



Pengana Capital Group (PCG)

15 September 2021

Initiating Coverage - Outperform

Recommendation: Outperform

Our View

PCG is a retail investment manager generating above industry margins by offering unique products designed to diversify a portfolio. PCG currently manages \$4.0bn with a cost base built to manage significantly more. Operating leverage from this cost base is in the early stages of becoming evident as highlighted by 27% FUM growth and 95% EBITDA growth in FY21. We see considerable opportunity for PCG to grow FUM and to generate earnings growth for the following reasons:

1. PCG is under-penetrated in the market where we estimate only 20% of advisers have been engaged with. The distribution team is changing this.
2. Funds with performance fees (77% FUM) are all near to/at high watermarks.
3. 34% of FUM is exposed to absolute performance hurdles which provide a higher level of certainty - including PE1 where PCG receives 100% of fees.
4. Utilising external managers raises the profile of a fund, provides an instant track record and generates better economics for PCG than internal teams.
5. Existing funds have >\$30bn capacity with many offering exposure to high-demand themes including ethical, ESG and impact investing.
6. Two international funds have just had upgraded ratings from Lonsec and will soon be included on more investment platforms.

We do not think the market appreciates the operating leverage inherent in this model and the extent to which earnings can grow in the near-term. We forecast FY22 operating EBITDA growth of 51% which is driven by management fee growth of 13% (flowing on from a rapid increase in FUM late in FY21) and performance fee growth of 12%. Trading on 8.6x our FY22E EPS we think PCG is undervalued and believe a 14x multiple is current fair value given the growth profile. This implies a \$3.12 share price. See pg. 10 for our valuation breakdown.

Key Points

Diversified, high-margin funds outperform peers on fees

PCG's funds are diverse in strategy, geography and size with the unique nature of the products enabling above-market fees to be generated. PCG funds accept Australian retail capital where typical management fees range 0.7-1.0%. Differentiated funds are in higher demand and retail investors are therefore willing to pay higher fees. With fund themes including ethical, impact, global, ESG, small caps, & private equity, PCG has generated an average management fee of 1.15% the last five years. Each fund is managed by a separate internal investment team or by an external manager in a JV with PCG. This model allows investors to obtain exposure to some of the world's top investment managers with their scale allowing for greater total FUM to be managed. Management fees are split between PCG and the investment teams with JV's providing better economics for PCG by 20-25bps. With a sharper return and the greatest capacity for FUM growth, we believe the JV funds will drive higher average management fees in the medium term.

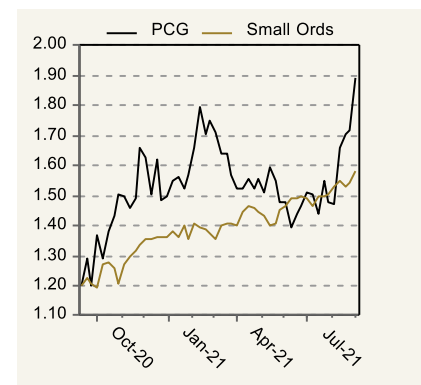
Performance fee growth the major driver of short-term earnings growth

PCG's diversified group of funds allow for largely uncorrelated performance fee returns and therefore we expect reasonable consistency in these returns over the medium-term. This is further supported by 34% of group FUM being exposed to absolute hurdles rather than relative hurdles, implying there is likely a lower threshold to overcome. Short-term, we expect notable growth in performance returns with all performance fee exposed funds approaching, or at, high watermarks. We note PCG receives 100% of performance fees from listed funds, PIA & PE1, where we expect strong FUM growth. Long-term we expect these fees to track at 1.0% of FUM that is exposed to performance fees (currently \$3.1bn).

Summary (AUD)

Market Capitalisation	\$201m
Share price	\$1.93
52 week low	\$1.25
52 week high	\$2.05

Share price graph (AUD)



Key Financials (AUD)

	FY21A	FY22E	FY23E
Total Revenue	69.9	78.2	83.5
Operating EBITDA	19.2	29.1	32.1
EBITDA Margin	27.5%	37.2%	38.4%
NPAT Adj.	15.3	24.1	26.3
EPS Adj.	14.2	22.3	24.3
PE Ratio	13.6	8.6	7.9
EV/EBITDA	9.4	5.9	5.0
EV/EBIT	9.6	6.0	5.1
Dividend	13.0	17.0	19.0
Div yield	6.8%	8.8%	9.9%

See page 10 for our valuation breakdown

Pengana Capital Group - Financial Summary Price \$ 1.93

PROFIT & LOSS SUMMARY (A\$m)					BALANCE SHEET SUMMARY (A\$m)				
Period	FY20A	FY21A	FY22E	FY23E	Period	FY20A	FY21A	FY22E	FY23E
Management fee revenue	37.5	40.3	45.4	48.9	Cash	15.3	19.9	28.8	36.7
Performance fee revenue	6.2	28.0	31.2	33.0	Contract Assets	3.8	21.5	23.4	24.7
Total Revenue	45.1	69.9	78.2	83.5	Investments	6.9	7.2	7.3	7.3
Total Expenses	(36.4)	(56.2)	(55.1)	(57.4)	Equity Investment in Financial Assets	9.1	10.5	11.0	11.5
Reported EBITDA	10.1	16.8	23.7	26.7	Intangibles	66.7	61.0	60.6	60.2
Net Interest	(0.3)	(0.2)	0.2	0.4	Other Assets	4.3	4.3	4.7	4.8
PBT	9.8	16.7	23.9	27.1	TOTAL ASSETS	106.1	124.5	135.8	145.3
Tax	(0.4)	(4.8)	(6.2)	(7.2)	Trade and Other Payables	11.3	23.5	25.8	27.6
Reported NPAT	6.0	8.8	14.5	16.7	Deferred Tax	4.9	3.9	3.9	3.9
Reported EPS	5.5	8.1	13.4	15.5	Other Liabilities	5.5	9.0	8.2	6.9
Operating EBITDA	9.9	19.2	29.1	32.1	TOTAL LIABILITIES	21.6	36.4	37.9	38.4
<i>Adjustment for interest earned on LSP</i>	2.0	1.5	1.5	1.5	TOTAL EQUITY	84.5	88.1	97.9	106.9
Underlying NPAT	10.3	15.3	24.1	26.3					
Underlying EPS	9.5	14.2	22.3	24.3					

EARNINGS AND DIVIDENDS				
Period	FY20A	FY21A	FY22E	FY23E
Weighted Average Units on Issue	107.93	108.00	108.09	108.09
Underlying EPS (c)	9.53	14.17	22.29	24.34
PERatio (x)	20.20	13.58	8.64	7.91
Underlying Dividend Payout Ratio	83.9%	91.7%	76.3%	78.0%
Reported Dividend Payout Ratio	99.7%	91.7%		
Dividend (c)	8.00	13.00	17.00	19.00
Dividend Yield (%)	4.2%	6.8%	8.8%	9.9%

DEBT RATIOS				
Period	FY20A	FY21A	FY22E	FY23E
Debt Per Share (c)	0.1	0.0	0.0	0.0
EBIT Interest cover (x)	23.2	89.8	102.7	117.7
Underlying NPAT cover (x)	36.0	100.0	120.5	131.6

CASH FLOW SUMMARY (A\$m)				
Period	FY20A	FY21A	FY22E	FY23E
Net Cash - Operating Activities	6.72	10.38	24.55	27.72
Net Cash - Investing Activities	4.18	2.91	(0.05)	0.05
Finance Cost	(0.29)	(0.15)	(0.20)	(0.20)
Net Cash from Financing Activities	(9.71)	(8.73)	(15.59)	(19.93)
Net Cash Flow	1.19	4.56	8.91	7.85
Opening Cash Balance	14.45	15.31	19.90	28.81
Closing Cash Balance	15.31	19.90	28.81	36.65

VALUATION RATIOS & MARGINS				
Period	FY20A	FY21A	FY22E	FY23E
Operating EBITDA margin	21.9%	27.5%	37.2%	38.4%
EV/EBIT	20.9	9.6	6.0	5.1
EV/EBITDA	18.9	9.4	5.9	5.0
<i>All figures utilise underlying earnings</i>				

Our forecasts present PCG on an operating basis. That is, we calculate an Operating EBITDA figure then our NPAT is calculated by deducting depreciation, interest and tax. Similar to adjusted figures reported by the company, we do not deduct amortisation to calculate adjusted NPAT and EPS as the majority of amortisation relates to the gradual write-down of acquired relationships. Further, our per share figures all include the 24.3m Treasury shares used for the loan funded share plan. The loan funded shares gradually come out of escrow from mid-2022 and the loans are payable within two years from the escrow release date. As we are including the treasury shares in our per share figures, we also include the interest earned on the loan funded share plan (which utilises the treasury shares) in our operating NPAT and EPS forecasts. We think presenting the figures this way provides the clearest picture of PCG's current operating model.

We also note that our fee revenue is calculated based upon FUM assumptions. These FUM assumptions do not include the impact of investment performance nor the impact of distributions from the funds within the PCG portfolio to the respective investors. Investment performance and specific fund distributions may impact FUM positively or negatively.

Finally, we wish to point out that whilst the interest from the loan share plan is included in our forecasts, the loan balance (\$29.6m) is off balance sheet. When the loans are repaid, this cash will sit on the balance sheet and will be utilised to increase shareholder value. We speculate that this could be through a special dividend, a buyback or further investment into PCG's listed vehicles.

Pengana Capital Group

Pengana Capital Group (PCG) is a diversified funds management group with distinct investment strategies. PCG's aim is to deliver superior long-term risk adjusted returns to investors with a focus on capital preservation. PCG's funds accept capital from the Australian retail investor market with a focus on advisors, self-managed super funds (SMSF) and high net worth (HNW) investors.

Company History

Russel Pillemer and Malcolm Turnbull founded Pengana Capital in 2003 after working as colleagues at Goldman Sachs. In 2008 NAB's then direct investment management business, nabInvest purchased a 49.49% stake in Pengana.

In March 2017, Pengana's FUM had grown to ~\$2bn when NAB sold its significant minority stake (49.49%) to Washington H. Soul Pattinson (Soul Patts). Only a few days later Pengana agreed to a merger with Hunter Hall (HHL.ASX) via reverse takeover whereby Hunter Hall acquired all the shares in Pengana in exchange for Hunter Hall shares. Following the merger, the combined group was owned ~73% by existing Pengana shareholders and ~27% by existing Hunter Hall shareholders with FUM of \$3.1bn.

Hunter Hall was founded by Peter Hall in 1993 where he was Executive Chairman and CIO. Prior to the merger, in December 2016, Mr Hall resigned as CIO and concurrently sold a portion of his holding (equivalent to 20% of Hunter Hall) to Soul Patts at \$1/share despite the share price being in excess of \$3. Soul Patts indicated its intention to acquire the remaining 80% of Hunter Hall however the following three months saw a bidding war as Pinnacle Investment Management also attempted a takeover. Prior to the merger of Hunter Hall and Pengana, Pinnacle had the highest bid of \$2.40/share however the Hunter Hall Board had not recommended shareholders accept any of the offers claiming the business was worth between \$2.75-\$3.20/share.

Following the announcement of the Pengana/Hunter Hall merger (prior to shareholder approval), Soul Patts launched a revised cash bid for the remaining shares in Hunter Hall at \$2.60/share. This was in conjunction with Mr Hall's agreement to sell his remaining 24% stake in Hunter Hall at this price and resulted in Soul Patts holding ~45% of Hunter Hall as well as ~49% of Pengana. Following the merger, Soul Patts has remained Pengana's largest shareholder and currently holds 36.9% of PCG.

In the three years following the merger, FUM fluctuated between \$2.8-\$3.5bn with the bottom being seen in March 2020 following the Covid-19 induced market selloff. Importantly, through this time PCG refreshed its distribution team and hired several senior industry people. Along with the benefit of a strong market rebound, the distribution team has grown FUM from \$2.8bn to \$4.0bn in 15 months, despite paying out \$112m in distributions, net of reinvestments.

The Australian Retail Investment Market

History

Historically, retail investors have tended to invest in specialist funds via investment platforms. These platforms acted as an administration service for investments with the benefit of providing access to a range of investments that may not normally be available to retail investors whilst also removing the deluge of paperwork and management of multiple investments. At the same time, ratings agencies such as Zenith, Morningstar and Lonsec, are used as consultants to identify suitable investment products. These ratings then dictate to the platform providers which funds from an investment manager are included on approved product lists and therefore can be invested in via the platforms.

Most importantly, large groups of financial advisers operated somewhat in unison under the umbrella of a 'Dealer group'. The larger dealer groups would have principals who acted as gatekeepers and were pivotal in determining which funds/products their financial advisers could invest their clients in to.

Until The Future of Financial Advice (FoFA) legislation was brought in in 2013, investment managers were able to pay commissions to dealer groups and advisers. The clear conflict of interest was removed however grandfather clauses allowed for pre-existing trail commissions to remain in place. The Financial Services Royal Commission of 2018 determined these were still creating conflicts and many institutions have since said they have been/will be cancelled.

Problems between dealer groups and advisers began to arise as advisers wanted access to a wider range of products than those approved within their group. This has led to notable disintermediation of large dealer groups as advisers have obtained their own license or have moved to smaller, more independent dealer groups.

Now

Although large dealer groups still exist, the market has, and continues to, undergo significant change with disintermediation bringing investment managers closer to the end investor. The proliferation of independent, smaller adviser groups has forced investment managers to rethink their marketing methods. Many of PCG's competitors still focus on the large dealer groups with oversight on billions of dollars of capital. Numerous independent/smaller providers are therefore not receiving the same level of service and this presents a notable opportunity for PCG.

Business Overview & Analysis

PCG currently manages 12 funds, each with a distinct investment strategy. These products have active strategies with non-benchmark mandates which allows the investment teams to invest in their best ideas. Each fund is run by a separate investment team and six of the 12 funds have an external investment team in place. External teams are utilised to ensure investors are exposed to unique, diversified products and experts in the respective strategies.

With a growing focus on ESG issues globally, all Pengana retail funds apply an ESG framework to their investment process, while specific ethical/impact investing is available through four of PCG's funds. Three of these funds are negatively screened which means industries are excluded that cause harm to people, animals or the environment, while one is a positive impact fund, focused on the opportunities created by the transition to a low carbon and sustainable global economy. Importantly, the ESG frameworks utilised by PCG's strategies are subject to review by several independent organisations.

Revenue

PCG revenue growth comes from two sources:

1. Management fees

Management fees will grow/contract in line with FUM movements. FUM movements are driven by

- Performance of the funds (Increasing share prices/dividends of investments = greater value of the fund)
- Distributions paid to investors. Distributions detract from FUM however are subject to performance of individual funds.
- Vertical growth - Inflow/outflow of investors into the funds. This is largely driven by the distribution team's ability to attract investors to the products
- Horizontal growth - New Funds/Strategies created by PCG

2. Performance fees

Performance fees will fluctuate based on the fund(s) outperforming benchmarks or previous high watermarks.

We note performance fees as a percentage of FUM have ranged from 0.2% to 2.0% the last five years and whilst fluctuations are likely over short periods of time, PCG expects 1.0% to be a sustainable level.

In the "PCG Funds" section below, we break down these fees in greater detail.

Our View

A key benefit of PCG accepting Retail capital is it tends to be stickier than Wholesale capital – that being, withdrawals/outflows are far less frequent. Additionally, retail and HNW capital attracts higher margins as Wholesale capital providers are by nature, larger, and have greater leverage to drive down fees. Retail capital tends to attract 0.7-1.0% fees however PCG's average fees are currently ~1.15%. We believe investors are prepared to pay a premium for the unique products PCG offers including Private Equity, Ethical, Sustainable and International funds.

Aside from performance, we expect vertical growth to be the strongest driver of FUM as PCG's distribution team continue to make Australian financial advisers aware of the Pengana stable of products. Whilst strong financial performance of the funds will drive inflows, we expect adviser awareness of how Pengana's funds can diversify a clients portfolio will be a greater driver of FUM growth. We note there is >\$30bn of FUM headroom until PCG's existing funds/strategies reach their cap.

We estimate only 20% of Australian's financial planners have had a conversation with a Pengana employee. We see this as a key area of opportunity for PCG, particularly given competitors have a far greater penetration into the Australian financial planning network.

We also expect PCG to develop new funds/strategies, further driving management fee growth over time. We think this will be limited to one new strategy p.a.

PCG Funds

Below we outline the funds managed by PCG and the specifics of management and performance fees with respect to the portfolio of funds.

Code	Fund Name	Strategy	Investment Team	FUM (\$m)	TC est. FUM Cap (\$m)	Mgmt Fee	Performance Fee
	Pengana Australian Equities	Australian Multi Caps	Internal	987	1,100	1.0%	10.25%*
	Pengana Emerging Companies	Australian Small Caps	Internal	842	1,000	1.3%	20% above ASX Small Ords
	Lizard Global Small	Global Multi Caps	Internal	483	2,000	1.0%	a range of fee structures
	Pengana Axiom International Ethical	Global Multi Caps	JV	434	10,000+	1.3%	n/a
PIA.ASX	Pengana International Equities Ltd	Global Multi Caps	JV	379	10,000+	1.2%	15% above MSCI World
PE1.ASX	Pengana Private Equity	Global Private Equity	JV	333	10,000+	1.2%	19.5% above 8%
	Pengana Global Small Companies	Global Small Caps	Internal	179	500	1.3%	20% above MSCI AC World SMID
	Pengana Harding Loevner International	Global Multi Caps	JV	69	10,000+	1.0%	n/a
	Pengana WHEB Sustainable Impact	Global Impact Investing	JV	180	800	1.3%	n/a
	Pengana Israel Alpha	Global Market Neutral	JV	37	500	1.5%	20% above 4%
	Pengana High Conviction Equities	High Conviction	Internal	45	200	1.8%	15% above RBA Cash + 3% p.a.
	Pengana High Conviction Property	Australian Multi Caps	Internal	8	700	0.7%	14.6% above ASX300 A-REIT

*10.25% of increase in net asset value subject to the Australian cash rate plus 6% p.a and high water mark, paid half yearly

PCG's funds are deliberately style agnostic so that financial advisers can see they offer genuine diversification and make sense for client portfolio construction. PCG's investment managers utilise a bottom-up investing approach where the impact of macro events is designed to have limited impact on investment performance.

Management fee key points

- PCG pays 30-40bps of the management fee to the external investment team when a JV is in place. When an internal investment team is utilised, the management fee is generally split 50/50 – that is, after direct expenses are applied.
- In FY21, PCG received 56% of reported management fees with 44% to investment teams. The portion PCG receives will increase over time as FUM growth is likely to occur in funds where a JV is in place.
- We estimate average management fees will remain between 1.1-1.2%.

Performance fee key points

- Generally, performance fees are split 50/50 with external investment teams. However, PCG receives 100% of performance fees from its listed vehicles, PIA and PE1. Performance fees are also split 50/50 with internal investment teams.
- 9/12 funds are subject to performance fees – this equates to 77% of FUM or \$3.1bn as of the end of FY21.
- Of the 9, three of the funds (\$1.36bn) are subject to absolute return hurdles. This is important as these performance fees are quite stable as the funds do not have to outperform a benchmark to achieve a return.
- Performance fees are spread across largely uncorrelated strategies, providing a degree of stability to income.
- In FY21, PCG received 55% of reported performance fees with 45% to investment teams - both internal and external.
- We expect performance fees attributable to PCG to grow due to:
 - an increasing proportion of funds utilising external investment teams and the favourable structures in place with these teams.
 - As PCG has grown, bargaining power has improved and therefore economics of strategies are more favourable. Bargaining power is also improved when developing strategies without FUM caps as both sides can generate greater gross fees as FUM increases.
 - PE1 tracking above its absolute hurdle and PCG receiving 100% of the fees for this product.
- We estimate average performance fees will remain around 1.0% of FUM.

Further key points

- Although internal investment teams share the economics of both management and performance fees 50/50, PCG allocates costs to these teams before the split is determined, essentially making this a profit share arrangement.

- Pengana Harding Loevner International Fund and Pengana International Equities (PIA.ASX) have both just received “Recommended” ratings from Lonsec. This was in addition to recent “Recommendation” ratings from Zenith. This is an improvement in rating for both funds and is notable having only brought Harding Loevner on board in May 2021. This will increase the number of platforms these funds are included in.
- Any new strategies will have large FUM capacity – management are highly focused on not capping growth potential.
- PCG owns 66.7% of Lizard Investors which was purchased in January 2020 for \$2.7m. This ownership deems the investment team to be internal. Additionally, Lizard Global Smalls comprises three different strategies with only one strategy being exposed to performance fees. This portion equates to \$256m at the time of writing.

Platforms

PCG funds are approved and included on approximately half of Australia’s retail investment platforms. This will increase following the upgrade in Lonsec ratings on the international funds as mentioned above. Coverage across all platforms is unrealistic however there is room for greater penetration of PCG funds and therefore a wider clientele base to target.

Our View

Whilst JV’s with external investment teams offer PCG more attractive economics on management and performance fees, we believe they are also more attractive to financial advisers, particularly across the international funds. External managers with a long history of outperformance, boots on the ground in the respective markets and larger teams are, in our opinion, likely to deliver greater returns than teams based in Australia. We think this opinion is supported by the upgraded rating from Lonsec on PIA.ASX and the Harding Loevner International Fund. The rating improvement is also likely to open more opportunities for FUM growth as these funds will be added to larger platforms.

We understand over the last few years PCG has focused on adapting the funds to better suit the demands of the market with the focus being on how they add value to an adviser and a client portfolio. This has helped build awareness of the group but importantly has provided advisers with a compelling reason to add PCG product to a clients portfolio. Poor performance is inevitable at some point (contracting markets) but importantly, we think the communication to advisers regarding value add and diversification will help limit outflows in such a situation. We think PCG now have an attractive, leverageable structure in place to generate significant FUM growth over a prolonged period.

Expenses

Expenses as per Accounts	% of FY21A Expenses	% of FY22E Expenses
Human resources expense	34.2%	35.5%
Fund manager profit share	44.4%	48.2%
Fund operating expenses	6.8%	6.8%
Occupancy expenses	0.8%	0.9%
Technology and Communications	3.0%	2.8%
Marketing and investment research	1.0%	0.9%
Insurance	2.0%	1.8%
Professional, registry and listing related expenses	1.5%	1.3%
Other operating expenses	5.3%	1.1%
Product development	0.9%	0.7%

As can be seen above, PCG is a people business with ~80% of costs related to salaries or profit share.

Having set up an infrastructure in preparation for growth, management believe the fixed cost base is now at a level where it can cater for significantly more FUM without fixed cost increases. Operating expenses of \$21.7m were artificially high in FY21 due to a spike in short-term incentives (STI’s) as management paid employees extra as a catch up for lean periods in the prior years. We expect operating expense levels of \$19.5m in FY22. We expect profit share to grow as a percentage of expenses as FUM grows whilst the remaining expenses should slowly decrease as a percentage given the operating leverage inherent in the business model.

Our View

We expect to see EBITDA margin growth as expenses remain steady. Although we expect profit share growth, this will be more than offset by PCG’s share of performance fee revenue.

Distribution Team

PCG's distribution team consists of eight distribution managers who are located across Australia and are 'on the road' promoting PCG. Two further business development associates, an investment specialist and third party distribution in NZ, offer additional support.

Following the merger of Pengana and Hunter Hall, the capability of the distribution team has been a focus for PCG management with the knowledge that the team is the major driver of FUM growth. The average tenure of the team is 2.5 years and although strong markets have assisted, FUM growth from \$2.8bn to \$4.0bn in the last 18 months can largely be attributed to this team.

To highlight the capacity for growth and the operating leverage on the existing cost base, the distribution team currently spends ~30% of time servicing current clientele. This implies ~70% of their time is engaging with and educating prospective clients or searching for other potential advisers to target.

Remuneration is salaried plus a combination of achieving targets based on the below:

- FUM net inflows
- FUM gross inflow
- Qualitative factors – meetings, corporate citizens etc

At any one point in time, the team are always pushing all funds in the PCG portfolio however there may be a more strategic and sustained focus on one fund at a point in time to try grow FUM. This focus would be in line with normal sales strategies such as taking advantage of themes in the market. Examples include targeting growth in a fund which is well positioned for inflation; or guiding advisers to a fund where markets are likely to bounce post vaccine-rollouts. In these instances, softer fund-specific targets may exist for the team and may also be linked to remuneration.

Our View

Whilst performance of the funds is important to maintain and attract FUM, we believe distribution is of far greater importance. This is highlighted by the recent FUM growth and we expect FUM momentum to step-up further as the team continue to increase awareness of PCG products. The opportunity for growth is large as we estimate 80% of financial advisers in Australia have not spoken with a Pengana distributor. Conversely, we estimate industry behemoths such as Pinnacle have touched ~80% of financial advisers and with retail FUM of \$20bn, present a case study as to the possible pathway for PCG.

As alluded to further above, the disintermediation of large dealer groups presents an opportunity for PCG. With several unique funds and a greater number of independent/smaller financial adviser groups not limited in their investment universe, the distribution team see a long pipeline of opportunity to grow FUM for a prolonged period. We understand the current sweet-spot to be adviser groups overseeing \$150-\$300m.

Distribution policy

Whilst not explicit, PCG's policy is to pay out the majority of underlying earnings. We note for consistency and to manage investor expectations, an element of smoothing may occur moving forward to avoid lumpiness in the dividends. This may involve lower than expected/lower than previous period payout ratios.

Growth Strategy

As alluded to further above, PCG's growth strategy is to grow management and performance fees. This will be done by:

1. Increasing FUM via Horizontal growth – via the distribution team.
2. Increasing FUM by Vertical growth – creating new funds/strategies to bring to market.
3. Deliberately diversifying FUM towards higher margin products.
4. Utilising external investment teams where PCG achieves better economics.

The past few years have seen a significant investment in sales and marketing capability and diversification of funds/strategies. When coupled with new relationships with global external investment managers and the continued shift of investable capital towards ESG, ethical screening and impact investing we see a robust pathway for PCG to continue strong management and performance fee growth.

Upcoming Event – Issue of PCG Shares

Pengana Investment Management Ltd is the Responsible Entity for Pengana Private Equity Trust (PE1.ASX). PCG is the Manager of PE1, and the Parent Company of Pengana Investment Management.

On PE1's listing, PCG issued 4,909,228 convertible preference shares ("Alignment Shares") to PE1. In connection with PE1's IPO, Pengana Investment Management signalled its intent to distribute the Alignment Shares to PE1 unitholders approximately two years after PE1's listing. On 31 August 2021 it was announced to distribute these shares. On distribution, the Alignment Shares convert into ordinary shares in PCG.

Once converted, PE1 holders are being provided the option to receive cash for their PCG share allocation. Coupled with some holders expected to end up holding unmarketable parcels, a sale process has been set up to sell the allotted PCG shares. Taylor Collison has been engaged to facilitate the orderly sale of PCG Shares that constitute small parcels and for PCG Shares received by eligible unitholders who elect for their PCG Shares to be sold.

The shares are already issued and are owned by PE1. We outline some of the key dates below.

Announcement of Distribution	31 August 2021
Record date for Distribution	7 September 2021
Sale Election Period opens for Eligible Unitholders	9 September 2021
Sale Election Period closes for Eligible Unitholders	23 September 2021
In-specie distribution date	30 September 2021
Alignment Shares convert to PCG Ordinary Shares (Conversion Date)	30 September 2021
Sale Period open date	5 October 2021
Converted PCG shares commence trading on ASX	6 October 2021
Sale Election Period Close Date	20 October 2021

Peer Group Analysis

Below we outline a selection of PCG's peers listed in the Australian market.

Company	Code	Mkt Cap	FUM %			Portfolio Exposure		FY21 Actual			FY22 Consensus Estimate		FY23 Consensus Estimate	
			FUM	Retail	Whole-sale	Inter-national	Ethical	EBITDA	EBITDA margin	PE (x)	EBITDA margin	PE (x)	EBITDA margin	PE (x)
Pinnacle Investment Mgmt	PNI	\$3.2bn	\$86bn	23.7%	76.3%	Yes	Yes	67.0	n/a*		n/a*	40.3	n/a*	33.8
Magellan Financial Group	MFG	\$8.0bn	\$118bn	27.0%	73.0%	Yes	Yes	612.0	85.0%	19.2	82.0%	16.9	83.0%	15.4
Platinum Asset Mgmt	PTM	\$2.3bn	\$24bn	71.0%	29.0%	Yes	Yes	200.0	74.0%	16	75.0%	16	75.0%	16
Australian Ethical Investment	AEF	\$1.2bn	\$6.1bn	70.0%	30.0%	Yes	Yes	17.3	30.0%	105				
Microequities Asset Mgmt	MAM	\$120m	\$497m	100%	0.0%	No	No	19.4	85.0%	9.1				
VGI Partners**	VGI	\$442m	\$3.2bn	100%	0.0%	Yes	No	44.6	70.0%	14.2				
Contango Asset Mgmt	CGA	\$45m	\$1.14bn	100%	0.0%	Yes	No	n/a	n/a	n/a				
Clime Investment Mgmt	CIW	\$44m	\$5.1bn	100%	0.0%	No	Yes	3.2	20.0%	22.5				
Pengana Capital Group	PCG	\$200m	\$4.2bn	100%	0.0%	Yes	Yes	19.2	27.5%	13.6	37.2%	8.6	38.4%	7.9

NB:

*PNI uses affiliates so total revenue is not disclosed and a true margin can not be calculated

**VGI actual figures are FY20 as it has a Dec year end

PCG forward estimates are TC estimates

Retail FUM is a broad definition and may include HNWI, family offices, charitable foundations

Our research has made clear that Australian listed investment managers are a bespoke group of companies with wide-ranging mandates, strategies and reporting metrics. There is no obvious peer for PCG however we note the following key points:

- **High earnings growth managers are rewarded with high PE multiples.** This is highlighted by PNI growing EBITDA >20% and trading on ~40x vs. MFG growing at <5% and trading on ~17x, despite MFG operating at a higher margin and managing more FUM.
- **Ethical themes trade at a premium.** A sharp increase in demand for ethical investing in recent times has helped valuations and FUM inflows. AEF is the standout in this regard trading on ~100x earnings however, all the remaining managers with ethical offerings still trade at a premium to those without an offering.
- **High operating margins don't necessarily lead to higher valuations.** CIW generates a 20% margin and trades on ~20x forward vs. VGI with a 70% margin trading on ~12x.

A distinction to make clear is that PCG has set up a cost-base and structure to grow FUM to levels comparable to larger peers such as PNI and PTM. For this reason, PCG's margin is lower than most peers, however, as highlighted above, this is not a prerequisite for premium valuation. Additionally, PCG is only now beginning to realise notable operating leverage from its cost structure and is well positioned for margins to expand. We note that more profitable peers with similar FUM (such as VGI) are not set up to bring in new capital and therefore are reliant on investment performance to achieve meaningful FUM growth. This limits the ability to generate EPS and dividend growth and therefore share price appreciation for investors.

With our FY22E and FY23E operating EBITDA growth forecasts of 51% and 10% respectively, we believe PCG fits in the high earnings growth category similar to PNI. PCG also ticks the box of offering meaningful ethical exposure with five of its 12 funds utilising a form of impact, ethical or ESG investing. We note our FY23 forecasts will prove to be light should positive investment performance occur in FY22.

Acknowledging PCG are smaller in terms of FUM, when we put these factors together, we see a strong case for PCG to trade at multiples in line with or closer to higher growth peers such as PNI.

Valuation

We believe our FY22E and FY23E EBITDA growth forecasts 51% and 10% respectively, represent a high growth investment manager. When coupled with the defensive nature of earnings, we believe PCG is befitting of a market multiple and with the ASX Small Ords forward earnings multiple of 18.1x, we see scope for revaluation as PCG continues to grow FUM and earnings.

Below we provide implied share prices based on varying levels of earnings and multiples. The PE multiple matrix is most relevant given our peer comparisons on the prior page.

Although peer comparisons are difficult, we highlight EV/EBITDA multiples and varying levels of EBITDA for clarity's sake as this emphasises the operating business without adjustments. Additionally, investors can make EV/EBITDA multiple comparisons to other companies growing at double digits with defensive earnings.

For each multiple and EBITDA combination we use our FY22E cash and debt levels. The current share price, our current underlying EBITDA forecast and the implied multiple are in bold.

		FY22 PE Multiple (x)							
		6	7	8.6	10	12	14	16	18
FY22E underlying EPS (\$m)	17	\$1.02	\$1.19	\$1.47	\$1.70	\$2.04	\$2.38	\$2.72	\$3.06
	18	\$1.08	\$1.26	\$1.55	\$1.80	\$2.16	\$2.52	\$2.88	\$3.24
	19	\$1.14	\$1.33	\$1.64	\$1.90	\$2.28	\$2.66	\$3.04	\$3.42
	20	\$1.20	\$1.40	\$1.73	\$2.00	\$2.40	\$2.80	\$3.20	\$3.60
	21	\$1.26	\$1.47	\$1.81	\$2.10	\$2.52	\$2.94	\$3.36	\$3.78
	22.3	\$1.34	\$1.56	\$1.93	\$2.23	\$2.67	\$3.12	\$3.57	\$4.01
	23	\$1.38	\$1.61	\$1.99	\$2.30	\$2.76	\$3.22	\$3.68	\$4.14
	24	\$1.44	\$1.68	\$2.07	\$2.40	\$2.88	\$3.36	\$3.84	\$4.32
	25	\$1.50	\$1.75	\$2.16	\$2.50	\$3.00	\$3.50	\$4.00	\$4.50
	26	\$1.56	\$1.82	\$2.25	\$2.60	\$3.12	\$3.64	\$4.16	\$4.68
	27	\$1.62	\$1.89	\$2.33	\$2.70	\$3.24	\$3.78	\$4.32	\$4.86
	28	\$1.68	\$1.96	\$2.42	\$2.80	\$3.36	\$3.92	\$4.48	\$5.04

		FY22 EV/EBITDA Multiple (x)							
		4	5	5.9	7	8	9	10	11
FY22E underlying EBITDA (\$m)	24	\$1.20	\$1.43	\$1.63	\$1.90	\$2.13	\$2.36	\$2.59	\$2.83
	25	\$1.24	\$1.48	\$1.69	\$1.96	\$2.21	\$2.45	\$2.69	\$2.93
	26	\$1.27	\$1.53	\$1.75	\$2.03	\$2.28	\$2.53	\$2.79	\$3.04
	27	\$1.31	\$1.58	\$1.80	\$2.10	\$2.36	\$2.62	\$2.88	\$3.15
	28	\$1.35	\$1.62	\$1.86	\$2.17	\$2.44	\$2.71	\$2.98	\$3.25
	29.1	\$1.40	\$1.68	\$1.93	\$2.24	\$2.52	\$2.81	\$3.09	\$3.37
	30	\$1.43	\$1.72	\$1.98	\$2.30	\$2.59	\$2.88	\$3.17	\$3.47
	31	\$1.47	\$1.77	\$2.03	\$2.37	\$2.67	\$2.97	\$3.27	\$3.57
	32	\$1.51	\$1.82	\$2.09	\$2.44	\$2.75	\$3.06	\$3.37	\$3.68
	33	\$1.55	\$1.87	\$2.15	\$2.51	\$2.83	\$3.15	\$3.47	\$3.79
	34	\$1.59	\$1.91	\$2.20	\$2.57	\$2.90	\$3.23	\$3.56	\$3.89
	35	\$1.62	\$1.96	\$2.26	\$2.64	\$2.98	\$3.32	\$3.66	\$4.00

PCG currently trades on 8.6x our FY22E EPS forecast. This represents a 52% discount to the current ASX Small Ords multiple of 18.1x. We expect PCG to re-rate higher as FUM growth is exhibited throughout FY22.

We believe a fair value multiple for PCG in FY22 is 14x, implying a share price of \$3.12. This implies a continued discount to peers and the market in the short-term to represent the fact that the major FUM and earnings growth is still ahead of the group.

As the market looks to FY23 in nine months' time, we note that based on our FY23E EPS forecast of 24.3cps the PCG implied share price is \$2.50 even if it only re-rates 20% from current levels.

We re-iterate that our forecasts do not account for investment performance and therefore positive investment performance provides upside to our FUM forecasts and subsequent earnings forecasts.

Financial Analysis and Forecasts

Our belief is PCG can reach FUM of \$5.5bn by the end of FY24 with this forecast forming the base of our assumptions. We think PCG can reach \$5.0bn via inflows alone over this period however the remainder will be required to come from performance and is net of distributions.

Notes to our forecasts

- As PCG has a loan funded share plan in place, there are escrowed Treasury Shares on issue for this purpose. Our per share figures all include the 24.3m Treasury shares used for the loan funded share plan. These gradually come out of escrow from mid-2022 and the loans are payable within two years from the escrow release date. We outline more on the loan share plan below our forecasts.
- Our forecasts present PCG on an operating basis. That is, we calculate an Operating EBITDA figure then our NPAT is calculated by deducting depreciation, interest and tax. Similar to adjusted figures reported by the company, we do not deduct amortisation to calculate adjusted NPAT and EPS as the majority of amortisation relates to the gradual write-down of acquired relationships.
- As we are including the treasury shares in our per share figures, we also include the interest earned on the loan funded share plan (which utilises the treasury shares) in our operating NPAT and EPS forecasts. We think presenting the figures this way provides the clearest picture of PCG's current operating model.
- We also note that our fee revenue is calculated based upon FUM assumptions. These FUM assumptions do not include the impact of investment performance nor the impact of distributions from the funds within the PCG portfolio to the respective investors. Investment performance and specific fund distributions may impact FUM positively or negatively.
- Finally, we wish to point out that whilst the interest from the loan share plan is included in the P&L, the loan balance (\$29.6m) is off balance sheet. When the loans are repaid, this cash will sit on the balance sheet and will be utilised to increase shareholder value. We speculate that this could be through a special dividend, a buyback or further investment into PCG's listed vehicles.

FY22 Forecasts

We estimate FY22 operating EBITDA of \$29.1m which is 51% growth on pcp. Our growth forecasts are underpinned by an increase in both management and performance fee revenue. FUM grew rapidly in 4Q21 and therefore the impact of higher management fees was not fully caught by the FY21 result. This will flow through in FY22 along with our estimate of an \$350m inflow of capital offset by \$50m of natural outflow churn. Inflows are driven by an anticipated step up in demand for the private equity (PE1.ASX), international and sustainable (WHEB sustainable impact) funds.

An increase in expected performance fee revenue is the greatest contributor to our EBITDA growth forecast as all major strategies with performance fees are at or close to high watermarks.

Given PCG has set the underlying cost infrastructure for significantly more FUM, we estimate fixed cost growth is limited which sees our EBITDA margin grow to 27.5% to 37.2%.

Although the distribution policy is to pay out the majority of underlying NPAT, we assume a payout ratio of 76% which equates to a distribution of 17cps. This is lower than pcp on the basis management will look to smooth the growth in distributions over time.

PCG have recently announced a share buyback to purchase up to 10% of the issued capital. This may impact our EPS figures and also our cash balance forecasts.

FY23 Forecasts

Our FY23 forecasts assume \$400m of inflows offset again by \$50m of natural outflow churn. Inflows are to be dominated by the international funds driven by ratings upgrades and an anticipated increase in awareness throughout FY22 as they are placed on new platforms. Once again we anticipate little growth in fixed costs and a similar rate of performance fees.

The flow on of these impacts is further EBITDA margin growth to 38.4% and a distribution of 19cps at a 78% payout ratio.

We believe our assumptions form what will be a continuous trend in the medium term for PCG.

Loan Funded Share Plan (LSP)

The group operates a loan share plan whereby limited recourse loans were provided to employees and fund managers to acquire shares in the company. The loans are interest bearing and have a maximum term of up to seven years. Recourse on the loans is limited to the associated shares and any dividend amounts applied to the loan balance. That is, dividends are used to pay down the loan balance as received.

The shares granted under the LSP are subject to a vesting condition, that the employees and fund managers must remain continuously employed for a period of three to five years from the grant date, except for shares associated with the LSP granted to the CEO which are not subject to a vesting period.

As the share purchases are funded by limited recourse loans, they are treated for accounting purposes as grants of share options and accounted for as equity-settled share-based payments. The shares issued under the LSP are fair valued on the date they are granted and amortised as an expense in profit or loss over the vesting period.

As at 30 June 2021, the CEO holds 15,872,528 shares with employees and fund managers holding a further 8,403,328. This equates to \$29.64m in loans.

The weighted average remaining contractual life of shares granted under this scheme is 2.9 years. At this time, treasury shares will convert to ordinary shares and the loans will be required to be paid. The individual will likely sell a portion to fund the repayment of the loan balance. The repayment of the loan will see an increase in the cash balances for PCG which would be utilised to increase shareholder value.

PCG likes the use of an LSP for long-term incentives and we believe would therefore look to continue to issue LTI under the LSP over time, but at a smaller scale.

Share Register

Top 20 Shareholders - as at 31/8/21	Shares	% Held
Washington H. Soul Pattinson & Co.	39,827,040	36.8%
Russel Pillemer	26,222,609	24.3%
Warwick Negus	3,585,184	3.3%
Jeremy Dunkel	1,896,483	1.8%
Roxanne Dunkel	1,803,150	1.7%
DJG Services Pty Ltd	1,657,095	1.5%
Radd Holdings	1,553,649	1.4%
HSBC Custody nominees	1,321,761	1.2%
DBR Corporation	1,255,260	1.2%
Rhett Kessler	1,299,590	1.2%
Damian and Julie Crowley	1,173,075	1.1%
Ed Prendergast	973,701	0.9%
National Nominees Ltd	903,106	0.8%
LMCTA Family	837,432	0.8%
David Groves	474,592	0.4%
Meg O'hanlon	672,335	0.6%
Steve Black	672,335	0.6%
Pretage Pty Ltd	630,051	0.6%
Frederick Wareham	520,000	0.5%
Total	87,278,448	81%
Total shares on issue	108,093,901	

Board of Directors

Warwick Negus Non-Executive Chairman

Warwick has more than 30 years' experience in the finance industry across Asia, Europe and Australia. His previous executive roles include CEO of Colonial First State Global Asset Management, co-founder and CEO of 452 Capital and Managing Director of Goldman Sachs in Australia, London and Singapore. He was also Vice President of Bankers Trust Australia. Warwick is also currently a director of Bank of Queensland, Washington H Soul Pattinson and Co and Dexus Group.

Russel Pillemer Managing Director & CEO

Russel co-founded Pengana in 2003 and has been CEO since its inception. Prior to founding Pengana, Russel worked in the investment banking division of Goldman Sachs in New York where he specialised in providing advice to funds management businesses. Before moving to New York, he was responsible for leading Goldman Sachs' Australian Financial Institutions Group. He was previously Chairman of Centric Wealth Group and is a member of Chartered Accountants Australia and New Zealand. Russel is also a director of Pengana International Equities (PIA.ASX).

Jeremy Dunkel Non-Executive Independent Director

Jeremy is a director of Taurus Capital, a family office investment consultancy specialising in philanthropy. His accounting and finance experience includes working for Chemical Bank, Chase Manhattan and Price Waterhouse. He is a director of Education Heritage Foundation and the Moriah College Foundation as well as being the Chair of Y2i.

Kevin Eley Non-Executive Independent Director

Kevin has over 30 years' experience in management in a broad range of industries including manufacturing, mining, retail, finance and funds management. He has worked for a major international accounting firm, two investment banks and was CEO of HGL limited. Kevin is currently a director of Milton Corporation, EQT Holdings and HGL Limited.

David Groves Non-Executive Independent Director

David has over 25 years' experience as a company director. He is formerly a director of EQT holdings, Tassal Group, GrainCorp Ltd and a former executive with Macquarie Bank and its antecedent, Hill Samuel Australia. David is a member of the Council of Wollongong University. He is a member of Chartered Accountants Australia and New Zealand and a fellow of the Australian Institute of Company Directors. David is also a non-executive director of Pengana International Equities (PIA.ASX), Redcape Hotel Management and Pipers Brook Vineyard.

Remuneration

We note that Directors are remunerated in the form of PCG shares as opposed to Directors' fees. The NED Equity Plan operates on a fee sacrifice basis, it does not involve additional cost to Pengana and enhances the alignment between the NED's and shareholders. The board recently has elected to continue receiving all of its remuneration in the form of shares. Russel Pillemer is not included in this structure.

Shares held by Board Members as at 30/6/21	# ordinary	# treasury shares held under the loan share plan
Warwick Negus	3,585,184	
Russel Pillemer	10,350,081	15,872,528
Jeremy Dunkel	1,896,483	
Kevin Eley	382,962	
David Groves	721,946	
Total	16,936,656	15,872,528
Total shares on issue/escrowed	83,818,045	24,275,856
% held by directors	20.2%	65.4%
Fully diluted shares held by directors		30.4%

Key Management Personnel

Paula Ferrao **Company Secretary**

Paula Ferrao is an Executive Director, having previously been interim Chief Executive Officer of Hunter Hall International Limited (HHL) and Chief Financial Officer of HHL since 2010. Paula has 19 years' experience in the funds management industry with strong expertise in financial reporting and tax for corporate entities, listed investment companies, managed investment schemes and public offer superannuation funds and in all aspects of fund operations. Paula was previously the Company Secretary of HHL, an Executive Director of Hunter Hall International (UK) Limited and of Rushcutter Investments Pty Limited, a Trustee of Hunter Hall Charitable Fund and a member of the Hunter Hall Charitable Committee. Paula holds a Bachelor of Business from the University of Technology, Sydney.

Katrina Glendinning **CFO**

Katrina is the Chief Financial Officer of Pengana and has held this role since the inception of the company in 2003. She is an Executive Director of Pengana Capital and Pengana Investment Management Limited and is a member of Pengana's Compliance and Risk Management Committees. Katrina is an experienced financial services executive with over 25 years' experience across a diverse range of products, investors and regulatory regimes. Prior to joining Pengana, Katrina was an Executive Vice President at BT Funds Management where she held a number of roles in the nine year period. Prior to that she worked for Price Waterhouse specialising in banking and financial services audit. Katrina has a Bachelor of Economics from the University of Sydney, is an Australian Chartered Accountant, a Fellow of FINSIA and a Graduate of the Australian Institute of Company Directors.

Adam Myers **Executive Director, Strategy and Distribution**

Adam Myers is an Executive Director and leads the distribution team at Pengana. Adam also has oversight of strategic initiatives and responsibility for the quantitative and structuring capability within the group. Adam developed an appreciation of market risk during a 15-year career trading equity derivatives, structuring derivative transactions and managing equity derivative traders. Prior to joining Pengana, he headed the Equity Derivatives business at Investec Bank in South Africa and the Corporate Equity Structuring function at Investec Bank in Australia. Adam holds a Bachelor of Commerce (Hons) from the University of Johannesburg.

Nick Griffiths **Chief Investment Officer**

As Chief Investment Officer, Nick is responsible for manager monitoring, performance analysis and risk management across Pengana's investment strategies. He also chairs the Risk Management Committee and is an Executive Director of Pengana Capital. Nick has more than 20 years' experience in the actuarial and investment industries in the UK and Australia. Prior to his current role, Nick was Head of Investment Research within Aon's Investment Consulting Practice in Sydney. Nick is a qualified Actuary and CFA Charterholder. He was educated in England and holds a Law and Economics degree from the University of Durham.

Keith McLachlan **Head of Operations**

Keith is the Head of Operations at Pengana. Keith has almost twenty years' experience in the financial services industry. Prior to joining Pengana in August 2015, Keith was a General Manager at Perpetual where he led operational and technology teams supporting the funds management and private clients businesses. Before that, Keith served in operational leadership roles in the Metropolitan Police Service in London. Keith has significant experience in operational management, project delivery, and leading organisational change. Keith has a Bachelors in Business Studies from the Bristol Business School and is Fellow of FINSIA

Dean Weinbren **Executive Director**

Dean Weinbren is an Executive Director, with oversight of Marketing, Media Partnerships and Brand initiatives across the Pengana Group. Prior to joining Pengana, Dean's previous experience includes the set-up and management of one of Australia's largest non-aligned risk insurance firms, as well as having founded and run both digital and experiential media agencies for major corporate sponsorships. Dean holds a BSocSci in Organisational Psychology and Industrial Sociology from the University of Cape Town, South Africa, as well as an Advanced Diploma in Financial Planning.

Daniel Fine **Head of Direct Clients**

Daniel Fine is the Head of Direct Clients, servicing all Pengana's direct client relationships. Prior to joining Pengana, Daniel was the founder and director of a general insurance business in South Africa, focusing on domestic and commercial business. Daniel holds a Bachelor of Commerce from the University of Witwatersrand in Johannesburg, South Africa.

Key Risks

Investment performance risk

The performance of the Company in providing its investment management services is dependent on its expertise and the outcomes of its investment decisions. The market may value the securities within the funds at prices materially different to the investment managers assessment from time to time, which may result in the poor performance of the funds.

Poor investment decisions and/or unfavourable market movements may also result in reduced or no performance fees and lower management fees, client redemptions of their investments, and may curtail any potential for new investment products.

Performance fee risk

Where PCG funds are exposed to performance fees, past good performance of Funds, and consequently the Company's ability to earn performance fees, are not necessarily a guide to future performance fee generation. The ability of the Company to earn performance fees is contingent on numerous factors, some of which cannot be controlled by the Company. A sustained period of poor performance may cause the value of the Funds to fall below its high-water mark. If this occurs, not only would the Company not generate performance fees during that period, but in future periods the fund would need to recoup past underperformance against the high-water mark before becoming entitled to a performance fee.

Reduced ability to retain and attract investors

A reduced ability, or inability, to attract new clients for existing funds or new strategies that it may seek to establish in the future, will reduce its ability to grow fee revenue, and/or offset redemptions.

Investment strategy risk

PCG employs a number of different investment strategies. There is a risk these strategies fall out of favour with the market and therefore investors redeem their capital.

Loss of key personnel

PCG relies on its ability to attract, train and retain high-quality employees and investment managers to generate future earnings and returns. Loss of these key personnel may affect the Company's ability to generate profits.

Changing market conditions

The Group's revenue is directly linked to its FUM which is driven by market performance and distribution. As such, the Company's performance is significantly linked to market performance and funds managed by the Company will be exposed to market risk. The market risk of assets in the Company's portfolio can fluctuate as a result of market conditions. The value of the Company's portfolio may be impacted by factors such as economic conditions, interest rates, regulations, sentiment and geopolitical events, as well as environmental, social and technological changes. Unfavourable global market movements, or a decline related to an asset class in which the Company manages assets, may reduce the Company's existing FUM, negatively impact net flows, result in reduced or no performance fees, client redemptions and curtail any potential for new investment products. This would likely have a material adverse effect on revenue and hence the financial performance of the Group.

New fund/product risk

The Company may establish new investment strategies or funds in the future, which may result in additional risks and uncertainties in the business. While the Company's new strategies are likely to include ones with clear adjacencies to PCG's existing area of expertise, such as ones which focus on a particular geographic region, the new strategies may extend to other areas. If the Company executes these new strategies poorly, the resulting underperformance may have a material adverse effect on the Group's financial performance or position.

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Taylor Collison are currently mandated to complete a sale process of unwanted or unmarketable parcels of PCG alignment shares issued to PE1 holders. This transaction is anticipated to be completed by the end of October 2021.

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Date Prepared: September 2021

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