INDIAN PACIFIC
FUNDS MANAGEMENT

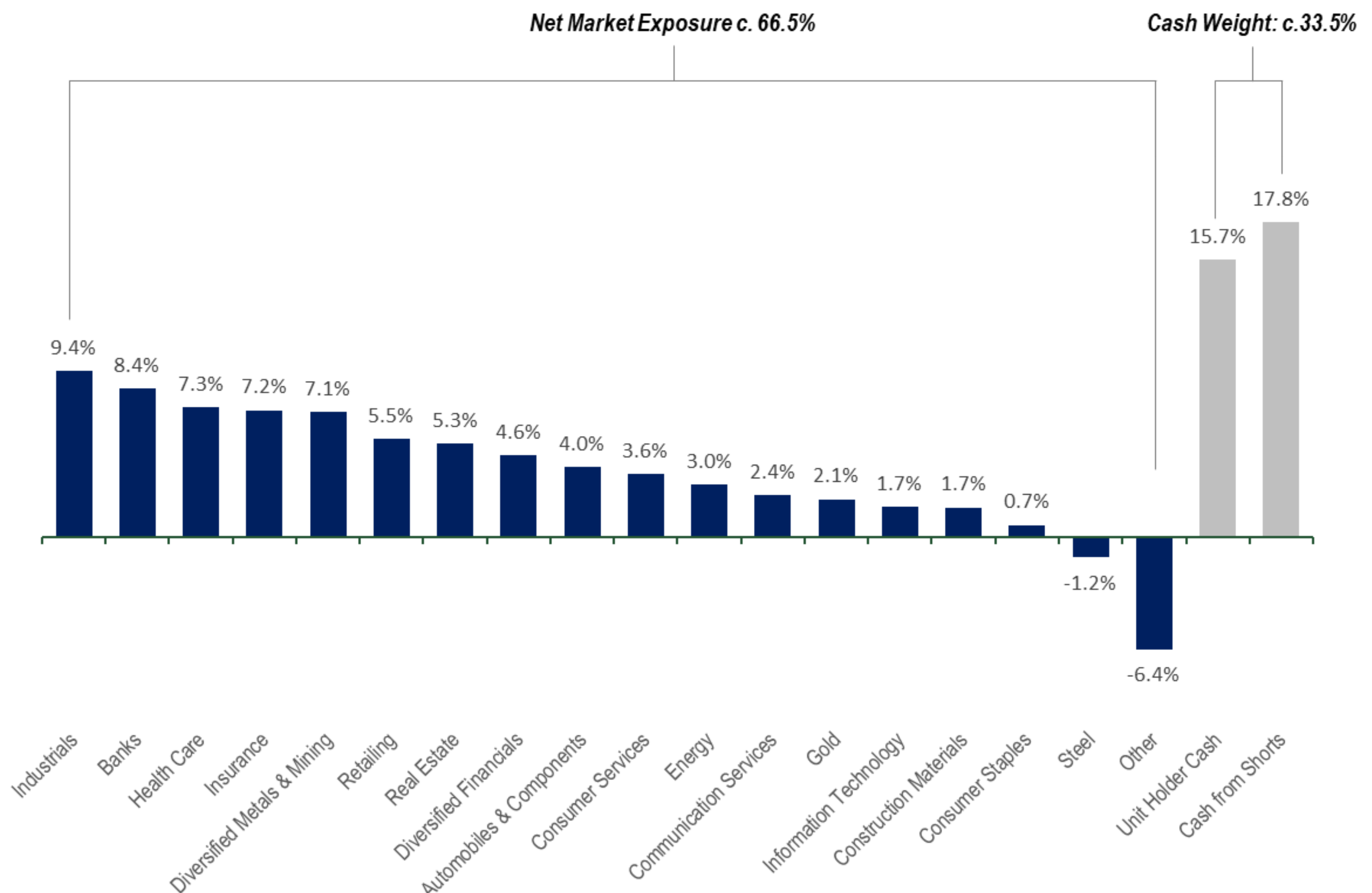
# Monthly Performance Report
## June 2022

| Net Returns | |
|---|---|
| 1 Month | -6.3% |
| 3 Months | -9.7% |
| 1 Year | -7.6% |
| 2 Year | 20.9% |
| Inception (Feb 2018) | 37.8% |

| Top 5 Holdings | Weight |
|---|---|
| Abacus Property Group | 5.3% |
| APM Human Services Intl | 4.7% |
| Macquarie Group | 4.6% |
| Aristocrat Leisure | 4.5% |
| Healius | 4.5% |
| Top 5 Holdings as % of AUM | 23.7% |

| Net Exposure | |
|---|---|
| Long Exposure | 84.3% |
| Short Exposure | -17.8% |
| Gross Exposure | 102.1% |
| Net Exposure | 66.5% |

## Portfolio Positioning




## Year in Review

The Fund's NAV was down -6.3% (net) in June (ASX All Ords -9.5%, ASX200 -8.9%, ASX Small Ords -13.4%), taking our **2022 return to -7.6%** (All Ords -11.0%, ASX200 -10.2%, Small Ords -21.6%) and **since inception return to +37.8%.** Investing in equities is never a straight line and nothing has been truer in recent years. While not satisfied with posting a negative return in any year, we've done our best to protect your money in a challenging environment but being a "net long" investor we are still correlated with markets (albeit to a lesser degree than most funds). This years returns follow a solid +30.8% net return in 2021 (v. All Ords +26.4%), and +3.3% in 2020 when the All Ords were down -7.2%. Our average exposure throughout FY 2022 was 72.6%, similar to the levels we have averaged since inception and our cash position and short portfolio played their role this year to help buffer our losses whilst our small cap positions were our worst performers on the long side.

As we begin a new financial year we think it is important for you to understand where our key "active" or "overweight" positions are today, and why we have confidence that these companies should be good custodians of our collective capital in more difficult economic times. As you will see most of these stocks have almost zero weighting in the index and if they are in the index our position size is many times larger than their index weighting. That is, where we take a position, we don't take the stocks' index weight into our consideration at all. In line with our investment process which you all know well, this interesting list of

industrial companies (and one miner) all have strong balance sheets, with good management teams, in industries we like and understand, with opportunities to grow, at valuations we consider attractive. Combined, we believe these stocks form a solid "backbone" for the portfolio as we head into FY23 and beyond. In the below table you can see the size of our positions, as well as some of the key valuation metrics for each stock. Below the table we explain in short why we hold each current position which we hope gives you some insight into how we think and invest.

**Indian Pacific Funds Top 10 "Active Positions"**

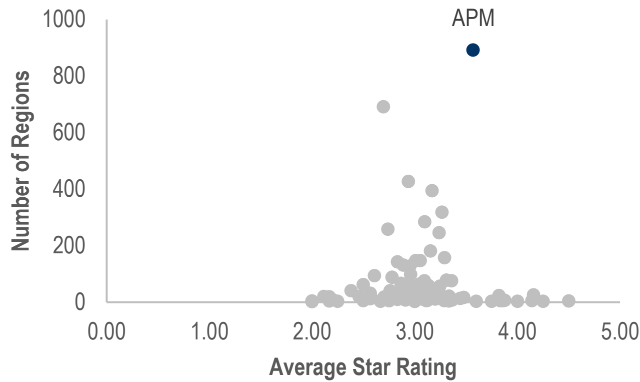
| Company | Portfolio % | ASX 300 % | Active % | Price | ND/EBIT FY23 | Int Cover FY23 | EV/EBIT | | P/E | | EPS CAGR 2yr | Payout FY23 | Yield FY23 | P/B FY23 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | FY22 | FY23 | FY22 | FY23 | | | | |
| Abacus Property Group | 5.1% | 0.1% | **5.0%** | $2.57 | N/R | 5.3x | 15.4x | 14.3x | 13.0x | 12.9x | 2% | 90% | 6.7% | 0.7x |
| APM Human Services | 4.5% | 0.0% | **4.5%** | $2.87 | 1.5x | 8.6x | 15.4x | 14.1x | 15.2x | 14.8x | 12% | 61% | 3.5% | 2.0x |
| Healius | 3.9% | 0.1% | **3.8%** | $3.67 | 2.7x | 4.3x | 7.0x | 14.0x | 7.0x | 15.7x | -34% | 64% | 4.0% | 1.1x |
| PSC Insurance Group | 3.6% | 0.0% | **3.6%** | $4.14 | 2.0x | 10.3x | 21.4x | 18.4x | 23.4x | 21.3x | 10% | 62% | 3.0% | 3.2x |
| Aristocrat Leisure | 4.6% | 1.2% | **3.4%** | $34.38 | 0.7x | 16.9x | 15.6x | 14.4x | 20.5x | 18.4x | 11% | 38% | 2.0% | 4.0x |
| Tourism Holdings | 3.3% | 0.0% | **3.3%** | $2.32 | 2.0x | 3.7x | N/A | 10.8x | N/A | 16.9x | N/A | 44% | 2.4% | 1.8x |
| Insurance Australia Group | 3.5% | 0.5% | **3.0%** | $4.36 | 3.3x | 57.8x | 16.2x | 10.2x | 23.2x | 14.2x | 32% | 81% | 5.6% | 1.6x |
| ReadyTech Holdings | 2.3% | 0.0% | **2.3%** | $3.10 | 1.0x | 10.3x | 19.4x | 15.9x | 22.3x | 19.7x | 16% | 9% | 0.4% | 3.1x |
| Capricorn Metals | 2.2% | 0.0% | **2.2%** | $3.13 | 1.0x | 27.0x | 11.0x | 10.0x | 12.4x | 11.9x | -1% | N/A | N/A | 3.4x |
| PWR Holdings | 2.1% | 0.0% | **2.1%** | $6.32 | -0.7x | -190.6x | 22.5x | 18.5x | 32.2x | 26.2x | 20% | 56% | 1.9% | 8.1x |

Note: EBIT replaced by EBITA where EBITA is closer to FCF in our estimates.
Source: Indian Pacific Funds Management

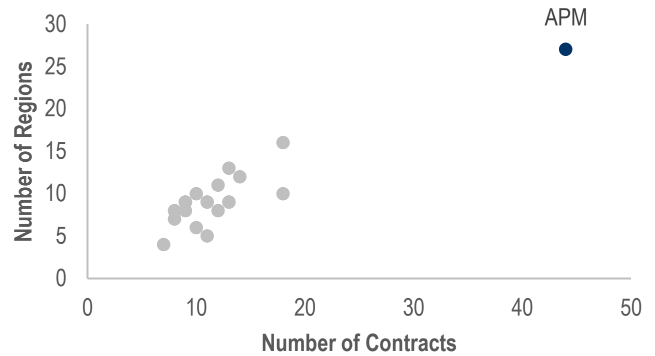
## Indian Pacific Company Commentary

**Abacus Property Group (ABP.AU)** – ABP is our preferred exposure to the property sector. It is an internally managed REIT focused on office and self-storage, and is a fairly nimble mid-cap operator by property standards (market cap $2.5bn). ABP has two key investment exposures: 1) a high-quality self-storage portfolio, which we believe offers strong long term growth and a steady income stream under their **Storage King** banner, and 2) an office portfolio weighted to A/B grade assets which provides stable income and distributions (albeit fairly fully valued at stated NTA), and repositioning opportunities. Following a $200m equity raise in March (25% above current price) and the sale of a non-core asset (464 St Kilda Road) ABP's gearing has fallen to c.30% (the low end of peers, and below their 35% target). Additionally, ABP has recently increased its interest rate hedging (now 76% and 50% hedged in FY23 and FY24), which is prudent given the backdrop of rising rates. As such ABP now have balance sheet optionality which should allow them to deploy capital into accretive assets as opportunites arise in tougher economic times. While we are more negative than positive on commercial property in unlisted markets, ABP currently trades at a c.30% discount to NTA ($3.70) which provides a buffer to any negative valuation movements, it trades at a c.20-25% discount to listed peers based on our estimates, and is yielding 6.6% based on 18.0cps company distribution guidance. We believe ABP should revert towards its sector peers and should settle between current levels and NTA over time given the quality and resiliency of its asset base.

**APM Human Services International (APM.AU)** – APM is a global provider of human services, assisting governments in managing disability, employment, and health services ($2.5B market cap). It has a market-leading position in employment services, helping challenged individuals (through disability, illness, welfare etc.) find sustainable employment. After a soft listing in November last year we had several discussions with management, led by founder and major shareholder Megan Wynne, which confirmed our beliefs that, either the market did not fully understand the company, or it had underestimated the company's potential to win these lucrative contracts (and roll their big contracts in Australia which they have subsequently done). We take comfort in APM's ability to perform services better than competitors (refer below charts and refer to their recent market share win in the new Workforce Australia scheme), which should drive future contract awards. Additionally, there is a lot of optionality yet to be priced, including pending contract wins in Canada (a large new market), an expansion into Sweden, a recent debt refinancing, an increase in their key Disability Employment Services contract allocation (likely in August), and what should be a strong maiden full year result and outlook statement also in August. Our $3.68 target price is based on a 25%/50%/25% blend of DCF, P/E (16.5x FY23) and EBITA (12.0x FY23) multiple analysis where we believe we are being conservative.

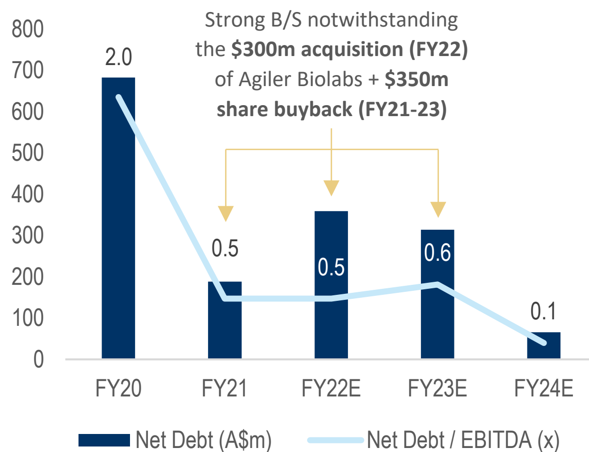



Source: Indian Pacific Funds Management




Source: Department of Education Skills & Employment

**Healius (HLS.AU)** – HLS (formerly Primary Health) is an Australian healthcare company with large market shares in the pathology, diagnostic imaging, and day hospital sectors. It provides these services predominantly under a bulk-billing model with funding flowing under the Federal Medicare Benefits Schedule. HLS has been a big beneficiary from COVID, at its peak doing an average of >35k PCR tests per day at a rate of $100 per test and to date on our numbers HLS has generated in excess of $1.1bn of revenue from the tests as they played a leading role in helping the government manage the COVID crisis. Clearly, high PCR revenues won't last though and for this reason the stock has been heavily sold off (-33% CYTD). Nonetheless, having now fully divested out of both its medical centres and IVF clinics, we are attracted to the long term growth in HLS's core businesses (ex PCR) and we love the cash PCR testing has generated (something many investors seem to not count) which have driven significant balance sheet deleveraging (and funded a $300m acquisition). We see a base business recovery and believe the companies cost out program should be able to offset some of the cost pressures they (and the industry) are experiencing short term. We see c.50% upside to the current share price in the next two years as base business conditions normalise and the market stops fretting that PCR testing revenue is dropping fast.




Source: Company Reports, Indian Pacific Funds Management

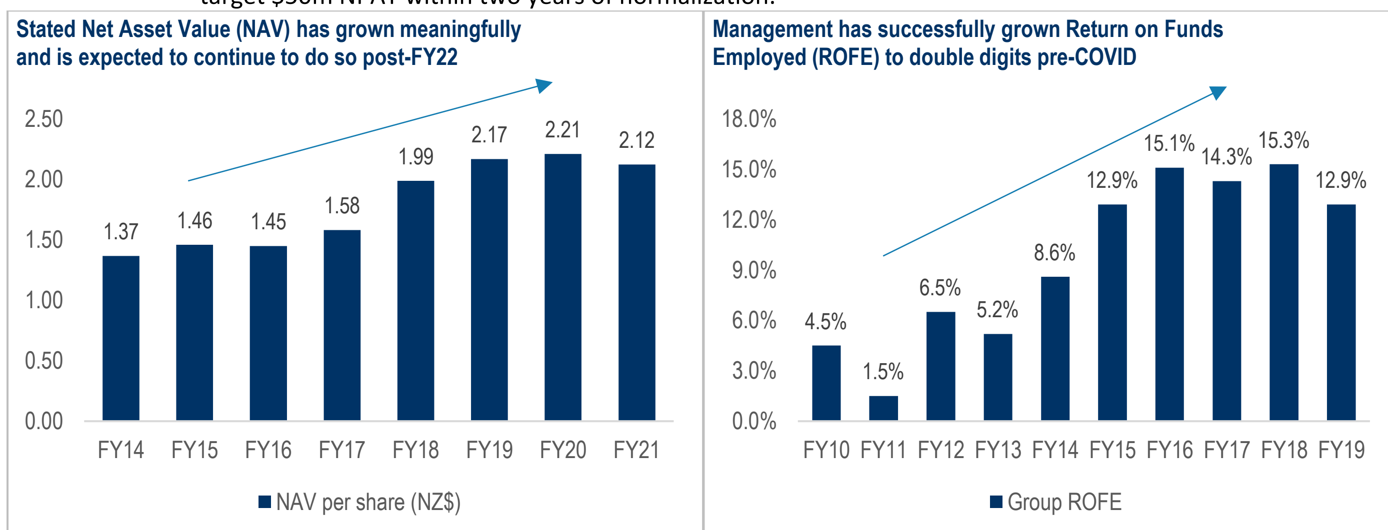
Source: Bloomberg

**PSC Insurance Group (PSI.AU)** – PSI ($1.4bn market cap) is a highly acquisitive insurance broking group led by three founders, Paul and John Dwyer, and Brian Austin (Chair). All three came out of OAMPS which was sold to Wesfarmers back in 2006, at which point PSI was formed and PSI is really following the same playbook, aggressively growing with the likely end game of selling out to a large industry player. We love that we are able to "hitch our wagon" to these industry stalwarts who are heavily aligned to shareholders (they own around 35% of the company). Having grown at circa 25% NPATA CAGR since 2016, Melbourne based PSI now own and operate over 40 businesses which are diversified firstly by geography across Australia, NZ, and the UK, and also across many classes and lines of insurance in which their brokers operate. Operating central services and leveraging the various businesses off each other, they have become experts at extracting both cost and revenue synergies from aquisitions. PSI is a very different proposition to investing in an underwriter such as IAG as they

don't take any underwriting risk, so they are not exposed to adverse weather events or climate change directly (they just receive fees from the insurers as businesses clients roll their policies every year). We like the defensive nature of PSI's income stream (the product is largely non-discretionary) and we hope to hold (and add to) this position as they execute on internal targets to doube revenue in the next four years. We value PSI at $4.35 via DCF but in all likelihood it will just be taken out on a multiple of c.FY25 earnings (at an attractive premium we're guessing) so while it is priced as a growth stock, we think it is deservedly so and we are comfortable holders.

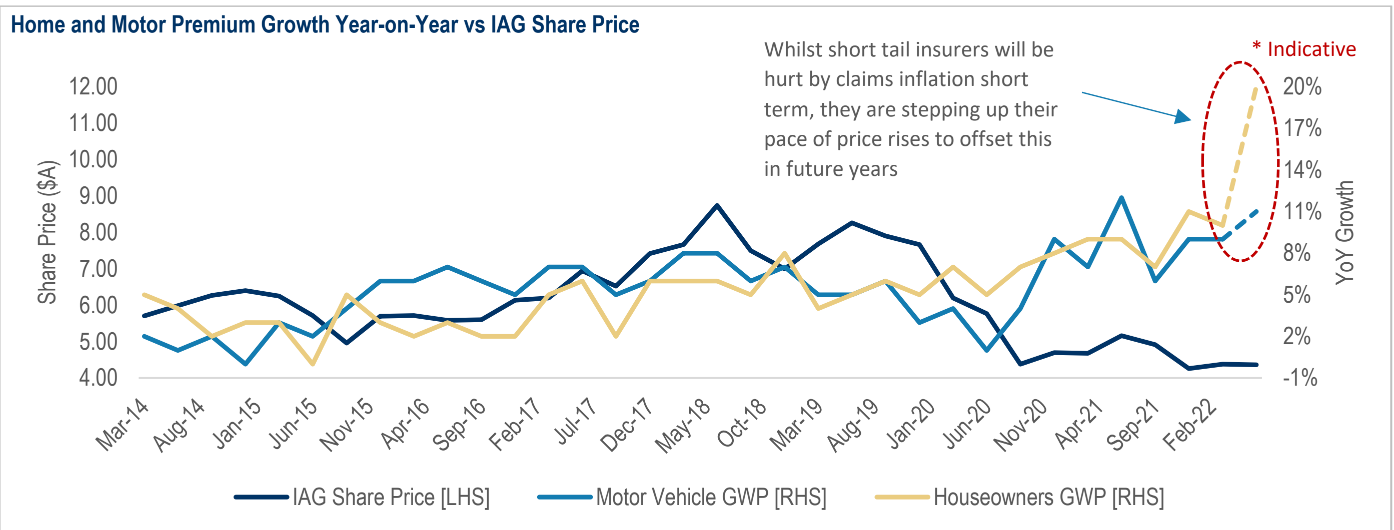
**Aristocrat Leisure Group (ALL.AU)** – ALL (market cap of A$23.2bn) is the WORLDS leading developer and manufacture of slot machines with revenue from more than 90 countries. It has the number one position in the key North American market where it competes in the Class II and III gaming operations market (revenue share model which is recurring) and in the Class III outright sales market. ALL also operates an online social casinos segment, leveraging its developed game catalogue to offer its content via Facebook, Apple iOS, and Android. We think the risk/reward is particularly attractive at the moment, given the digital growth and capital management opportunities, coupled with strong execution by management (despite a challenging cyclical environment). ALL possesses timely balance sheet optionality post the shareholder rejection of their Playtech (PTEC.LN) bid, with a net cash position of A$524m, paired with strong free cash flow generation. From here the company has three avenues to deploy their excess cash: 1) via organic investment; 2) inorganic investment into real-money gambling; and 3) capital returns to shareholders. Having already announced a A$500m share buyback at the 1H22 result, we think the market would be most excited by deployment via the second option above. Valuation is particularly undemanding for a business with extremely strong FCF generation and a multi-year growth pipeline across multiple avenues (iGaming to be live across two US jurisdictions by year end). With the stock trading on a modest 14.4x F23 EV/EBIT and our conservative valuation (a blend of SOTP, PE and EBIT analysis) sitting at $43.80 (+27% upside) we see the recent pullback in ALL as a great long term buying opportunity.

**Tourism Holdings (THL.NZ)** – THL (NZ$370m market cap) has been a New Zealand listed company since 1986 and is the largest provider holiday campervans (RV's) for rent and sale in Australia and New Zealand, and the second largest in North America, under brands you would recognise such as Maui and Britz. We initially invested in THL during the big COVID pullback in 2020 as we saw it as a risk free play on the recovering international tourism sector, as we were able to initiate our position below NTA (the value of their fleet less debt which at the time was around NZ$2.00) after the share price halved with international border shutdowns. We have long admired THL's management team from afar, with their ability to generate higher than peer Return on Funds Employed, largely due to their disciplined fleet management (which is the key to winning in this inustry), and superior balance sheet management. This indeed played out post COVID as management entered the pandemic with a strong starting NTA position which allowed them to reduce net debt from c.NZ$200m down to just ~NZ$40m earlier this year by reducing their fleet size (as demand for vehicles soared). As it stands the stock is still only trading at a small premium to NTA, and operationally they are now firmly on the road to post-pandemic recovery with recent feedback we received from management indicating a strong recovery in all international markets as travel restrictions are lifted. Pleasingly, average yields in all countries are returning to pre-COVID levels or higher. This is in addition to the unrealised embedded value in the fleet from used vehicle inflation. Due to their very strong balance sheet position, THL is also currently attempting to take over their key Australian and NZ peer Apollo Tourism (ATL.AU) which, in our view, remains a free option largely unpriced for both companies. If successful, it would result in the combined group becoming an even more dominant player in Australia and New Zealand, significantly stronger in the US and Europe, and deal closure would offer up very large synergies to THL shareholders. Our $3.30 target price is based on a 10x P/E multiple of a company stated target $50m NPAT within two years of normalization.



Source: Company Reprots, S&P Capital IQ

**Insurance Australia Group (IAG.AU)** – IAG ($10.7bn market cap) operates as a general insurancer largely in a (close to) duopoly market structure in Australia and NZ (along with Suncorp Insurance). While higher than historic perils (owing especially to severe weather events over in the east coast) will no doubt dent the FY22 reported margins (as they did in the prior two years!), we are playing the patient game here believing that a more normal perils year will come along at which point earnings will rise by 30%+, and then market doing as the market does, will then rerate the stock back to more normal multples +30% higher (just as it's derating it on depressed earnings at present). We also find comfort (wehre others don't) in the IAG's storng balance sheet and at some point think we could see a capital return due to their over raise (and provision) and then subsequent court win around Business Interuption insurance. Claims inflation is the enemy of all short tail insurers at present, and we're not expecting anything pretty at the upcoming result, but with a fairly large degree of top line pricing power, and evidence of that being exercised (refer below chart), we see IAG as a deep value, out of consensus, investment with leverage to rising rates (via shareholder and technical reserve returns) which we think will offset a lot of the claims pressure they are seeing. Our $5.03 target price is based on a modest 16.0x P/E multiple (on 31.5c EPS versus 46.5c achieved in 2018).



Source: Australian Prudential Regulation Authority; IPFM estimate post March 2022

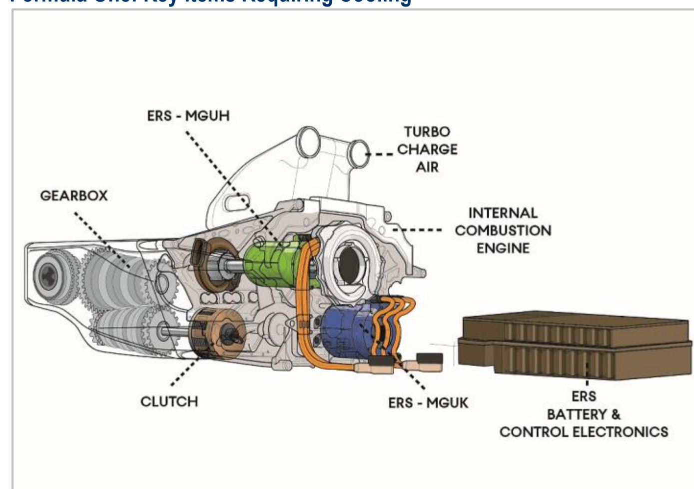
**ReadyTech Holdings (RDY.AU)** – RDY (A$328m mkt cap) is a leading SaaS provider for the education and workforce solutions segments in Australia, and the government and justice industry segments in Australia and the UK, with over 4.6k customers. RDY operates in industry verticals with large addressable markets and solid long-term growth characteristics. We are attracted to RDY's high recurring SaaS revenue >85%, high revenue retention rate of over 94%, strong consistent EBITDA margin of over 35%, which is at the upper end of its peer group, and strong pricing power with cost inflation passed through to customers in annual price increases. Management is led by founder and CEO Marc Washbourne along with one of the stronger CFO's we regularly speak to, Nimesh Shah, and we consider the RDY leadership team capable of executing on their aggressive growth strategy (albeit we don't factor in their full ambitions to double revenue to >A$140m by FY26 organically). RDY has screened as very cheap when compared to their peers (many that are unprofitable) and that has served as well as their peer group have seen big share price falls in the last 6 months as RDY has been largely flat. Even after those falls it remains at a good discount on an absolute and growth-adjusted basis versus peers and we believe it can narrow the discount by delivering on their stated targets. Our $4.00 target price is based on a blend of DCF, P/E and EBITA (given the A = non-cash) multiples.

**Capricorn Metals (CMM.AU)** – WA based gold producer CMM ($1.2bn mkt cap) is our preferred ASX gold exposure with management's strong track record the key initial attraction for us. With their maiden project (Karlawinda) delivered on time, on budget, in a challenging cost environment in mid 2021, the operation has hardly skipped a beat delivering at the top end of their 110-120koz pa production guidance in FY22 and generating $30-40m cash per quarter which allowed them to pay back their Macquarie project loan facility within their first year of operation. In the current environment of massive cost inflation for the miners, clearly you want to own the the lowest cost (AISC) players and CMM is amongst the lowest cost ASX pure-play gold producers (reporting A$1,086/oz in the March 2022 quarter, with management re-iterating full-year AISC guidance of A$1,100 - $1,200). This compares against its peer group average of ~A$1,560. From here, all eyes are turning to news flow from their Mt Gibson gold asset which they acquired (or some might say stole) for ~$20/resource oz as Karlawinda commenced production. There is currently a massive 80,000 metre drill program underway with strong drill resutls published in April, so we should see a significant Reserve upgrade in September, followed by feasibility study in December this year. In time, CMM will likely become a steady

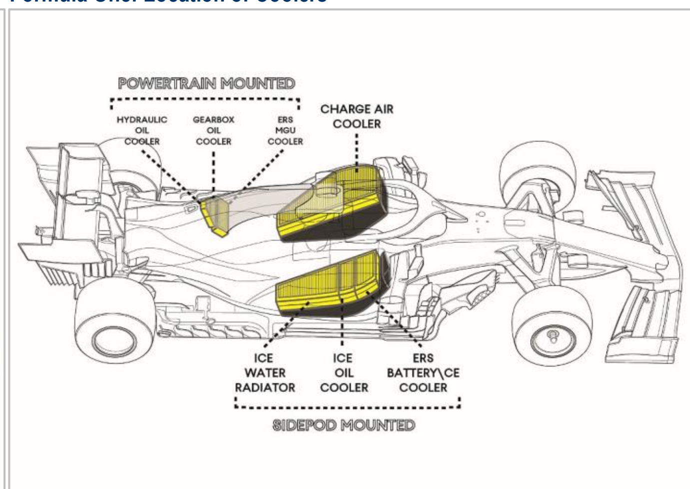
dividend payer (refer the Regis Resources playbook from this management team) which will likely see a further premium rating built in to the CMM share price. We derive our $4.30 target price (+43% upside) using DCF and can see a path to $5.00 should the company get to some of their stated long term goals (c. 300koz production in 3-4 years).

**PWR Holdings (PWH.AU)** – we are pleased to advise that one of our favourate small cap stocks recently re-entered the fund, having been a great contributor in our initial years but we sold PWH in late 2021 on valuation grounds. We added it back into the portfolio at around $6.00, with the stock having dropped 40% from their May highs $10.30. Many of you will know this story from our previous writeups but for those that don't, PWH is a leading provider of customised cooling solutions to the global motorsports market as well as the wider automotive industry. It develops and manufactures the majority of the radiators, intercoolers, oil coolers, and heat exchangers, used in top-tier global championships such as Formula One, NASCAR, GT/LMP, and Supercars. PWH is a clear leader in a market with low competition and high barriers to entry, high-quality client base, and highly innovative manufacturing ability. When the valuation is acceptable, it ticks all the boxes we look for in companies – a founder led business, with Kees Wheel, an industry icon, leading the company with an iron fist (in a velvet glove), a balance sheet that is almost always net cash (he hates debt), an aggressive growth profile, huge IP and barriers to entry (paid for by their clients … think Redbull Racing, McLarren, Ferrari etc), and fantastic long term structural trends as demand for their IP to be applied to new market verticals such electric vehicles, military, and space applications is becoming a reality today. We recently caught up with Kees and PWH's CFO, Martin McIver, in their Gold Coast head office and while the short term growth has been good, we are very excited about the big long term opportunites ahead (in FY25 and beyond). Premium stock – yes, but a premium growth profile with optionality to match.

**Formula One: Key Items Requiring Cooling**




**Formula One: Location of Coolers**




Source: Motorsport Technology; Formula One

## Outlook

As we kick off the new financial year, the global economy is on a tenuous footing. We all know the reasons why; rising inflation, supply gluts, war and other geopolitical risks, resultant internatlisation of trade (and associated cost increases), global slowdown and the various cyclical impacts that will have, rising rates from lows never seen before, and the list goes on. While we don't have a crystal ball, and don't even consider ourselves macro forecasters (rather, bottom-up stock pickers), we are cognisant that as we stand today (that is, with the S&P having delivered its worst first half in 50 years), these are largely the "known knowns". We also know that the market moves very fast these days to factor in the known knowns. It's also pretty quick to factor in the "known unknowns", the key one being whether rising rates really will result in a long recession which is now being priced in to some sectors and share prices. The big factor that will drive markets in the next 12 months is whether markets have factored in too much too soon with regard to rising interest rates. If they have (and rates retreat), then some parts of the market will gain comfort on valuations with discount rates unlikely to push higher thereby not impacting valuations any more than they already have. This is actually what has happened in the last couple of weeks with the US and AUssie yield curves retreating significantly from where it stood a month ago. Reading the curve, it's now saying, "if rates move up as fast as they it looks like they will, we're headed for a recession and in fact rates will have to be cut in 2024 to re-stimulate the economy". At the point where bond rates peak on the current inflationary surge, there will be a strong case for a bounce in equity markets as bad news likely (once again) becomes good news (for rates). The question in the short term, is how much pain we have to go through to get to that point (or are we already there?). Lastly, there are the "unknown unknowns", and these have been the real driver of inflation and rising rates in the last few years – ie. COVID-19 and the Russia/Ukraine wa. Could the war end, grain and oil prices fall, and pressures on central banks ease significantly in 6-12 months? It feels too early to position for that, but nonetheless it is a distinct possibility.
The silver lining to the market turmoil is the signficiant de-rating in equity markets means the valuation cases of companies (both ones we own and those on our "wishlist"), have reverted back towards or below the long-run averages and we are genuinely

excited by the quality of companies we are now able to rebuild positions in at the most attractive levels we have seen in a long time. These are the times we are able to set the portfolio for the next 3-5 years. Even in poor economic environments, there great companies, with strong balance sheets, with strong management teams who possess the "will to win", that still manage grow earnings and/or protect their businesses better than the rest.

It is with this in mind, that we set out to build and protect your (and our) wealth in the year, and years, ahead. We look forward to working hard on your behalf in fiscal year 2023 and as always, please don't hesitate to contact me.

Regards,

Preston Hamersley
Portfolio Manager

## About the Fund

The Indian Pacific Fund is an Australian Equity long/short fund founded in February 2018. The fund has an absolute return focus (with long bias), has no cash limit, and can invest in both large and small cap companies. The investment process is a fundamental bottom-up investment process with a focus on balance sheet risks and identifying companies with strong cash flows, in good industries, with strong management teams. The fund was founded with the view that whilst markets rise in the long term it is always prudent to maintain the flexibility to hold more cash when markets are overly optimistic, and selectively short stocks if opportunities arise.

| | | | |
|---|---|---|---|
| **Holdings** | Typically 15-25 long, selective short positions | **Investor Eligibility** | Wholesale Clients |
| **Management Fee** | 1.0% of the GAV of the Fund, plus GST | **Prime Broker** | Morgan Stanley |
| **Performance Fee** | 20% of Outperformance over RBA Cash, high water mark | **Fund Administrator** | Apex Fund Services Ltd |
| **General enquiries** | | **Contact the Fund Manager** | |
| E admin@indianpacificfm.com.au | | E preston@indianpacificfm.com.au | |
| W indianpacificfm.com.au | | P +61 8 6280 0129 | M +61 403535820 |

This newsletter is not to be distributed to any retail clients within the meaning of the Corporations Act 2001 (Cth). This newsletter contains performance figures and information in relation to Indian Pacific Fund Main Series. The actual performance for your account will be provided in your monthly statement. Actual performance may differ for investments made in different classes or at different times throughout the year. This newsletter is intended to provide general background information only. It does not constitute investment, tax, legal or any other form of advice or recommendation to be relied upon when making an investment or other decision. Past performance is not a reliable indicator of future performance. While all reasonable care has been taken to ensure that the information in this document is complete and correct, no representation or warranty is given as to the accuracy of any of the information provided, including any forecasts. To the maximum extent permitted by law, the Trustee and Investment Manager and related bodies corporate, directors, employees and representatives are not liable and take no responsibility for the accuracy or completeness of this document. No investment in the Fund should be made without fully reviewing the information, the disclosures and the disclaimers contained in the Information Memorandum.