-water mark.

All performance numbers are quoted net of fees. Past performance should not be taken as an indicator of future performance. Sources of information in this report are Mainstream Fund Services, Bloomberg and L1 Capital.

**Information contained in this publication**

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The L1 Capital Long Short Fund's Target Market Determination is available at https://bit.ly/3a0Kj68. A Target Market Determination is a document which was required to be made available from 5 December 2021. It describes who this financial product is likely to be appropriate for (i.e. the target market), and any conditions around how the product can be distributed to investors. It also describes the events or circumstances where the Target Market Determination for this financial product may need to be reviewed.


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