31 DECEMBER 2022

EQUITY ALPHA PLUS FUND

PARADICE
INVESTMENT MANAGEMENT

PERFORMANCE NET (%)	1 MONTH	3 MONTH	1 YEAR	3 YEAR	SINCE INCEPTION* P.A.
Equity Alpha Plus Fund	-1.59	12.16	7.21	15.25	14.60
S&P/ASX 200 – Total Return Index	-3.21	9.40	-1.08	5.55	5.24
Excess Return	1.62	2.76	8.29	9.70	9.36

*Inception date – 12 July 2019

Past performance of the Fund is not a reliable indicator of future performance. The value of an investment in the Fund may rise or fall. Returns are not guaranteed by any person. Fund returns are calculated before tax, after ongoing management costs and any accrued performance fees, and assumes the reinvestment of distributions. Returns greater than 1 year are annualised.

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

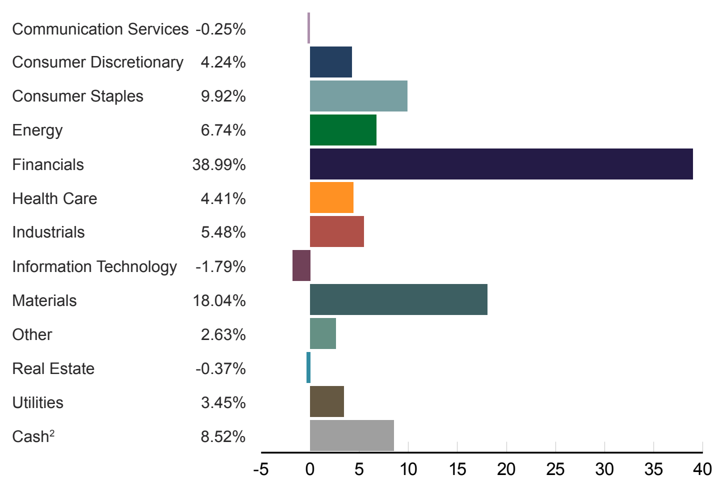
Tom Richardson

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	105.95
Short	-14.47
Net	91.48

SECTOR ALLOCATION



KEY DETAILS	
Number of Holdings	65
Portfolio Dividend Yield	4.99%
Fund Size (AUD)	$120M
Redemption Price	$1.2527

TOP 10 POSITIONS	WEIGHT %
BHP Group Ltd.	13.96
National Australia Bank Ltd.	8.62
Commonwealth Bank of Australia	8.14
ANZ Banking Group Ltd.	5.27
Woodside Energy Group Ltd.	4.45
Qantas Airways Ltd.	4.08
Coles Group Ltd.	3.97
QBE Insurance Group Ltd.	3.81
Westpac Banking Corporation	3.70
Wesfarmers Ltd.	3.60

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%

[1] The management fee is effective 3 April 2020. Prior to this date the management fee was 1.15% p.a. [2] The Cash percentage in the Sector Allocation chart is inclusive of derivatives held in the Fund, if any.

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Performance in AUD unless otherwise noted.

MARKET REVIEW

Global equity markets rebounded over the quarter on reduced inflationary pressures, and interest rate expectations stabilising. China embarking on a reopening, and the Ukraine pushing back Russian forces helped. The MSCI World Net Total Return Index rose 9.8% (in USD)[1], and the S&P/ASX 200 Total Return Index improved 9.4%. Globally, only the Technology heavy NASDAQ disappointed as it fell 0.3% (in USD) on a declining earnings outlook.

US Core Inflation eased slightly to 6.0% in November from a peak of 6.6% in September, and (although still elevated) has now remained in a range from 5.5% to 6.6% for 12 months, giving some comfort that inflation isn't spiralling out of control. Although the US Federal Reserve lifted their target rate by 125bp to 4.50% in December, from 3.25% in September, this was largely in line with expectations and the US 10-year government bond yield rose just 4bp over the quarter. However, with interest rates still moving higher, US economic growth faces headwinds. Futures imply a 5.0% US Fed target rate by June 2023. The US 2-to-10-year yield curve remains inverted by 55bp, which is an indicator of an impending recession. Bloomberg contributing economists' US 2023 Real GDP growth expectations fell to just 0.3%, and they are now forecasting a 65% probability of a recession.

The economic situation in Australia is better than in the US due to the relative benefit of China reopening and lower wage pressures. Futures imply a 3.7% cash rate in June 2023, which is a 40bp reduction from September. The Australian 2-to-10-year yield curve is positive by 64bp, which is an 8bp improvement over the quarter. Bloomberg contributing economists' Australian 2023 Real GDP growth expectations sit at 1.8%, and they are forecasting a 30% probability of a recession.

The Bloomberg Commodity Total Return Index (in USD) gained 2.2%. Nickel bounced 42.2%, Iron Ore 20.9% and Copper 9.7% (all in USD) on more positive sentiment stemming from China's reopening. Spodumene rose 7.5% (in USD) over the quarter but was higher earlier on strong demand and then eased on deteriorating end market demand and excess inventory. Thermal coal eased 6.8% (in USD) on lower demand as Europe enjoyed a warmer autumn. Brent weakened 2.3% (in USD) as China and India bought Russia's oil exports.

Utilities were the strongest sector of the S&P/ASX 200 Total Return Index rising 28.0% on Brookfield's bid for Origin Energy. Materials (+15.2%) outperformed on a recovery in commodity prices driven by sentiment around China's reopening. REITS (+10.4%) outperformed as valuations bounced due to interest rate expectations easing. Financials (+10.5%) marginally outperformed largely as Banks rose on an improved Net Interest Margin (NIM) outlook. Consumer Discretionary and Information Technology underperformed due to deteriorating earnings outlook.

The Australian Government announced coal and gas energy price caps. BHP entered into a scheme to buy OZ Minerals. CSL and Newcrest CEO's both announced their departures. Woolworth's bought a 55% stake in Petspiration.

ENVIRONMENTAL, SOCIAL, GOVERNANCE ISSUES (ESG)

A number of notable developments related to nature and natural capital occurred during the quarter. Firstly, the much-delayed UN Conference on Biodiversity, COP15, was able to achieve a landmark agreement with 196 countries signing up for the Kunming-Montreal Global Biodiversity Framework. A key commitment made was to protect 30% of the world's land and water by 2030. In Australia, the Federal Government released a Nature Positive Plan with significant reforms proposed including a new environmental protection agency (EPA) and increased protections for areas of national environmental significance. We anticipate that these developments will further drive the fast-emerging investor focus on natural capital and enhanced corporate reporting on management of nature-related risks and opportunities.

With two high profile cyber incidents in recent months and potential vulnerabilities exposed across corporate Australia, cyber resilience has become a key focus for companies and investors alike. While we understand that legal settings in Australia are likely to make customer class actions challenging, companies which fall victim can face other financial impacts such as fines and regulatory impost. So far, we have found that customer churn is lower than one might anticipate given negative media coverage. Additionally, in our view, cyber resilience needs to be approached in a holistic manner, well beyond a focus on IT systems and security and extend to human capital and customer management practices. For further thoughts on understanding the human side of cyber resilience to mitigate risk please see our recent article here.

Australia is one step closer to a mandatory climate-related disclosure regime which has the potential to change the landscape of reporting across ASX-listed entities. Recently the Treasurer announced a consultation on such a regime, seeking input from industry on items such as who should be required to report and to what extent should a local regime align with international standards. Australian efforts follow a similar endeavour commenced by the US Securities and Exchange Commission earlier in the year. MSCI research found that the proposal of climate-related reporting requirements through the consultation was enough to see a 67% uptick in US companies reporting Scope 3 emissions. Regardless of the exact shape of the Australian regime, in our view there will be a significant impetus for ASX companies to expand the climate-related disclosures provided to the market.

ENGAGEMENT

During the quarter, we undertook a total of 16 engagements in which we explicitly discussed ESG matters with 12 companies relevant to the strategy. Of these, 81% 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 climate transition, executive pay and cyber risk.

Cyber security dominated engagement in the period with Medibank Private (MPL). We held various meetings at executive and board-level, seeking to understand the incident, the impacts to customers and ultimately the potential for penalties or other liabilities. While the compromise of sensitive medical data for a significant portion of the Australian population is obviously a negative, we believe Medibank has responded to the incident responsibly by refusing to pay a ransom and has been transparent in its disclosure (made challenging by the rapidly evolving situation). We are of the view that policyholder churn in the short term and penalties under prevailing law is likely limited, but it is too early to conclude longer term ramifications.

We also held a meeting with Woolworths Group (WOW) dedicated to modern slavery. After learning that the company had confirmed modern slavery was found at a supplier in Malaysia, we sought to understand more about the incident itself as well as how the company was responding. Overall, we took comfort that Woolworth's approach was very thorough and the company had evidenced a strong commitment to transparency.

OUTLOOK AND POSITIONING

Global growth continues to slow in response to rapidly rising interest rates. Inflation is likely peaking, although we expect the services component to remain sticky. Central banks will remain vigilant in this environment which will act as a handbrake to equity markets.

While a re-opening of China in 2023 could be supportive of further commodity strength, resource companies have rallied extensively, and the Fund is now slightly underweight the Materials sector. The Fund continues to be overweight Financials as the domestic economy is thus far responding well to a rise in interest rates. We have increased our defensive exposure through Consumer Staples.

[1] For the purposes of comparison commentary is quoted in Australian dollar terms and Australian sector returns refers to the S&P/ASX 200 Total Return Index unless stated otherwise.