Zenith Investment Partners

Highly Recommended
Recommended
Approved
Not Rated
Redeem

Product Assessment

Pengana Australian Equities Fund

Report data as at 31 May 2021
Rating issued on 24 Jun 2021

APIR Code
PCL0005AU

Asset / Sub-Asset Class
Australian Shares
Absolute Return

Investment Style
Neutral

Investment Objective
To achieve a total investment return (after fees and taxes), in excess of the risk free rate plus a margin to compensate investors for the extra risk of investing in Australian equities, with a volatility of return less than the Australian equity market.

Zenith Assigned Benchmark
S&P/ASX 300 (Accum)
RBA Cash Rate

Net Returns (% p.a.)

	5 yrs	3 yrs	1 yr
Fund	8.09	8.50	26.55
Benchmark	10.22	10.11	28.74
Median	7.00	6.67	21.67

Income (% p.a.)

	Income	Total
FY to 30 Jun 2020	7.49	-3.86
FY to 30 Jun 2019	7.78	3.56
FY to 30 Jun 2018	4.30	8.07

Fees (% p.a., Incl. GST)
Management Cost: 1.10%
Performance Fee: 10.25% on outperformance of the RBA Cash Rate plus a 6% p.a. hurdle (after fees).

VIEWPOINT

The Fund, managed by Pengana Capital Group Limited (Pengana), provides investors with a concentrated and high conviction exposure to Australian equities. The Fund invests across the market capitalisation spectrum, however, where opportunities that meet Pengana's investment criteria cannot be identified, up to 100% of the portfolio may be held in cash. Zenith maintains a high opinion of Pengana, given its experienced team of investment professionals and robust investment process.

Pengana is an Australian funds management boutique founded in 2003. Pengana offers a diversified range of equity-based strategies totalling $A 3.8 billion in funds under management, as at 31 May 2021. The Australian equities boutique responsible for the Fund managed approximately $A 981 million, as at the same date.

The Australian equities boutique was established in 2008 and consists of four investment professionals. The team is led by Rhett Kessler, who is supported by Anton du Preez. Although relatively small by industry standards, Zenith notes that Pengana's investment team size is calibrated to the Fund's investment strategy.

Pengana conducts detailed fundamental analysis to identify stocks that exhibit favourable industry dynamics. Once a stock has been identified, the collective members of the team assess its viability based on its valuation. Whilst the valuation process comprises an assessment of both qualitative and quantitative factors, Pengana has a particular focus on assessing after-tax cash earnings yields by analysing financial statements. In Zenith's opinion, Pengana's stock selection process is thorough and leverages the experience of the investment team, particularly the strong accounting experience of several team members.

Responsibility for portfolio construction rests with Kessler, with the Fund expected to hold between 20 and 25 positions. However, the Fund's number of positions has consistently exceeded this range over the most recent five-year period. Pengana has indicated that this is attributable to the increase in the strategy's assets, which has necessitated a more patient approach when entering and exiting stock positions.

In addition to traditional stock selection, Kessler may invest in positions that reflect his views on the current global macroeconomic environment and potentially hedge out exogenous risks facing the portfolio. Whilst Zenith believes that many of these trades are consistent with Kessler's capital preservation philosophy, we would prefer Kessler to focus on his core competency of fundamental stock research. However, Zenith acknowledges that these trades are used opportunistically and are not expected to form a material part of the Fund.

Zenith notes that effective 1 July 2019, the performance fee hurdle rate changed to the RBA cash rate plus 6% p.a. (after fees), rather than solely the RBA cash rate. Zenith views the Fund's change in fee structure positively, as we believe the hurdle rate is now more reflective of the Fund's risk profile. However, given that the Fund's risk exposures are primarily driven by Australian equities, we would prefer that the Fund's performance fee is linked to an Australian equity benchmark, which we believe would provide stronger alignment.

FUND FACTS

- High conviction, benchmark unaware portfolio
- Flexibility to invest up to 20% in international equities
- Expected portfolio turnover between 20% p.a. and 30% p.a.
- Zenith has assigned the Fund a Responsible Investment Classification of **Aware**

ABSOLUTE RISK (SECTOR)

VERY HIGH
▶ HIGH
MODERATE
LOW
VERY LOW

RELATIVE RISK (FUND WITHIN SECTOR)

Geared
▶ Active - Benchmark Unaware
Active - Benchmark Aware
Index - Enhanced/Fundamental
Index

INCOME DISTRIBUTIONS PER

MONTH | QUARTER | **6 MONTH** | ANNUM

INVESTMENT TIMEFRAME

1-2 YRS | 3-4 YRS | 5-6 YRS | **7+ YRS**

APPLICATIONS OF INVESTMENT

SECTOR CHARACTERISTICS

The Zenith 'Australian Shares - Large Companies' sector consists of long-only strategies investing in the Australian equity market. The sector incorporates both benchmark aware and benchmark unaware strategies and focuses predominantly on large capitalisation stocks. The sector is one of the most competitive in the investment landscape, based on the number of managers and strategies available to investors. Despite the competitiveness of the sector, the Australian share market has historically provided many opportunities for active management, with the median active manager outperforming a passive index over the longer term.

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

The Australian share market, as represented by the S&P/ASX 300 Index, is highly concentrated and narrow. Technically, a company is considered large cap if it falls within the S&P/ASX 50 Index, with companies falling between the S&P/ASX 50 and S&P/ASX 100 considered mid cap. All stocks outside of the S&P/ASX 100 Index are considered small capitalisation stocks.

As at 31 May 2021, 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 29.9% of the Index, and Materials approximately 20.7%. The split between Industrials and Resources stocks was approximately 76%/24%. The top 10 stocks represented approximately 44.7% of the weighting of the Index, and the top 20 stocks represented over 55% of the Index.

PORTFOLIO APPLICATIONS

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 market also only represents approximately 2% of global equity markets (in terms of market capitalisation). Therefore, to mitigate this concentration risk, Zenith recommends that investors diversify their investments across asset classes, both domestically and globally.

The Fund offers an opportunity to diversify a portfolio, given its concentrated and benchmark unaware approach. The Fund is expected to exhibit significantly different risk/return characteristics and less correlation to other large-cap funds throughout different stages of the investment cycle. Therefore, Zenith believes the Fund would blend well with other large-cap Australian equity funds or funds that hold investments in the S&P/ASX 20 Index.

Investors should be aware that whilst the majority of the Fund is expected to be invested in the mid to large capitalisation segment of the market, the Fund has historically maintained a meaningful exposure to small and micro-cap companies. Over the most recent five-year period the Fund has had an average small and micro-cap exposure of 38%.

In addition, where opportunities that meet Pengana's investment criteria cannot be identified, up to 100% of the portfolio may be held in cash. Historically, the Fund's cash exposure has ranged between 8% to 60%. In addition, Pengana may also invest up to 20% of the Fund in internationally listed companies, although Zenith notes that this facility has rarely been utilised outside of New Zealand listed companies.

The Fund's portfolio turnover is expected to range between 20% p.a. to 30% p.a., which Zenith considers to be low. Pengana has indicated that approximately 50% of the expected turnover is attributed to resizing existing positions and approximately 50% is due to complete sales and new additions. Given this expected level of turnover, the majority of the Fund's returns 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 highly 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.

RISKS OF THE INVESTMENT

SECTOR RISKS

Funds within the 'Australian Large Cap' sector are exposed to the following broad risks:

MARKET & ECONOMIC RISK: As is the case with all long-only Australian Share funds, the biggest risk to performance is a sustained downturn across the Australian share market. In addition, 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 time frame.

SPECIFIC SECURITY RISK: This is the risk associated with an individual security. The price of shares in a company may be affected by unexpected changes in that company's 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 quickly enough due to insufficient trading volumes in the market. When trading volumes are low, sellers can significantly impact the price of a security when attempting to quickly exit a material position.

STYLE BIAS RISK: Australian equity managers will either employ a growth, value or neutral (combination of value and growth) styled approach to investing. Each style is conducive to certain market conditions. That is, growth should outperform value in an upward-trending market and vice versa in a downward-trending market. As with market risk, investors should adhere to the Fund's investment time frame to avoid short-term market movements and style impact.

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

REGULATORY RISK: The ASIC Regulatory Guide 97 ‘Disclosing Fees and Costs in Product Disclosure Statements and Periodic Statements' came into effect on 1 October 2017 and seeks to establish a common framework for disclosing fees with respect to registered managed investment schemes issued to retail investors.

In November 2019, ASIC released its final recommendations, with proposed changes to be phased in from 30 September 2020, with all Funds required to be compliant by 30 September 2022.

In its current form, RG97 will not impact the actual costs (or after fee returns) on existing investments. Rather, the guide is focused on providing increased transparency with respect to the costs of management. Given this, it is feasible that under RG97, investors become more sensitive to the costs charged and seek lower cost alternatives, potentially leading to fund outflows.

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: As with most boutique fund managers, Pengana is subject to a level of key person risk. In Zenith's view, Rhett Kessler, as portfolio manager and ultimate decision-maker, is critical to the Fund. Whilst he has significant support from Anton du Preez, his departure would warrant an immediate review of the Fund's rating. Zenith notes that this risk is somewhat mitigated by Kessler's substantial co-investment in the Fund and his significant equity ownership in the vehicle holding profit share interests derived from the Fund.

CAPACITY RISK: Excessive levels of funds under management (FUM) can materially hinder the ability of a manager to meet its performance objectives. As at 31 May 2021, Pengana managed approximately $A 981 million in the strategy. Pengana has provided a capacity target of 0.5% of the total market capitalisation of the S&P/ASX mid and small-cap indices (representing approximately $A 3.1 billion, as at 31 May 2021). Zenith believes Pengana’s capacity target is at the upper end of what can reasonably be managed under the strategy. In addition, Zenith notes that over time, Pengana has continuously revised its capacity limit upwards.

Pengana limits the Fund’s exposure to mid and small-cap equities to 50%. However, Zenith notes that historically the strategy's exposure to mid and small-cap equities averaged greater than 50%. Zenith believes this development was an indication that the Fund may have been experiencing potential constraints resulting from high levels of FUM. However, we note that the Fund has experienced a significant decrease in FUM over recent years and as such, Zenith believes that capacity is not as pronounced an issue as it has been in the past. However, we will continue to monitor FUM to ensure it does not begin to impact Fund performance.

BENCHMARK RISK: Zenith notes that the Fund's performance fee is assessed against any increase in net asset value (NAV) subject to three payment conditions; recoupment of prior negative performance, the return must exceed the cumulative RBA Cash Rate plus 6% and the performance fee cannot reduce the net return below the RBA Cash Rate. Given that the Fund's risk exposures are primarily driven by Australian equities, we would prefer that the Fund's performance fee is linked to an Australian equity benchmark, which we believe would provide stronger alignment.

CONCENTRATION RISK: Given the Fund's concentrated nature, the degree of stock-specific risk is higher than more diversified Australian equities peers, leading to the potential for more volatile returns. The expected Tracking Error will also be higher as the Fund may deviate significantly from the benchmark. Furthermore, the lack of formal risk constraints could lead to concentration risk or biases to certain stocks and sectors.

CURRENCY RISK: Investments in international markets are exposed to changes in the value of the Australian dollar (AUD) relative to foreign currencies, which may lead to increased levels of volatility. The Fund is permitted to invest up to 20% in stocks listed on foreign stock exchanges.

FINANCIAL INSTRUMENT RISK: Kessler has the ability to utilise a number of financial instruments to express macroeconomic views in the Fund. Up to 20% of the Fund in aggregate may be held in exchange traded funds (ETFs), listed bond securities and derivative instruments. Zenith does not believe that Kessler possesses a competitive advantage outside of Australian equities. Accordingly, we would prefer that the Fund be invested in only Australian equities or cash. However, Zenith acknowledges that these trades are used opportunistically and have not historically formed more than 10% of the Fund.

QUALITATIVE DUE DILIGENCE

ORGANISATION

Pengana Capital Group Limited (Pengana) is an Australian funds management boutique founded in 2003. Pengana aims to find and support experienced fund managers with long track records, providing staff and support whilst leaving the investment staff entirely responsible for the performance of the funds that they manage.

In June 2017, Pengana merged with Hunter Hall International Limited (ASX: HHL). As a result, HHL was renamed Pengana Capital Group Limited (ASX: PCG). The combined entity offers a diversified range of equity-based strategies totaling $A 3.8 billion in funds under management (FUM), as at 31 May 2021.

PCG is majority-owned by Pengana staff and Washington H. Soul Pattinson (ASX: SOL). SOL has a 39.25% shareholding in PCG after holding a material interest in Hunter Hall prior to the merger and subsequently purchasing NAB Asset Management's stake in Pengana in March 2017. The majority of equity ownership resides with Pengana staff and directors, which Zenith views positively.

The Fund was established in July 2008 by Rhett Kessler in conjunction with Pengana. Pengana and the Fund's management team equally share in the profits generated by the business unit.

As at 31 May 2021, Pengana managed $A 981 million in the strategy, all of which was in the Fund.

INVESTMENT PERSONNEL

Name	Title	Tenure
Rhett Kessler	CIO and Senior Fund Manager	13 Yr(s)
Anton du Preez	Deputy CIO and Fund Manager	12 Yr(s)

Pengana's Sydney-based Australian equities team is led by Rhett Kessler. Kessler is supported by Anton du Preez and two analysts, Mark Christensen and Chris Tan.

Kessler has over 20 years of experience in investment management, including senior fund management roles at Liberty Asset Management in South Africa, UBS Australia and IAG Asset Management. Kessler is responsible for stock selection and oversight of the company models derived by each analyst. Zenith has met with Kessler on several occasions and regards him highly, owing to his portfolio management and analytical skills.

Each member of the team has generalist responsibilities and the team is collectively responsible for idea generation, stock valuation assessment and portfolio construction. As Pengana's investment process does not incorporate any formal filters, each investment team member is responsible for generating stock ideas from the entire investable universe.

Responsibility for portfolio construction rests with Kessler, with du Preez assisting in a backup capacity. Team interaction is frequent, with a team meeting occurring each week to discuss stocks and valuations. Although relatively small by industry standards, Zenith notes that Pengana's investment team size is calibrated to the Fund's investment strategy.

Pengana and the Fund's management team equally share in the profits generated by the business unit, in addition to having significant co-investment in the Fund. Zenith believes there is an appropriate alignment of interests between the team and investors.

The investment team may draw on the investment insights of a panel of nine additional investment professionals from the other Pengana equity teams. While Zenith views the collegiate-styled approach with which investment ideas are shared and discussed as a positive, further resources dedicated to the Fund would provide a greater level of confidence given the breadth of the investment universe.

INVESTMENT OBJECTIVE, PHILOSOPHY AND PROCESS

The Fund's investment objective is to achieve a total return (after fees and taxes), in excess of the RBA Cash Rate plus a margin to compensate investors for the extra risk of investing in Australian Equities, over a medium to long-term investment horizon, with a volatility profile that is less than that of the Australian equity market.

Zenith would prefer to see the delineation of a specific outperformance target, as opposed to a descriptive, qualitative objective. Zenith believes this would provide investors with greater transparency with regards to returns expectations and to the level of risk embedded in the Fund.

Pengana's investment philosophy is based on the belief that markets are inefficient over the long term and the ability to accurately forecast becomes more difficult as the time horizon increases. Pengana seeks to take advantage of these market inefficiencies by adopting a long-term investment horizon when positioning the Fund.

Pengana utilises a benchmark unaware, fundamental approach with a macroeconomic overlay to portfolio construction. Pengana has a particular focus on assessing after-tax cash earnings yields. In practical terms, for a security to be eligible for the portfolio, it is expected to deliver an after-tax cash earnings yield of 6% p.a. (which equates to a return of the risk-free rate plus 4% p.a.) as a minimum investment hurdle. The investment process is based on Pengana's core belief that capital preservation is preferred over supernormal returns and that if Pengana is unable to find appropriate investments from a risk-return perspective, the Fund will remain invested in cash.

SECURITY SELECTION

The Fund's primary investable universe all companies listed on the Australian Stock Exchange, however, Pengana has the flexibility to invest in hybrids, listed bonds, precious metals, exchange traded funds, derivatives and international equities.

Investment ideas are generated from external sources including investment banks, research houses, industry specialists, competitors, suppliers, customers, company visits and investment professionals from other Pengana equity teams. Research ideas are shared internally through various forums including weekly team meetings chaired by Kessler. Stock ideas are centred on companies exposed to favourable industry dynamics such as strong pricing power over customers and/or suppliers. Kessler appraises approximately ten new ideas per day with one or two a month typically making it into the portfolio.

Once a stock of interest has been identified, the team assesses its viability as a collective group, based on its valuation. The valuation process comprises an assessment of both qualitative and quantitative factors.

The qualitative assessment seeks to gain a thorough understanding of the underlying business model, management competence, business model resilience and industry structure. As part of its qualitative assessment, Pengana conducts a regular company visitation program, with the investment team attending approximately 150 company visits annually.

The quantitative assessment derives a company valuation through an internally generated financial model template. Through an understanding of the company's underlying business model, as well as an in-depth analysis of financial statements, the team produces detailed half-year forecasts on several key valuation metrics. Zenith notes that the majority of the investment team have accounting backgrounds, a skill set that compliments the investment process.

In order for a stock to be considered for inclusion in the Fund, it must meet the following criteria:

- Transparent and resilient business models
- Rational cash earnings multiples
- Competent management with a track record of integrity
- A favourable relationship between the market price and the future cash flows of the business
- Solid balance sheet
- Strong underlying intrinsic asset valuation

In addition to traditional stock selection, Kessler may invest in a number of discrete positions that are used as both a source of return enhancement and risk mitigation. These positions are expected to reflect Kessler's views on the current global macroeconomic environment and can range from expressing currency views through foreign-denominated exchange-traded funds (ETFs), buying put options on banks to alleviate concerns on residential housing markets and investing in hybrid securities. Zenith believes the use of such a broad mandate represents a deviation from Kessler's Australian equity-centric trading background, and accordingly, Zenith would prefer the Fund be invested in securities that have been subject to Pengana's fundamental due diligence. However, Zenith acknowledges that these trades are used opportunistically and are not expected to form a material part of the Fund.

In Zenith's opinion, Pengana's stock selection process is thorough and leverages the experience of the investment team, particularly the strong accounting-based experience of several team members.

PORTFOLIO CONSTRUCTION

Responsibility for portfolio construction rests with Kessler.

In constructing the Fund, Kessler prioritises the fundamental quality of a business, with the internally derived valuation gap being a secondary consideration. Prior to entering a position, Kessler will consider the market's appetite for risk, potential merger and acquisition activity and market sentiment (including technical analysis and share register composition). The decision to buy or sell a security and the resultant portfolio weighting is based on Kessler's level of conviction and the attractiveness of the risk/reward profile.

The starting point is for the Fund to be 100% invested in cash. When the team identifies investment ideas that have the potential to meet the investment hurdle (an after-tax cash earnings yield of 6% p.a.), then capital will be deployed.

The Fund is concentrated and expected to hold 20 to 25 core stock positions, with position sizes typically between 3% and 7%. The maximum allocation to an individual stock is 10% at purchase, with a hard limit of 15% to allow for capital appreciation. There are no strict sector or benchmark limits imposed. The Fund can invest up to 20% in international equities, with input from Pengana's global equities resources to assist in identifying ideas.

Although Pengana has consistently held more than 25 stocks for the past five years, Zenith notes that the increase has been driven by non-core positions. Kessler has indicated that this is attributable to the increase in FUM, which has necessitated a more patient approach when entering and exiting stock positions. Zenith will continue to monitor portfolio exposures to ensure that the increasing FUM does not begin to impact Fund performance.

Kessler will sell a stock under the following circumstances:

- Reduced conviction in the investment thesis
- Target price has been reached

If Pengana is unable to find appropriate investments opportunities, the Fund will invest in cash. The decision to allocate to cash is an outcome of the investment process as opposed to a market timing decision. Historically, the Fund's cash allocation has ranged from 8% to 60%. Over the most recent five-year period, the Fund's cash exposure has averaged 17%.

The Fund's portfolio turnover is expected to range between 20% p.a. and 30% p.a. (in normal market conditions), which Zenith considers to be low. Kessler will also consider tax consequences when buying or selling a stock to ensure the portfolio is managed in a tax-effective manner.

Overall, Zenith considers the portfolio construction process to be intuitive, relying on Kessler's ability to structure a diversified portfolio.

RISK MANAGEMENT

Portfolio Constraints	Description
Number of Stocks	20 to 25 (Averaged 32 over the most recent five-year period)
Absolute Stock Weight (%)	max: 15% (10% at initiation)
International Equity Exposure (%)	max: 20%
Cash (%)	max: 100%
Expected Portfolio Turnover (% p.a.)	20% p.a. to 30% p.a.
ESG Constraints - Excluded Sectors	N/A

The portfolio is governed by the risk constraints detailed in the table above.

The first stage of risk management is undertaken by the investment team and is embedded within the investment process. The core of the risk management process undertaken by the investment team is in its bottom-up fundamental analysis of eligible securities in conjunction with its quantitative assessments.

The second stage of risk management is undertaken by an independent risk management team within Pengana. Various checks occur on a daily and weekly basis to ensure the Fund is compliant with its risk constraints. The independent risk management team utilises Bloomberg and an internally developed application to monitor risk across the portfolio.

Zenith believes the firm's risk management procedures are adequate and well-integrated into each stage of the investment process.

Responsible Investment Approach

Pengana has an established Responsible Investment Policy, last updated in 2020, that guides its investment decisions. In addition, Pengana is a signatory of the United Nations Principles for Responsible Investment (UNPRI), assigned the following ratings:

- Strategy and Governance: **A**
- Listed Equity - Incorporation: **B**
- Listed Equity - Active Ownership: **D**

Although the Fund does not have any mandated environmental, social and governance (ESG) exclusions, Pengana incorporates ESG considerations throughout the investment process. Where appropriate, Pengana will raise ESG concerns with companies and encourage sound ESG practices. Zenith believes that this qualitative analysis of a company's operations is crucial on a forward looking basis, given that a company's performance with regards to ESG considerations is increasingly being reflected in the company's share price. Overall, Zenith is comfortable with Pengana's approach to ESG.

From a classification scale of:

- Impact
- Thematic
- Integrated
- Aware
- Traditional

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

INVESTMENT FEES

The sector average management cost (in the table below) is based on the average management cost of all flagship Australian Shares – Absolute Return funds surveyed by Zenith.

The Fund charges a management cost of 1.101% p.a. and a 10.25% performance fee, subject to:

- Recoupment of prior negative performance
- Return must exceed the cumulative RBA cash rate plus 6% p.a.
- Performance fee cannot reduce the net return below the RBA Cash Rate

The performance fee is accrued daily and is paid semi-annually.

Zenith notes that effective 1 July 2019, the performance fee hurdle rate changed to the RBA cash rate plus 6% p.a. (after fees), rather than solely the RBA cash rate. In addition, the performance fee payment period changed from quarterly to six monthly. Zenith views the Fund's change in fee structure positively, as we believe the hurdle rate is now more reflective of the Fund's risk profile. However, given that the Fund's risk exposures are primarily driven by Australian equities, we would prefer that the Fund's performance fee is linked to an Australian equity benchmark, which we believe would provide stronger alignment.

Overall, Zenith believes the Fund's fee structure is expensive, relative to peers, given its stated objectives. In addition, we believe that investors have not been sufficiently compensated by way of risk-adjusted performance given the fees paid over the past three years (ending 30 June 2020).

There is also a 0.20% buy/sell spread applicable on applications and redemptions.

(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.)

Fees Type	Fund	Sector Average (Wholesale Funds)
Management Cost	1.10% p.a.	0.89% p.a.
	Description	
Performance Fee	10.25% on outperformance of the RBA Cash Rate plus a 6% p.a. hurdle (after fees).	
	Buy Spread	Sell Spread
Buy / Sell Spread	0.20%	0.20%

PERFORMANCE ANALYSIS

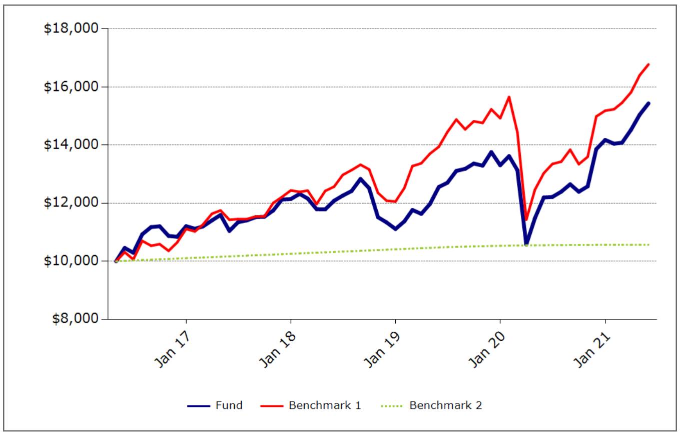
Report data: 31 May 2021, product inception: Jul 2008

Monthly Performance History (%, net of fees)

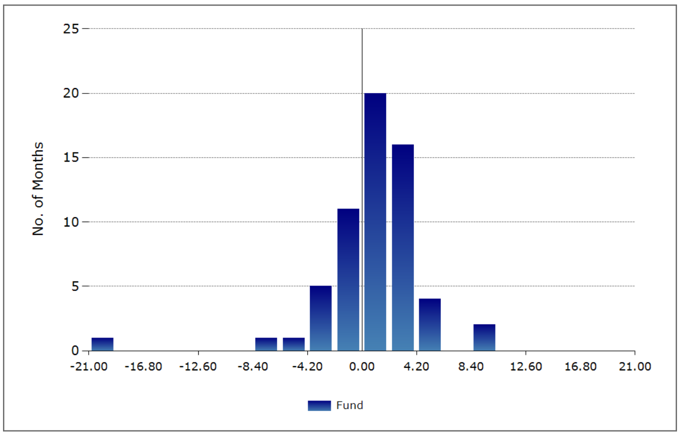
	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	FUND YTD	BM1 YTD	BM2 YTD
2021	-0.92	0.27	3.13	3.57	2.61								8.87	10.51	0.04
2020	2.36	-3.55	-19.47	8.54	6.23	0.15	1.49	2.05	-2.03	1.50	10.18	2.29	6.55	1.74	0.31
2019	2.37	3.45	-1.13	2.90	4.90	1.17	3.20	0.55	1.37	-0.53	3.51	-3.30	19.75	23.78	1.17
2018	1.46	-1.30	-3.02	-0.05	2.52	1.46	1.29	3.35	-2.48	-7.99	-1.55	-2.00	-8.50	-3.07	1.50
2017	-0.78	0.71	1.83	1.66	-4.74	2.70	0.56	0.98	0.12	1.89	3.20	0.14	8.35	11.95	1.50

Benchmark 1: S&P/ASX 300 (Accum), Benchmark 2: RBA Cash Rate

Growth of $10,000



Monthly Histogram



Minimum and Maximum Returns (% p.a.)

ABSOLUTE PERFORMANCE ANALYSIS

Return	Incpt.	5 yr	3 yr	1 yr
Fund (% p.a.)	10.18	8.09	8.50	26.55
Benchmark 1 (% p.a.)	6.94	10.22	10.11	28.74
Benchmark 2 (% p.a.)	2.52	1.08	0.80	0.16
Median (% p.a.)	10.18	7.00	6.67	21.67
Ranking within Sector	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Fund Ranking	1 / 1	2 / 4	2 / 4	2 / 4
Quartile	1st	2nd	2nd	2nd
Standard Deviation	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Fund (% p.a.)	11.41	13.75	16.51	10.14
Benchmark 1 (% p.a.)	14.54	14.55	17.49	10.42
Median (% p.a.)	10.88	11.65	13.93	9.73
Downside Deviation	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Fund (% p.a.)	7.83	10.30	12.72	2.23
Benchmark 1 (% p.a.)	10.47	10.92	13.67	3.59
Median (% p.a.)	6.90	8.01	9.97	3.04
Risk/Return	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Sharpe Ratio - Fund	0.65	0.49	0.45	2.61
Sortino Ratio - Fund	0.94	0.66	0.59	11.88

For consistency purposes, Zenith benchmarks the Fund against theS&P/ASX 300 Accumulation Index. Accordingly, all performance and risk measurements are calculated with the Zenith assigned index.

All commentary is as at 31 May 2021.

The Fund aims to achieve a total return in excess of the risk-free rate, plus a margin to compensate investors for the additional risk associated with investing in Australian equities. Pengana expects to achieve this objective with a volatility of returns that is less than the Australian equity market.

Zenith would prefer to see the delineation of a specific outperformance target, as opposed to a descriptive, qualitative objective. Zenith believes this would provide investors with greater transparency with regards to returns expectations and to the level of risk embedded in the Fund.

The Fund has achieved its investment objectives since inception.

The Fund's risk, as measured by Standard Deviation, has been materially below the benchmark since inception.

RELATIVE PERFORMANCE ANALYSIS

Alpha Statistics	Incpt.	5 yr	3 yr	1 yr
Excess Return (% p.a.)	3.24	-2.13	-1.61	-2.19
% Monthly Excess (All Mkts)	49.03	43.33	41.67	41.67
% Monthly Excess (Up Mkts)	31.31	39.53	38.46	36.36
% Monthly Excess (Down Mkts)	80.36	52.94	50.00	100.00
Beta Statistics	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Beta	0.70	0.87	0.89	0.91
R-Squared	0.79	0.84	0.89	0.87
Tracking Error (% p.a.)	6.89	5.83	5.67	3.75
Correlation	0.89	0.92	0.95	0.93
Risk/Return	**Incpt.**	**5 yr**	**3 yr**	**1 yr**
Information Ratio	0.47	-0.36	-0.28	-0.58

All commentary is as at 31 May 2021.

Zenith seeks to identify funds that can outperform in over 50% of months in all market conditions, as we believe this represents consistency of manager skill. The Fund is marginally below this objective since inception.

Zenith notes that the Fund has shown a greater level of outperformance consistency in falling markets, which is consistent with the Fund's capital preservation focus and relatively high levels of cash.

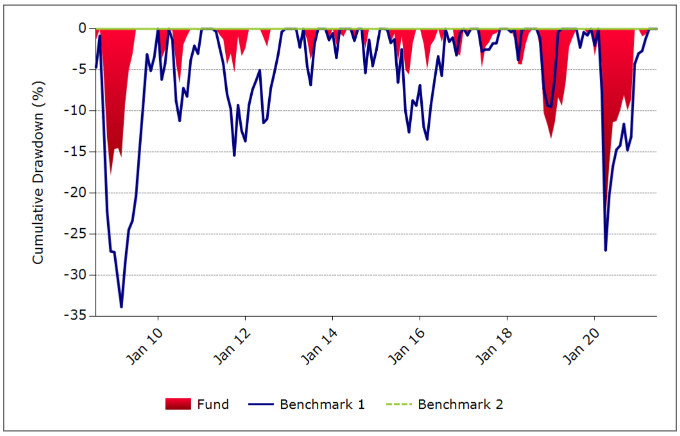
On a relative risk adjusted basis, the Information Ratio has been positive since inception, and as such, the Fund has generally rewarded investors for the active risk inherent in the Fund's strategy. This suggests that the active risk taken by Pengana has been sufficiently compensated.

DRAWDOWN ANALYSIS

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.

Drawdown Analysis	Fund	BM1	BM2
Max Drawdown (%)	-23.12	-33.89	
Months in Max Drawdown	4	8	
Months to Recover	8	10	

Worst Drawdowns	Fund	Benchmark 1	Benchmark 2
1	-23.12	-33.89	
2	-17.88	-26.97	
3	-13.43	-15.41	
4	-6.64	-13.46	
5	-5.57	-11.20	



All commentary is as at 31 May 2021.

The Fund's drawdowns have generally been significantly lower than the benchmark. Zenith believes this is consistent with Pengana's capital preservation focus.

INCOME/GROWTH ANALYSIS

Income / Growth Returns	Income	Growth	Total
FY to 30 Jun 2020	7.49%	-11.35%	-3.86%
FY to 30 Jun 2019	7.78%	-4.22%	3.56%
FY to 30 Jun 2018	4.30%	3.77%	8.07%
FY to 30 Jun 2017	4.80%	5.38%	10.19%
FY to 30 Jun 2016	3.06%	4.65%	7.71%
FY to 30 Jun 2015	1.56%	7.33%	8.89%
FY to 30 Jun 2014	8.19%	0.94%	9.13%
FY to 30 Jun 2013	5.90%	18.06%	23.96%
FY to 30 Jun 2012	3.48%	4.79%	8.27%

Pengana aims to distribute Fund income on a semi-annual basis (June and December).

The Fund's portfolio turnover is expected to range between 20% p.a. to 30% p.a., which Zenith considers to be low. Pengana has indicated that approximately 50% of the expected turnover is attributed to resizing existing positions and approximately 50% is due to complete sales and new additions. Given this expected level of turnover, the majority of the Fund's returns 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 highly 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.

REPORT CERTIFICATION

Date of issue: 24 Jun 2021

Role	Analyst	Title
Author	Jock Allen	Investment Analyst
Sector Lead	Jacob Smart	Senior Investment Analyst
Authoriser	Bronwen Moncrieff	Head of Research

RATING HISTORY

As At	Rating*
24 Jun 2021	Recommended
18 Jun 2020	Recommended
20 Jun 2019	Recommended
21 Jun 2018	Recommended
29 Jun 2017	Recommended
30 Jun 2016	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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This report refers to the Australian unit trust for the fund, and the fund and benchmark returns are all in AUD.

Zenith has charged Pengana Capital Group a fee to produce this report.