

K2 Australian Small Cap Fund (Hedge Fund)

30 September 2022

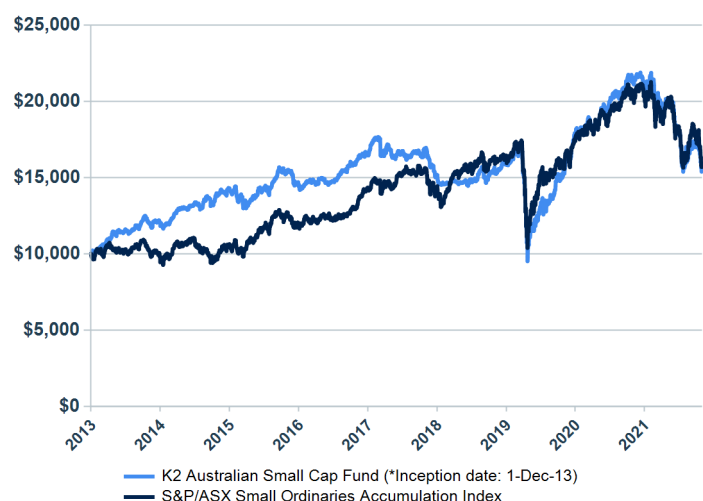


The K2 Australian Small Cap Fund is an Absolute Return equities fund. The fund is index-unaware, aiming to produce positive absolute returns over the long term with a capital preservation mindset. The Fund's mandate allows it to actively manage its net market exposure – utilising both cash and shorts to help protect clients' capital.

| | 1 Month | Unit Price | Inception (%pa) |
|---------------------------|---------|------------|-----------------|
| Performance (Net of Fees) | -9.78% | 2.19 | 5.15% |

Refer below detailed performance data matrix

Growth of \$10,000



| Top 5 Stock Holdings | Current | Monthly Move |
|------------------------------|---------|--------------|
| Summerset Group Holdings Ltd | 7.7% | +0.5% |
| Seven Group Holdings Ltd | 6.9% | +0.1% |
| PeopleIn Ltd | 5.9% | -0.5% |
| Judo Capital Holdings Ltd | 5.6% | +0.6% |
| Kina Securities Ltd | 5.3% | +0.1% |

| Market Capitalisation Coverage | Current | Monthly Move |
|--------------------------------|---------|--------------|
| Large Caps >=AUD\$7.5b | 0.0% | 0.0% |
| Mid Caps >=AUD\$2b < AUD\$7.5b | 29.5% | -3.9% |
| Small Caps < AUD\$2b | 58.5% | +2.0% |

| Month End Exposures | Current | Monthly Move |
|-------------------------|---------|--------------|
| Communication Services | 2.7% | +0.1% |
| Consumer | 9.3% | -3.1% |
| Energy | 7.1% | +0.0% |
| Financials | 19.8% | 0.0% |
| Health Care | 12.4% | +0.4% |
| Industrials/Real Estate | 28.9% | -2.1% |
| Information Technology | 2.4% | -0.7% |
| Materials | 6.0% | +3.8% |
| SHORTS | -0.3% | 0.0% |
| Number of Positions | 29 | -1 |
| Gross Equity Exposure | 89.0% | -1.5% |
| Cash Weighting | 11.7% | +1.5% |
| Net Equity Exposure | 88.3% | -1.5% |

Commentary

The K2 Small Cap Fund returned -9.78% for the month.

Australia appears to be in the cross hairs of global macro traders. At present the consensus trade seems to be sell long bonds, buy VIX, buy US dollars and sell Australian assets. As a result, the Australian dollar is trading like an emerging market currency. However, Australia is performing better than the currency suggests. Australian households have built up over \$3 trillion of superannuation assets and this now accounts for almost 20% of their total assets. In addition, the Australian household debt to assets ratio is just 17% whilst interest payments on housing debt remains manageable at 4.7% of household disposable income. Interest payments will rise in-line with higher rates over the coming year but the impact is softened by the embracement of fixed rate loans during the COVID pandemic. Additionally, the global economy is losing momentum. Hence, the Reserve Bank of Australia (RBA) should be able to be more pragmatic with monetary policy over the coming months.

Back in the early 1990's, the RBA accepted that an appropriate target for monetary policy would be to achieve an inflation rate of 2-3%, on average, over time. Since then, the RBA has changed the official cash rate on 70 occasions. Importantly, the RBA has kept rates unchanged 80% of the time. Given that global oil and food prices have retreated 27% and 13% respectively since mid-year, and the impact of monetary policy typically occurs with a lag, we feel that the RBA must get more comfortable that its target inflation rate is within reach. Therefore, we believe that the RBA is getting closer to a period of inaction. The Small Ordinaries Index has historically responded well when the RBA is sedentary. Since 1990, during the quarters when the cash rate was unchanged, the Small Ordinaries Index delivered an average total return of +3.7%. As a result, the Fund is optimistically positioned in financials and industrials.

The best performance contributors for the Fund this month were Megaport (MP1), Winton Land (WIN) and Gold Road Resources (GOR). MA Financial (MAF) and PeopleIn (PPE) were detractors. During the month the Fund bought News Corporation (NWS) and Megaport (MP1). Harvey Norman (HVN) was sold. The median holding for the Fund has a market capitalisation of \$1.2 billion and, using next years' estimates, trades on a PE of 10.4x and generates an ROE of 15.7%.

| Fund Characteristics | |
|----------------------------|--|
| Portfolio Managers | Campbell Neal, David Poppenbeek and Bill Laister |
| Strategy | Australian and New Zealand Small Cap Equities |
| Objectives | To deliver consistent returns over the investment cycle with a focus on capital protection during periods of market declines |
| Return Target | S&P/ASX Small Ordinaries Accumulation Index + 3%pa |
| Number of Stocks | 25 to 50 |
| Cash | Up to 100% of portfolio |
| Distributions | Annually |
| Management Fee | 1.31% |
| Buy/Sell | Bought and Sold on the ASX market (ASX: KSM) |
| Performance Fee | 15.38% pa of the amount by which the NAV per unit exceeds the High Water Mark once the fund achieves its hurdle |
| Investment Horizon | 5 Years |
| Style Bias | Growth At a Reasonable Price |
| Market Capitalisation Bias | >\$1billion |

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K2 Australian Small Cap Fund Net Monthly Returns in AUD

| Year | Jul | Aug | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Apr | May | Jun | Fin YTD | Fin YTD Index (1) | Average Cash | Average Short |
|---------|-------|-------|-------|-------|-------|-------|-------|-------|--------|-------|-------|---------|---------|-------------------|--------------|---------------|
| 2013/14 | | | | | | 2.86 | 3.19 | 3.06 | 4.44 | 0.36 | 1.15 | -1.26 | 14.52 | 1.12 | 41.95% | 0.00% |
| 2014/15 | 3.64 | 2.57 | -0.68 | 0.50 | -1.04 | -0.37 | 2.60 | 4.48 | 1.37 | -0.22 | 2.23 | -2.11 | 13.51 | 0.44 | 22.50% | 0.00% |
| 2015/16 | 5.71 | -2.77 | 3.61 | 1.57 | 1.31 | 1.20 | -3.95 | -5.76 | 4.80 | 3.33 | 1.21 | -0.40 | 9.58 | 14.40 | 12.48% | -0.20% |
| 2016/17 | 4.80 | 3.05 | 0.00 | -1.48 | -3.76 | -0.39 | 1.57 | -1.54 | 3.14 | -2.28 | 0.78 | 2.80 | 6.50 | 7.01 | 15.90% | -0.54% |
| 2017/18 | 2.08 | 3.58 | 0.05 | 2.86 | -0.23 | 5.91 | -0.28 | -3.36 | 0.04 | -2.06 | 1.65 | -1.87 | 8.29 | 24.25 | 21.35% | -2.04% |
| 2018/19 | 1.82 | -0.96 | 2.06 | -6.33 | -4.24 | -3.25 | -0.36 | 1.48 | -1.08 | 1.04 | 0.31 | -0.08 | -9.53 | 1.92 | 44.79% | -3.92% |
| 2019/20 | 5.21 | -3.19 | 3.27 | -0.11 | 2.71 | 1.01 | 2.56 | -8.00 | -28.03 | 11.37 | 6.81 | -0.18 | -12.11 | -5.67 | 26.59% | -1.28% |
| 2020/21 | 4.81 | 11.25 | 1.40 | 3.21 | 12.13 | 1.58 | 0.80 | -1.11 | 2.75 | 6.18 | 1.08 | 3.57 | 58.25 | 33.23 | 5.99% | -0.23% |
| 2021/22 | -1.03 | 4.78 | 0.19 | 0.75 | -2.02 | 2.31 | -8.61 | -1.08 | 2.50 | -0.86 | -9.08 | -13.71 | -24.36 | -19.52 | 8.02% | -0.01% |
| 2022/23 | 9.20 | 1.14 | -9.78 | | | | | | | | | | -0.36 | -0.47 | 14.21% | -0.23% |
| | | | | | | | | | | | | Incept. | 55.80 | 58.51 | | |
| | | | | | | | | | | | | Incept. | 5.15%pa | 5.35%pa | 21.38% | -0.84% |

(1) S&P/ASX Small Ordinaries Accumulation Index

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