Product Assessment

Report as at 15 Jun 2023

Zenith

RECOMMENDED

Auscap Long Short Australian Equities Fund

Rating issued on 15 Jun 2023 | APIR: ASX0001AU

Investment objective

To achieve absolute returns of 10% p.a. to 15% p.a. (before fees) over the long term.

Auscap maintains an equal focus on meeting its performance objectives and capital preservation.

Manager	Auscap Asset Management
Distributor	Auscap Asset Management
Sector	Australian Shares \ Long Short
Investment Style	Variable Beta
RI Classification	Aware
Absolute Risk	High
Relative Risk	Very High
Investment Timeframe	7+ Years
Benchmark	S&P/ASX 300 (Accum)
Min Investment Amount	$A 0
Redemption Frequency	Monthly
Income Distribution	Annually
Fund Size (31 Jul 2021)	$292.00M
Management Cost	1.69% p.a. Incl. GST
Performance Fee	15.375% of performance (after fees) in excess of dual hurdles, the S&P/ASX All Ordinaries Accumulation Index and the RBA Cash Rate, subject to the recoupment of prior underperformance
Buy / Sell Spread	0.20 % / 0.20 %
Inception Date	04 Dec 2012

Fund facts

- Expected to hold between 30 and 60 stocks including short positions
- Net exposure typically ranges between 90% and 100%
- Expected portfolio turnover to average between 30% p.a. and 50% p.a.
- Monthly liquidity with a one-month redemption notice period (daily liquid class, APIR: ASX6124AU)

Viewpoint

The Fund, managed by Sydney-based Auscap Asset Management (Auscap), provides investors exposure to Australian equities through a value and quality-focused, long/short variable beta strategy. Zenith's conviction in the Fund is underpinned by the attractiveness of Auscap’s underlying philosophy and its sound investment process. Overall, we believe the Fund is well-placed to deliver on its investment objectives.

Auscap was established in 2012 by Tim Carleton and Matthew Parker as a boutique, Australian equities-focused long/short investment manager. In May 2023, Parker left the business. Zenith considers his departure to be a loss for the team, however, we are comforted by the ongoing involvement of Carleton. Going forward, we believe it is important for the investment team to experience a sustained period of consolidation and stability.

The investment team of three is led by Carleton, with direct support provided by William Mumford and Gavin Rogers. Carleton has 19 years of industry experience, previously managing an Australian equities long/short strategy with proprietary funds at Goldman Sachs. Zenith views Carleton as a highly experienced investment professional with a strong understanding of the Australian equities market.

The Fund is expected to be long-biased and is constructed through a benchmark unaware bottom-up approach, strongly leveraging the stock selection process. Once an investment opportunity is identified, it is subject to both quantitative and qualitative analysis. Zenith believes Auscap's stock selection process is sound, drawing on the bottom-up stock selection experience of the investment team.

Portfolio weights are determined by the conviction of Auscap's investment thesis and stock liquidity, with Carleton considering market dynamics to determine optimal entry and exit points. Carleton and Mumford are responsible for dealing, which Zenith believes is a prudent approach allowing for a better understanding of market forces and sentiment.

The Fund's long and short exposures are primarily a function of the investment opportunity set, with Auscap having the flexibility to allocate up to 100% to cash in the absence of compelling investment opportunities. Auscap is highly selective with regard to short selling and, as such, it is rarely utilised. Zenith believes that Auscap's portfolio construction process and decision-making structure ensures the Fund holds the team's highest conviction ideas.

Effective 1 January 2021, the Fund's performance fee structure included dual hurdles (S&P/ASX All Ordinaries Index and the RBA Cash Rate). Zenith views the introduction of an equity benchmark for the performance fee in addition to the RBA Cash Rate positively, given the Fund is expected to maintain a substantially long equity bias.

This document has been prepared by Zenith.. Zenith's Financial Services Guide is available at https://www.zenithpartners.com.au/important-information/financial-services-guide/ and full details regarding Zenith's contact details, research processes, ratings information and conflicts of interest are available at https://www.zenithpartners.com.au/our-solutions/investment-research/fund-research-regulatory-guidelines/

Fund analysis

Fund characteristics

Constraint	Value
Number of Stocks	30 to 60
Net Exposure (%)	-150% to 150% (Typically 90% to 100%)
Gross Exposure (%)	Max: 400%
Long Exposure (%)	Max: 200% (Typically 90% to 140%)
Short Exposure (%)	Max: 200% (Typically 0% to 10%)
Cash (%)	Max: 100%

Investment objective and philosophy

The Fund aims to achieve absolute returns of 10% p.a. to 15% p.a. (before fees) over the long term.

Auscap believes that markets are efficient over the long term, however, inefficiencies can occur over the short term due to behavioural biases and the time required for information to be disseminated and fully analysed. These inefficiencies result in the deviation of stock valuations from their intrinsic value. Auscap attempts to exploit these inefficiencies through the use of a concentrated, long/short strategy that is driven primarily by fundamental analysis.

Auscap adopts a value-style approach to investing, whilst seeking to identify stocks with attractive quality attributes. Zenith draws comfort from Auscap's discipline in applying its value-style process through a range of market conditions.

Portfolio applications

Investors should be aware that the Fund has monthly liquidity. In addition, Auscap requires a minimum notice period of one month for redemptions. Zenith notes that a daily liquid unit class of the Fund is available (APIR: ASX6124AU). However, investors can only access this investment option via select investment platforms.

In general, compared to most other asset classes, equities offer investors the opportunity for higher capital growth over the longer term with some income. However, this higher growth is also often associated with higher volatility. Therefore, it is recommended that investors adopt a longer time frame when investing in equities.

Investors should also be cognisant of the fact that the Australian equity market is relatively concentrated, with the Materials and Financials sectors dominating the market. The Australian equity market also only represents approximately 2% of global equity markets (in terms of market capitalisation). Therefore, to mitigate this concentration risk it is highly recommended that investors diversify their investments across asset classes, both domestically and globally.

Unlike a traditional long-only Australian equities fund, Auscap employs a long/short investment strategy, which provides it with greater flexibility to meet its investment objectives over the long term. Auscap's short selling capability enables the Fund to profit from companies that are expected to fall in price or hedge against declines in the broader market. As such, investors should be aware that the Fund's return profile will likely deviate from the benchmark and peers.

Investors should be aware that the Fund targets its return objective with leverage. The gross exposure (long plus short exposure) of the Fund has varied between 60% and 230% since inception. Zenith believes this is an important measure for investors to understand as it is indicative of the actual leverage in a portfolio, which may amplify losses should Auscap fail to deliver added value from both its long and short components (i.e. gross leverage of greater than 100% magnifies the level of success and failure).

Zenith notes that the Fund's net equity exposure has ranged between 45% and 135% since inception. Relative to variable beta peers, Auscap has been more dynamic in adjusting exposures over shorter discrete periods, subject to the availability of investment opportunities or for risk management purposes.

While Zenith believes the Fund can be held as a standalone exposure to the Australian equities sector, to achieve a more diversified exposure to the asset class, the Fund should be blended with other style-neutral or growth-orientated Australian equities products. Zenith encourages investors of the Fund to adopt a medium to long-term investment timeframe of greater than seven years.

The Fund's portfolio turnover is expected to average between 30% p.a. and 50% p.a. over a market cycle, which Zenith considers to be low to moderate. Auscap was not able to provide any insight on the proportion of expected turnover attributed to the resizing of existing positions and that which is due to initiating and closing positions. Given this expected level of turnover, a sizeable proportion of the Fund'sreturns are expected to be delivered via capital appreciation in the unit price, rather than through the realisation of capital gains in income distributions. In addition, realised capital gains are likely to be eligible for the capital gains tax discount. As such, holding all else equal, the Fund may be more appealing to investors who are high marginal tax rate payers as it will result in superior after-tax return outcomes.

Fund responsible investment attributes

Key Information	Description
Zenith RI classification*	Aware
Has Responsible Investment Policy	Yes
Negative screens**	**Full/Partial**
Armaments	Full
Gaming	Partial
Adult Entertainment	Full
Tobacco	Full
Nuclear Power	Full
Human rights abuse	Full
Animal cruelty	Full

Key Information	Description
Other Measures	Payday Lending (Full), Predatory Lending (Full), Unsustainable Logging (Full)
PRI Status	
PRI Signatory	Yes

*Zenith RI Classification scale:

- Traditional
- Aware
- Integrated
- Thematic
- Impact

***Data has been supplied by third parties. While such information is believed to be accurate, we do not accept responsibility for any inaccuracy in such data.*

Absolute performance

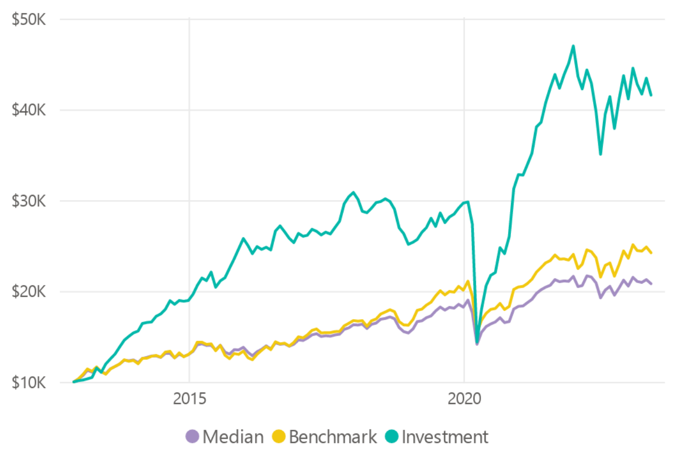
Performance as at 31 May 2023

Monthly performance history (%, net of fees)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	BM YTD*
2023	8.22%	-3.93%	-2.57%	4.19%	-4.28%								1.02%	2.58%
2022	-7.15%	-3.13%	4.93%	-3.30%	-7.31%	-11.78%	12.65%	4.83%	-8.45%	8.53%	6.25%	-5.84%	-12.40%	-1.76%
2021	-0.16%	3.43%	3.77%	8.24%	1.36%	5.50%	4.09%	3.45%	-3.44%	3.58%	2.77%	4.26%	43.15%	17.55%
2020	0.42%	-8.17%	-47.44%	24.96%	14.63%	5.41%	1.48%	12.38%	-2.63%	7.72%	20.29%	5.00%	10.57%	1.74%
2019	0.92%	1.19%	3.08%	1.96%	3.82%	-3.21%	5.46%	-3.70%	2.24%	1.13%	2.32%	1.89%	18.06%	23.78%

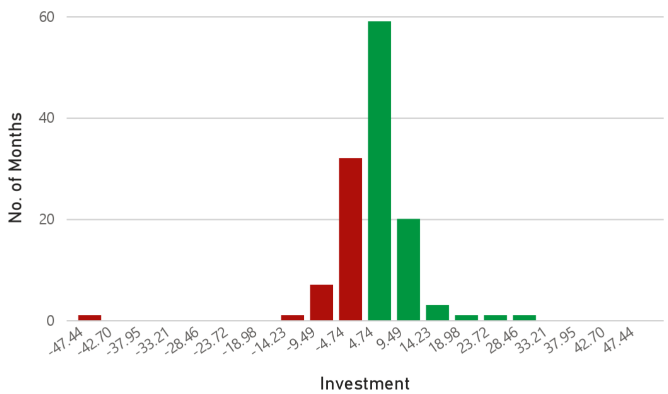
**S&P/ASX 300 (Accum)*

Growth of $10,000

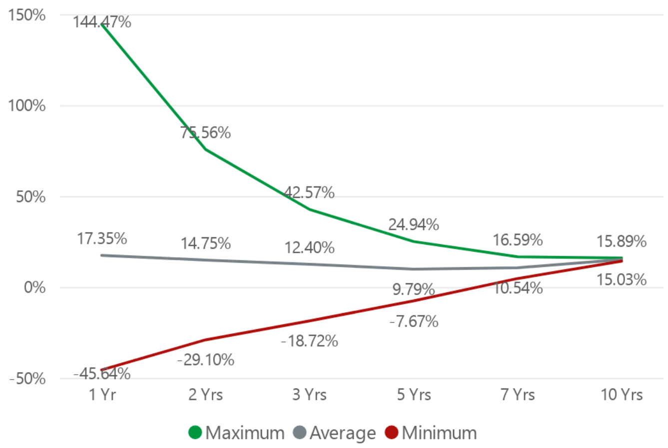


Risk / return

Monthly histogram



Minimum and maximum returns (% p.a.)



Absolute performance analysis

Instrument	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Investment	4.62%	26.36%	6.93%	14.17%	14.54%
Benchmark	2.36%	11.33%	7.43%	8.10%	8.79%
Median	-0.30%	8.99%	4.81%	6.49%	7.24%
Cash	2.64%	0.91%	1.14%	1.69%	1.76%

Ranking within sector (p.a.)

Ranking within Sector	1 Yr	3 Yrs	5 Yrs	Inception
Fund Ranking	9 / 40	3 / 39	17 / 33	1 / 19
Quartile	1st	1st	2nd	1st

Absolute risk

Instrument	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Standard Deviation (% p.a.)					
Investment	25.69%	22.64%	31.56%	23.65%	23.29%
Benchmark	17.32%	13.64%	16.41%	13.90%	13.89%
Median	13.59%	11.03%	14.54%	11.88%	11.92%
Downside Deviation (% p.a.)					
Investment	16.87%	11.96%	23.90%	17.29%	16.92%
Benchmark	11.99%	8.38%	12.31%	9.91%	9.80%
Median	10.12%	7.07%	11.33%	8.74%	8.64%

Absolute risk/return ratios

Instrument	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Sharpe Ratio (p.a.)					
Investment	0.08	1.12	0.18	0.53	0.55
Benchmark	-0.02	0.76	0.38	0.46	0.51
Median	-0.22	0.73	0.25	0.40	0.46
Sortino Ratio (p.a.)					
Investment	0.12	2.13	0.24	0.72	0.76
Benchmark	-0.02	1.24	0.51	0.65	0.72
Median	-0.29	1.14	0.32	0.55	0.63

All commentary is as at 31 May 2023.

The Fund aims to achieve absolute returns of 10% p.a. to 15% p.a. (before fees) over the long term.

The Fund has achieved its investment objective over the long term, outperforming the benchmark and median manager. Furthermore, the Fund has ranked within the first quartile among peers since inception.

The Fund's volatility of returns (as measured by Standard Deviation) has been significantly higher than the benchmark across all assessed time periods, which is expected given its use of leverage.

The Fund has produced a Sharpe Ratio slightly greater than the benchmark and peer median since inception, suggesting investors have been compensated on a risk-adjusted basis for the higher level of active risk inherent in the strategy.

Investors should be aware that Auscap does not target a specific level of income, with distributions made annually where possible.

Relative performance

Excess returns

Statistic	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Excess Return	2.25%	15.03%	-0.50%	6.07%	5.74%
Monthly Excess (All Mkts)	41.67%	58.33%	48.33%	53.33%	53.17%
Monthly Excess (Up Mkts)	83.33%	79.17%	64.10%	56.41%	54.88%
Monthly Excess (Down Mkts)	0.00%	16.67%	19.05%	47.62%	50.00%

Capture ratios (% p.a.)

Statistic	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Downside Capture	154.03%	145.49%	170.62%	102.92%	100.03%
Upside Capture	161.16%	180.13%	151.18%	126.97%	122.96%

Tracking error (% p.a.)

Instrument	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Investment	10.11%	12.00%	18.50%	15.13%	15.04%
Median	4.23%	3.32%	2.82%	2.89%	2.85%

Information ratio

Instrument	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Investment	0.22	1.25	-0.03	0.40	0.38
Median	-0.63	-0.71	-0.93	-0.56	-0.54

Beta statistics

Statistic	1 Yr	3 Yrs	5 Yrs	10 Yrs	Inception
Beta	1.43	1.49	1.71	1.36	1.32
R-Squared	0.93	0.81	0.79	0.63	0.62
Correlation	0.96	0.90	0.89	0.80	0.79

All commentary is as at 31 May 2023.

Zenith seeks to identify strategies that can outperform in over 50% of months in all market conditions, as we believe this represents consistency of manager skill. In addition, we view a strategy's ability to produce stronger upside capture ratios relative to downside capture ratios as an attractive feature.

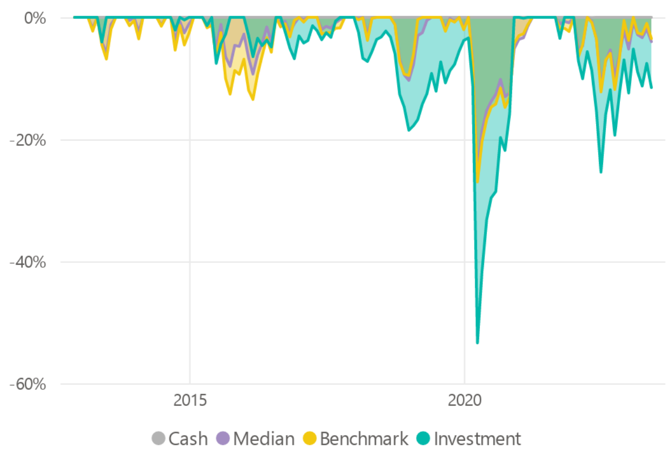
The Fund has produced strong excess returns relative to the benchmark since inception in all market conditions, with greater outperformance consistency during rising markets. However, the Fund has exhibited significant downside capture since its inception.

The Fund's Information Ratio has been positive over the long term, suggesting that investors have been rewarded on a risk-adjusted basis for the inherent active risk in the Fund.

Zenith notes that the Fund's Tracking Error has remained high, which is consistent with an absolute return benchmark unaware mandate.

Drawdown analysis (since inception)

Drawdown analysis assesses the relative riskiness of a Fund versus the benchmark, in reference to capital preservation. The maximum Drawdown is recorded as the percentage decline in the value of a portfolio from peak to trough (before a new peak is achieved). All Drawdown analysis is calculated commencing from the inception date of the Fund in question, and Drawdown analysis for the Fund and benchmark(s) are calculated independently. That is, the largest drawdown for the Fund and benchmark(s) will not always refer to the same time period.



All commentary is as at 31 May 2023.

Whilst the Fund has historically demonstrated an ability to limit drawdowns during periods of market stress, Zenith notes this has not been achieved when assessing the Fund's more recent performance. Consequently, Zenith is disappointed with Auscap's inability to limit drawdowns in recent market conditions.

Product Exposures

Holdings not provided by the manager

Fund commentary

Fund risks

Zenith has identified the following key risks of the Fund. Although Zenith believes the risks noted are all significant, we have listed them in order of importance. In addition, we have not intended to highlight all possible risks.

Key person risk: Auscap is subject to a high level of key person risk. Zenith views Tim Carleton as critical to the success of the Fund, with his departure triggering an immediate review of our rating. However, we acknowledge Carleton's material equity ownership in Auscap which we believe mitigates the risk of his departure, at least in the medium term.

Business risk: Business risk is generally higher for boutique firms; however, as is the case with Auscap, it is reduced substantially once profitability is reached. The firm's level of funds under management (FUM) is approximately $A 284 million, as at 30 April 2023. Zenith highlights that there has been a material decline in FUM from a peak of approximately $A 637 million (as at 30 September 2018). Although Auscap maintains significant working capital, we note that business stability has diminished meaningfully. Zenith will continue to monitor business stability going forward.

Relative performance risk: The Fund holds a concentrated portfolio of stocks (typically 30 to 60 including shorts). Investors should be aware that this may result in higher levels of stock specific risk and therefore, performance may deviate from the benchmark and peers.

Capacity risk: Excessive levels of FUM can inhibit a manager's ability to trade portfolio positions effectively and may, therefore, limit outperformance potential. Whilst Zenith does not consider capacity to be a current issue, given strategy FUM of approximately $A 284 million, as at 30 April 2023, Zenith will continue to monitor this risk closely.

Leverage risk: The Fund has the ability to short-sell stocks and use the proceeds to increase its long exposure. This increases an investor's exposure to Auscap's stock-specific decisions and can magnify gains and losses. The maximum gross exposure, namely the sum of the Fund's long and short exposures, is limited to 400% of the value of the Fund's net assets.

Derivative risk: The Fund can use derivatives such as options and futures and these investment securities can be volatile, speculative, illiquid and leveraged. The use of derivatives is limited to hedging purposes with index and stock puts used to hedge physical stock positions, whilst futures are used to adjust the market exposure of the portfolio. However, the Fund can only use exchange-traded derivatives and cannot use them to leverage up the Fund.

Accessibility risk: The Fund offers investors monthly liquidity. Zenith notes that this is inconsistent with peers and would prefer more favourable liquidity terms, given that a large portion of the investments in the Fund are in a relatively liquid segment of the Australian equity market (S&P/ASX 200). In addition, Auscap also applies a one-month minimum notice period for redemptions.

Zenith notes that a daily liquid unit class of the Fund is available (APIR: ASX6124AU). However, investors can only access this investment option via select investment platforms.

Counterparty risk: The Fund's custody and counterparty contracts are subject to potential default risk. In particular, the Fund is exposed to counterparty risk with its Prime Broker, Citigroup Global Markets Limited (CGML). Assets of the Fund are required to be transferred to CGML when borrowing stock for short selling. Assets up to the required collateral amount are held on CGML's balance sheet and are not segregated from other CGML assets.

Should CGML become insolvent, there is a risk that the assets posted by the Fund may not be recoverable.

Security/asset selection

The Fund's investable universe includes all Australian listed equities, however, Auscap will tend to focus predominantly on stocks within the S&P/ASX 200 Index.

The stock selection process begins with the identification of attractively priced potential investment opportunities. Auscap screens the universe on the following metrics:

- Forecast earnings yield
- Anticipated earnings growth
- Price to earnings ratio (P/E)
- Price to cash flow ratio (P/CF)
- Enterprise value to earnings before interest and tax ratio (EV/EBIT)
- Dividend yield
- Price to net tangible assets (P/NTA)

In addition to the quantitative screen, Auscap also considers opportunities from a variety of sources, such as:

- Industry data
- Company meetings and site visits
- Discussions with management
- Discussions with sector & stock analysts
- Review of external research reports and valuation work

Once an investment opportunity is identified, it is subject to both quantitative and qualitative analysis, which includes financial analysis and a company visitation program.

Quantitative analysis includes an assessment of the following metrics:

- Historic cash flow generation and conversion
- Balance sheet strength (Debt/EBIT, Interest coverage ratio and Debt to market capitalisation)
- Return on invested capital (ROIC)
- Return on assets (ROA)
- Return on equity (ROE)
- Historic, near-term and sustainable revenue and earnings growth
- Historical profitability
- Sector and stock revenue growth drivers
- Volatility of revenues, earnings and cash flows

Qualitative analysis involves the assessment of the following factors:

- Quality and strength of management
- Industry feedback and perception
- Simplicity of the business model
- The nature of the goods and services offered
- Investigative and anecdotal evidence
- Testing of the investment thesis against similar and contrary opinions

In addition, Auscap also has access to numerous brokers for external investment research reports, broker research reports and corporate access.

Specific to short-selling opportunities, Auscap seeks the following characteristics:

- Poor cash flows
- A weak balance sheet
- Declining earnings and/or cash flows
- Complex business models
- Questionable accounting practices
- Poor cash flow conversion (as a percentage of reported profits)
- Undisciplined, inexperienced or poor management
- A market capitalisation that significantly exceeds an estimate of fair value
- Market sentiment, investor psychology and technical indicators that suggest downside price risk

Overall, Zenith believes Auscap's stock selection process is intuitively sound, drawing on the bottom-up stock selection experience of the investment team.

Responsible investment approach

Auscap has an established Responsible Investment Policy, last updated in 2020, that guides its investment decisions.

While the portfolio has no specific exclusions, Auscap incorporates environmental, social and governance (ESG) considerations into its research effort. The identification of ESG issues can be reflected in a company's quality assessment and/or valuation, which if deemed to be significant, can preclude the company from potential investment. Zenith believes that this qualitative analysis of a company's operations is crucial on a forward basis, given that a company's performance regarding ESG considerations is increasingly being reflected in a company's share price. Overall, Zenith is comfortable with Auscap's approach to ESG.

Zenith has assigned the Fund a Responsible Investment Classification of Aware.

Portfolio construction

Carleton is ultimately responsible for the Fund's portfolio construction.

The Fund is expected to retain a long bias and is constructed through a benchmark unaware and bottom-up approach, which strongly leverages the stock selection process.

The Fund will typically hold between 30 and 60 stocks, both long and short combined.

Portfolio weights are determined based on the conviction of Auscap's investment thesis and stock liquidity. Long positions are typically initiated at weights between 0.5% and 5%, whilst short positions are typically initiated at weights between -0.2% and -2.5%.

Carleton will consider investor psychology and market sentiment to determine optimal entry and exit points. Individual positions will be exited when one of the following occurs:

- The investment thesis becomes invalidated by new data, changing circumstances and/or a change in Auscap's view
- The position trades above (for long positions) or below (for short positions) Auscap's view of intrinsic value
- Poor technical indicators suggest a continued deterioration in the share price is probable, without an appropriate justification for continued investment

Carleton and Mumford are responsible for dealing, which Zenith believes allows for an understanding of market forces and sentiment.

Portfolio turnover is expected to average between 30% p.a. and 50% p.a. over a market cycle, which Zenith considers to be low to moderate. However, Zenith notes that historically the Fund's turnover has been significantly higher than this expected range.

The Fund's long and short exposures are predominantly a function of the investment opportunity set, however, Auscap has highlighted that they may short futures to hedge the risk of the long portfolio. In addition, the Fund may hold cash (up to 100%) in the absence of compelling investment opportunities or for risk management purposes.

Zenith is confident in Auscap's portfolio construction approach and believes Carleton is well-placed to utilise the Fund's flexible investment mandate to meet its investment objectives.

Risk management

The Fund is managed within its portfolio constraints. Whilst broad, Zenith believes these constraints provide the Fund with sufficient flexibility to achieve its investment objective, whilst maintaining a disciplined approach to investing.

At the individual security level, Zenith believes that risk management is well incorporated in the detailed fundamental research process undertaken by Auscap.

The gross and net equity exposures of the portfolio are primarily driven by the investment opportunity set and are subject to the Fund's portfolio constraints. Zenith believes the gross and net equity exposure constraints are appropriate given the strategy and objective.

Zenith notes that there are no industry, sector or market capitalisation exposure limits, which can potentially lead to high levels of concentration in certain sectors.

Given the asymmetric risk profile of short selling, Auscap manages short positions more actively than their long counterparts by typically assigning smaller weights. Greater consideration is given to liquidity and high levels of short interest, with short positions typically taken in companies with market capitalisations of greater than $A 1 billion. Whilst the Fund's short exposure has historically ranged between 0% to 40% since inception, Zenith highlights that Auscap has become highly selective with regard to short selling and, as such, it is expected to be rarely utilised on a forward-looking basis.

Zenith is comfortable with Auscap's risk management process and in particular notes the disciplined approach undertaken by Carleton. However, investors should be aware there is significant reliance on the judgement and skill of the investment team.

Investment fees

	Fund	Sector Average
Total Fees and Costs (RG 97)	2.98 % p.a.	2.22 % p.a.
Management Fees and Costs	1.69 % p.a.	1.10 % p.a.
Transaction Costs	0.07 % p.a.	0.47 % p.a.
Performance fees as at 30 Jun 2022	1.22 %	0.84 %
Performance fees description	15.375% of performance (after fees) in excess of dual hurdles, the S&P/ASX All Ordinaries Accumulation Index and the RBA Cash Rate, subject to the recoupment of prior underperformance	
Management Cost	1.69 % p.a.	1.13 % p.a.
Buy / Sell spread	0.20 % / 0.20 %	0.26 % / 0.26 %

All fees and costs are inclusive of GST unless indicated otherwise. The Performance Fee shown is the performance fee disclosed in the PDS. It is calculated by taking the average performance fees charged over the last five financial years (or less if the investment or performance fee mechanism has not been in place for five financial years).

The Sector average management cost is based on the average management cost of all flagship Australian Shares - Long Short funds surveyed by Zenith.

The performance fee is calculated and paid monthly.

Prior to 1 January 2021, the Fund's performance fee was paid on the outperformance of the RBA Cash Rate. Zenith views the introduction of an equity benchmark for the performance fee in addition to the RBA Cash Rate positively, given the Fund is expected to maintain a substantially long equity bias.

Overall, Zenith believes the Fund's fee structure is expensive, relative to peers, given its stated objectives. However, we believe the fees paid over the past three years (ending 30 June 2022) are justified given the Fund's risk-adjusted performance over the same period.

(The fees mentioned above are reflective of the flagship version only, fees may differ when the product is accessed through an alternate investment vehicle such as a platform.)

About the fund manager

Investment personnel

Name	Title	Industry Experience (yrs)	Tenure (yrs)	Location
Tim Carleton	Portfolio Manager	19	12	Sydney, Australia

Organisation

Based in Sydney, Auscap Asset Management (Auscap) was established in 2012 as a boutique Australian equities-focused long/short investment manager.

In May 2023, Parker left Auscap. Zenith considers his departure to be a loss for the business, however, we are comforted by the ongoing involvement of Carleton, who currently holds 100% of Auscap's equity.

As at 30 April 2023, Auscap had approximately $A 284 million in firmwide funds under management (FUM). As at the same date, Auscap managed approximately $A 284 million in its Australian long/short strategy.

Zenith highlights that there has been a material decline in firmwide FUM from a peak of approximately $A 637 million (as at 30 September 2018). Although Auscap maintains significant working capital, we note that business stability has diminished meaningfully.

Personnel

The investment team of three is led by Carleton, with direct support provided by William Mumford and Gavin Rogers. Carleton has 19 years of industry experience, previously managing an Australian equities long/short strategy with proprietary funds at Goldman Sachs. Zenith views Carleton as a highly experienced investment professional with a strong understanding of the Australian equities market.

In May 2023, Parker left the business. The Fund had been managed by Carleton and Parker under a co-portfolio manager structure since its inception. As a result, Carleton is now solely responsible for the construction of the Fund. Zenith considers Parker’s departure to be a loss for the team, however, we are comforted by the ongoing involvement of Carleton. Going forward, we believe it is important for the investment team to experience a sustained period of consolidation and stability.

Investment support is provided by Gavin Rogers and William Mumford, with Auscap's investment team comprising three individuals. With over 25 years of investment experience, Rogers is based in Melbourne and predominantly acts as a sounding board for Carleton. Zenith notes that Rogers previously worked with Carleton and Parker at Goldman Sachs. Mumford has seven years of industry experience, serving in a variety of investment banking and finance-related roles prior to joining Auscap in July 2018.

Carleton holds a majority equity stake in the business. The remaining investment team members are remunerated with a salary and discretionary bonus, determined based on a number of qualitative criteria. Whilst Zenith believes the ownership structure of Auscap aligns the interests of the investment team to the Fund's performance and the overall success of the business, Zenith would prefer greater breadth in equity participation to assist in the retention of key staff.

Zenith continues to have high regard for Auscap's senior investment professionals. However, we consider the level of resourcing available to be less than peers. As such, we believe that the Fund would benefit from additional analytical resources. Overall, Zenith believes Carleton has the requisite experience and expertise to successfully manage the Fund.

About the sector

Sector characteristics

The Zenith 'Australian Shares – Long Short' sector consists of long/short funds investing across the Australian equity market cap spectrum. Managers in this sector can short-sell equities and/or SPI futures to capture excess return opportunities and manage risk. Over the long term, Zenith expects rated long/short products to outperform the S&P/ASX 300 Accumulation Index, given a manager's ability to generate positive excess returns from short selling.

Long/short managers can utilise fundamentally driven and/or quantitatively-driven investment processes with a variety of trading biases. Managers in this sector employ active extension or variable beta investment styles. Active extension funds can be used as an alternative to traditional long-only funds where the investor wishes to increase their exposure to equities. That is, the manager can build a higher conviction portfolio by shorting stocks it believes will underperform and using the proceeds to invest long in stocks that it believes will outperform. Variable beta funds can be used by investors seeking to reduce market risk otherwise associated with a fully-invested long-only fund. Variable beta managers can decrease their market exposures to protect against market falls (by increasing shorts and/or cash holdings) or increase their market exposures, with leverage, to generate higher returns.

Zenith benchmarks all funds in this sector against the S&P/ASX 300 Accumulation Index. However, many managers in this sector benchmark themselves against the S&P/ASX 200 Accumulation Index. Both indices are market-capitalisation weighted, resulting in companies with the largest market capitalisations receiving the highest weightings within the index. Over the longer term, Zenith believes there will be minimal difference between the return profiles of these indices.

The Australian equities asset class, as represented by the S&P/ASX 300 Index, is highly concentrated and narrow. Zenith considers a company to be a large-cap company if it falls within the S&P/ASX 50 Index, with stocks falling within the S&P/ASX 51 to 100 considered mid-cap companies. Furthermore, Zenith considers stocks that fall within the S&P/ASX 101 to 300 to be small-cap companies.

As at 31 March 2023, the Financials and Materials sectors combined represented a significant portion of the S&P/ASX 300 Accumulation Index, with the Financials sector accounting for approximately 27% and Materials approximately 26%. In addition, the top 10 stocks represented approximately 46% of the Index and the top 20 stocks represented approximately 61%.

Sector risks

Funds within the 'Australian Shares – Long Short' sector are exposed to the following broad risks:

Market and economic risk: A sustained downturn across the Australian equity market is a risk to the absolute performance of funds in the sector. Additionally, changes in economic, social, technological or political conditions, as well as market sentiment, could also lead to negative fund performance. This risk can be significantly reduced by investors adhering to a fund's prescribed investment timeframe.

Specific security risk: This is the risk associated with an individual security. The price of common shares in a company may be affected by unexpected changes in company operations such as changes in management or the loss of a significant customer.

Liquidity risk: This is the risk that a security or asset cannot be traded promptly, due to insufficient trading volumes in the Australian equity market. When trading volumes are low, buyers/sellers can significantly impact the price of a security when entering or exiting a position.

Style bias risk: Australian equity managers employ different investment styles such as Growth, Value or Neutral (a combination of Value and Growth). Each style is conducive to certain market conditions. This risk can be significantly reduced by investors adhering to a fund's prescribed investment timeframe.

Capacity risk: High levels of funds under management (FUM) can present additional challenges to an Australian equity manager. High FUM has the potential to restrict a manager's ability to trade efficiently and/or be forced to disclose substantial shareholdings to the market (most common in smaller companies).

Regulatory Risk: All investments carry the risk of being affected by changes to government policies, regulations and laws. Security prices in which funds may have exposure are also subject to certain risks arising from government intervention in the Australian equity market. Such regulation or intervention could adversely affect fund performance.

Short risk: Australian long/short funds can borrow securities and sell them on the equity market (otherwise known as short selling). Given such securities will ultimately need to be returned to a lender, funds that short-sell securities may be required to re-purchase such securities at a higher price, thereby incurring a loss. Such losses can potentially be unlimited given that there is no theoretical upper limit on security prices.

Zenith rating

Report certification

Date of issue: 15 Jun 2023

Role	Analyst	Title
Analyst	Stephen Colwell	Senior Investment Analyst
Sector Lead	Tom Goodrich	Senior Investment Analyst
Authoriser	Bronwen Moncrieff	Head of Research

Rating history

As At	Rating
15 Jun 2023	Recommended
22 May 2023	Recommended
23 Jun 2022	Recommended
17 Jun 2021	Recommended
09 Jun 2020	Recommended
12 Jun 2019	Recommended
14 Jun 2018	Recommended

Last 5 years only displayed. Longer histories available on request.

In March 2021, Zenith implemented a new ratings methodology for products classified as Traditional Index. Any rating issued from this date forward for Traditional Index products only reflect this change in methodology, with the relevant Traditional Index ratings being Index Approved, Index Recommended and Index Highly Recommended. Ratings issued for Traditional Index products prior to March 2021 are retained for historical purposes in line with our regulatory requirements and were issued in line with Zenith's Fund Research Methodology. Further information in relation to Zenith's Traditional Index Research Methodology and Traditional Index Ratings can be found on the Zenith website.

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