31 March 2022

Equity Alpha Plus Fund

PARADICE INVESTMENT MANAGEMENT

Performance Net (%)	1 Month	3 Month	1 Year	2 Year	Since Inception* p.a.
Equity Alpha Plus Fund	7.50	2.35	22.98	35.26	16.99
S&P/ASX 200 - Total Return	6.89	2.24	14.97	25.72	8.04
Excess Return	**0.61**	**0.11**	**8.01**	**9.54**	**8.95**

* Inception date - 12 July 2019

Investment Objective

The Fund aims to outperform the S&P/ASX 200 Total Return Index (after fees and before taxes) over the long term.

Lead Portfolio Manager

Tom Richardson

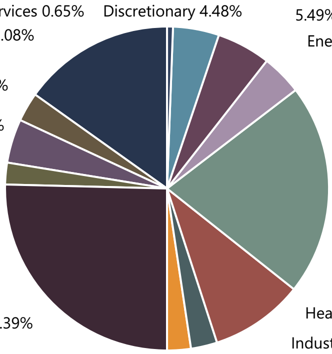
Fund Overview

With a focus on capital preservation, this fund uses a detailed fundamental research process to invest in stocks that are well placed for future growth (longs) and takes advantage of stocks we believe have structural headwinds (shorts). The Long/Short investment style is designed to enhance returns and manage downside risks.

Market Exposures

Long	90.45
Short	-5.54
Net	84.92

Sector Allocation



Geographic Location. The Fund holds no single international asset representing more than 10% of the Fund's net asset value and total international assets no greater than 30%.

Key Details

Number of Holdings	57
Portfolio Dividend Yield	4.62%
Fund Size (AUD)	$110M
Redemption Price	$1.344

Top 10 Positions	Weight %
BHP Group Ltd.	15.08
CSL Ltd.	9.68
Commonwealth Bank of Australia	7.18
National Australia Bank Ltd.	6.81
Macquarie Group Ltd.	5.92
Woolworths Group Ltd.	4.63
Goodman Group	4.57
IDP Education Ltd.	3.40
South32 Ltd.	2.54
Computershare Ltd.	2.44

Fund Details

APIR Code	ETL8096AU
Distribution Frequency	Semi-Annually
Management Fee[1]	0.99% p.a.
Performance Fee	15% p.a.
Buy Sell Spread	+/- 0.30%
Minimum Investment	$20,000
Stock Range	Long 20-60, Short 0-50
Cash Range	0-20%

Market Review

For the purposes of comparison commentary is quoted in AUD terms and Australian sector returns refers to the S&P/ASX 200 Total Return Index except where stated otherwise.

Global equity markets eased over the quarter on concerns of stagflation and the Ukraine invasion. The MSCI World Net Total Return Index fell 5.2% (in USD) in the December 2021 quarter. The Ukraine invasion propelled Energy and Commodity prices higher. The Bloomberg Commodity Total Return Index rose 25.5% (in USD). Australian equities beat global peers due to a larger exposure to Commodities. The S&P/ASX 200 Total Return Index rose 2.2%.

Stagflation is the combination of inflation and slowing or even falling economic growth. US headline inflation accelerated to 7.9% in February 2022 year on year. The Ukraine invasion creates further inflationary pressures via increased Energy, soft and hard Commodity prices, as supply is disrupted from both Ukraine and Russia. This is true not only in short term spot markets, but also medium-term futures markets as security of supply is questioned necessitating Europe seek alternative supply. As an example, Brent Oil for 2025 delivery now trades at US$82bbl, which is a ~US$20 increase versus pre-invasion. Bloomberg contributing economists' US 2022 GDP growth expectations peaked at 4.3% back in September 2021 and has fallen to 3.4% now on expectations of tighter monetary conditions and because of the Ukraine invasion. A similar outcome exists globally outside the US. Australia though has fared better due to less wage pressure flowing into inflation, and a better growth outlook driven by Commodities and Energy. Inflation in Australia was 3.5% in December 2021.

As inflation expectations further increased, monetary authorities globally have become even more 'hawkish'. The US Federal Reserve increased rates 25bp in March, which is the first for this cycle. Markets now imply a ~55% chance of 50bp rises in both May and June, which is more than double the size of increases implied for the entire rest of the year pre-invasion. The Reserve Bank of Australia has not yet raised, but guidance commentary continues to incrementally move, with Governor Lowe dropping the phase that they're "prepared to be patient" on 5 April. The US 10-year yield rose 83bps and the Australian equivalent 117bps.

Several commodities within the group experienced large increases due to supply concerns as Russia is a meaningful producer, and higher energy costs leading to steeper cost curves. Nickel rose 49.2%, Alumina 35.8%, and Iron Ore 29.6%. Within Energy, both Lithium carbonate and Thermal Coal rose ~80% and Brent 34.7%. Russia and Ukraine are also important soft (food) commodity producers. The Bloomberg Agriculture Spot index rose 16%.

The best performers for the quarter in the sectors of the S&P/ASX 200 Total Return Index were Energy (+28.6%) and Materials (+15.4%). Financials also did well (+4.5%). The laggards were Tech (-13.7%) and Healthcare (-10.0%). These growth and defensive sectors have longer duration cash flows and valuations are negatively impacted by higher rates.

On corporate activity, shareholders approved the BHP unification. Crown accepted an increased offer from Blackstone. AGL Energy and Uniti received takeover offers. The February 2022 earnings' season revealed concerns over inflation, including wage inflation, especially technology workers.

ESG

Australian corporates continue to increase their focus on ESG, as evidenced in the February reporting season. Dozens of companies featured ESG-related content more prominently in their results presentations than previous years, with many sharing progress on ESG-related performance or highlighting new sustainability initiatives commenced.

A trend we continue to monitor is that many corporate climate plans, especially those of companies with harder-to-abate emissions, intend to purchase carbon offsets to achieve net zero emissions. As such, we continue to follow the Australian carbon market and corporate use of offsets. To unlock more Australian Carbon Credit Units (ACCU), in early March the Federal Government announced a change to the ACCU regime allowing farmers and project owners to pay the government the original price for fixed delivery, they can then sell the credits on the voluntary market and pocket the difference earned. After hitting $55 a tonne in early 2022, by March 31 the spot price was $30.50. This disruption to the market came at the same time as the former chairman of a key carbon market oversight committee, Professor Andrew Macintosh, came forward with claims that some carbon abatement projects generating ACCUs lack integrity. The Greens have referred the matter to the Auditor-General, while Labor says they will establish an inquiry if they win office. With both price volatility and increasing scrutiny of the integrity of credits coming to the fore, we continue to prefer company climate plans that prioritise actual emissions reduction over offsetting.

Globally, there were two notable ESG-related developments which have longer term implications for companies. The first was the publication of the draft disclosure framework of the Taskforce on Nature-related Financial Disclosures' (TNFD) which is now in a consultation phase as the taskforce moves to finalise its recommendations. The TNFD is striving to solicit decision-useful information out of companies regarding their exposure to and management of nature-related risks and opportunities such as biodiversity loss and deforestation.
The second development came from the United Nations (UN) where member states have approved a landmark agreement to create a legally binding global plastic pollution treaty. A UN Environment Assembly spokesperson said it's "the most significant environmental deal since the Paris accord". The aim is to agree a treaty by 2024 which would cover the entire plastics value chain to address pollution.

Engagement

During the quarter, we undertook a total of 10 engagements in which we explicitly discussed ESG matters with 8 companies relevant to the strategy. Of these, 90% were held at either board or executive level. The engagements covered a range of issues and most meetings discussed multiple ESG matters. In this period, the most commonly discussed topics were ethical conduct and stakeholder relations, climate transition, and human capital management.

One company of focus during the quarter was Rio Tinto Ltd (RIO). We met with the CEO and Chair in separate meetings, discussing a number of ESG issues as well as the forthcoming AGM. A key ESG matter discussed was 'Everyday Respect' workplace culture report. We sought to understand more about how RIO would implement the report's recommendations. We also discussed RIO's climate plan and climate-related lobbying. We encouraged stronger action where misalignment occurs at industry groups and indicated we would be supportive of climate being included in future Long-Term Incentive Plans. Additionally, we tested how RIO would be interpreting 'against' votes for its upcoming Say on Climate resolution, encouraging appropriate stakeholder engagement. Finally, we discussed board renewal, in particular the selection process for the incoming Chair.

We also held meetings with Origin Energy Ltd (ORG) and South32 Ltd (S32). We met with Origin management to discuss the decision to close its Eraring coal-fired power station early, and sought to understand the expected impact on the company's emissions reduction efforts as well as how it would be managing the transition of its local workforce. Our meeting with South 32 management covered how recent changes to the South 32 asset portfolio would help in expediting the transition to clean energy and reducing carbon emissions. Additionally, we discussed workplace health and safety at South 32's South African operations

Outlook

Early last quarter the portfolio was positioned for reopening, reflation, and a rotation from growth and long duration stocks to value and more economically cyclical exposure. That meant the portfolio was overweight Commodities, Green Metals as an alternative to Oil and Gas Energy, and Financials.

During the quarter inflation accelerated and Russia invaded Ukraine. This raises the possibility of stagflation, that is even higher inflation and lower (or even negative) economic growth. Wars tend to be inflationary as they disrupt supply. Russia is a material Commodity and Energy supplier. At this stage the EU is still purchasing Energy from Russia, but will likely diversify away from them medium term. This will be positive for Australian Energy and Commodity producers as reliable alternatives.

Concerning also for the economic growth outlook, the US 10 year – 2-year yield curve has inverted, which historically is a signal implying a recession is coming in circa 12 months. Our view is that this may be a false signal. First, the long end of the yield curve is pressured lower because of US Federal Reserve bond buying. Second, short-dated bonds are significantly higher than the actual Fed Funds rate signifying futures market participants are more concerned about inflation than the Fed. Third, the “real” curve is still in contango. Other reads on economic growth are also still implying expansion. The JP Morgan Purchasing Manager Indices in all major regions are still in expansionary territory. There are risks however, with the main one being that the invasion propels inflation significantly higher and the Fed then needs to aggressively raise rates to choke that off. Weaker Chinese demand from a continuation of their covid zero policy is another risk.

Oil and Gas Energy stocks have been added to an overweight position on an increased Brent oil price outlook that has lifted their cash flow generation and valuation support. Further, proposed asset sales should now be easier to complete, and previously marginal projects now have justifiable economics. ESG issues remain a concern, but all companies added provide LNG, which has seemingly also become more accepted as a transition fuel recently.

The Financials exposure has been skewed more into stocks that benefit from higher short-dated yields. Computershare will benefit via exposed cash balances, and Insurance companies via their investments in short-dated fixed income securities. Traditional Banks though have been reduced as lower economic activity will weaken credit growth, and a flatter yield curve negatively impact Net Interest Margins (NIM).

Within the Consumer sectors, the portfolio is still positioned to benefit from a reopening in areas such as air travel where we see pent up demand. We are however more cautious on Consumer health as sentiment has deteriorated, so Consumer discretionary, including Gaming has been reduced. The portfolio is still selectively exposed to more defensive consumer staples.

Within Industrials more broadly, the portfolio is only exposed to stocks with pricing power as inflationary pressures build. We see margin expectations for Industrials generally too high. Strong demand over the covid period may be replaced by cost inflation next.

The portfolio is underweight IT, Infrastructure and Telcos where valuations tend to be negatively impacted by rising rates.