

10 April 2024

Finger on the Pulse

NEED TO KNOW

- **Unique Private Credit Retail Offering to Launch Mid-2024.**
- **Playing to Strengths with Product Innovation.**
- **Performance fees may return in FY25.**

Pengana Private Credit (PPC) portfolio to deliver second product mid 2024: PCG will deliver four distinct investment offerings in its Private Credit business, which it now owns 100% of the economics for. With the wholesale fund launching in October 2023, the next product set to go live is a retail Listed Investment Trust (LIT) that is currently planned to IPO around the middle of 2024, subject to ASX final approval. Following this, term accounts and tailored accounts are set to follow, with fully digital and simplified onboarding and account management infrastructure.

Performance Fees in FY24/FY25: Three key funds drive performance fees for PCG, and despite strong outperformance over the last year, most funds remain below highwater marks. We expect the Emerging Companies Fund (one of PCG's key funds for performance fees) to be close to receiving performance fees over the next year, with the remainder appearing on track to get back in 12-24 months range.

Investment Thesis

Unique Private Credit business only needs one bucket to fire: We see value in the unique product set that Pengana has created, and we think that with a strong distribution channel, could mean significant sustained inflows.

Cracking the Funds Management Code: It is not immediately obvious, but PCG's product innovation with its Global Private Credit offering is likely to be transformational for the Group. PCG has created a globally scalable product by utilising its industry knowhow, relationships, but more importantly – understanding a competitive advantage PCG has, which includes retail distribution.

By doing so, PCG is able to deliver a multi-pronged product with attractive economics, with immediate impact. The likely success here may be a precursor for other product innovation in the Group, marking a new era for the firm (which we do not see as fully appreciated yet, but a big part of the investment opportunity in PCG).

Upside to performance fees: Performance fee revenue is now coming off a low base. With PCG expecting its group fee margin to move back to its long-term average, and funds expected to hit high-water marks over the next 12-24 months, we may see material revenue from performance fees over the medium-long term.

Valuation

We note there has been a transfer of coverage to PCG and as such our valuation is \$1.85 per share. We use a DCF to value PCG, using a risk-free rate of 3% and a WACC of 12.6%.

Risks

PCG has a range of risks applicable to it which we outline on page 10 of this report.

Report prepared by MST Access, a registered business name of MST Financial services ABN 617 475 180 AFSL 500 557. This report has been prepared and issued by the named analyst of MST Access in consideration of a fee payable by: Pengana Capital Group (PCG.AX)

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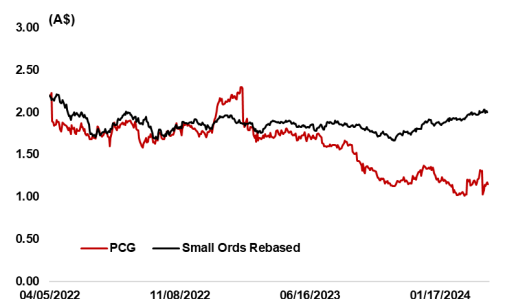
Pengana Capital Group is a fund manager who is a leading Australian provider of premium, value added products focused on the higher-end retail market (advisors and self managed superannuation funds) and high net worth individuals operating for over 20 years with around A\$3bn of funds under management. It has a unique funds management business model using both inhouse teams and joint ventures with offshore groups. It runs robust, scalable and technologically advanced "institutional grade infrastructure". www.pengana.com

Valuation	A\$1.85 (from A\$2.28)
Current price	A\$0.85
Market cap	A\$94.2m
Cash on hand	A\$10.7m

Upcoming Catalysts / Next News

Period	
- Mid-2024	- GPC Listed Investment Vehicle
- Mid-2024	- GPC Tailored/Term Accounts
- August 2024	- FY24 result

Share Price (A\$)



Source: FactSet, MST Access

Figure 1: Financial Summary

Penganena Capital							
Year end 30-June							
MARKET DATA				12-MONTH SHARE PRICE PERFORMANCE			
Price	A\$						0.85
Valuation	A\$						1.85
52 week low - high	A\$						0.85 - 1.47
Market capitalisation	A\$m						94.2
Enterprise value	A\$m						85.5
Shares on issue (diluted)	m						110.5
Options / rights	m						0.0
Other equity (treasury shares)	m						-26.7
Shares on issue (basic)	m						83.1

INVESTMENT FUNDAMENTALS		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
EPS - adj. basic	cps	25.2	5.1	4.2	6.1	9.1	12.2
EPS - reported diluted	cps	17.4	-0.4	-0.5	2.6	4.9	7.3
EPS - adj. diluted	cps	18.9	3.9	3.1	4.6	6.8	9.1
EPS growth	%	33%	-80%	-18%	46%	49%	34%
PE	x	4.5	22.0	27.0	18.5	12.4	9.3
DPS	cps	20	3	1	3	4	6
Franking	%	100%	100%	100%	100%	100%	100%
Dividend yield	%	24%	4%	1%	4%	5%	7%
Payout ratio (adj. NPAT)	%	106%	78%	32%	65%	59%	66%
Operating cash flow per share	cps	23.2	0.1	-0.2	4.1	7.3	9.3
Enterprise value	\$m	69.8	80.0	85.5	80.5	78.2	74.1
EV/Total Revenue	x	0.9	2.2	2.4	1.9	1.5	1.2
EV/EBITDA	x	2.2	21.6	27.2	12.7	7.7	5.3
NAV per share	A\$	1.05	0.93	0.90	0.93	0.95	1.00
Price / NAV	x	0.81	0.91	0.94	0.92	0.89	0.85
NTA per share	A\$	0.84	0.78	0.78	0.83	0.86	0.90
Price / NTA	x	1.02	1.09	1.09	1.02	0.99	0.94

PROFIT AND LOSS		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
Management fees	A\$m	41.8	36.0	35.1	37.8	40.7	45.1
Performance fees	A\$m	32.7	0.0	0.0	4.4	11.3	16.5
Total fee revenue	A\$m	74.5	36.0	35.1	42.2	52.0	61.6
Net fund direct expenses	A\$m	3.1	2.9	3.1	3.2	3.4	3.5
Operating expenses	A\$m	16.3	18.2	19.1	21.7	24.5	27.1
Team profit share	A\$m	23.2	11.1	9.8	10.9	14.0	16.9
Operating EBITDA	A\$m	31.8	3.7	3.1	6.3	10.2	14.1
Underlying profit before income tax	A\$m	29.2	6.0	5.0	7.3	10.8	14.4
Underlying profit after tax	A\$m	20.4	4.2	3.5	5.1	7.5	10.1
Reported NPAT	A\$m	18.9	-0.5	-0.6	2.9	5.4	8.1
Cash NPAT	A\$m	21.8	3.0	0.4	3.9	6.0	8.7
Weighted average diluted shares	m	108.4	109.4	110.3	110.5	110.5	110.5

BALANCE SHEET		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
Cash and cash equivalents	A\$m	25.7	14.2	8.7	13.7	16.0	20.1
Receivables	A\$m	1.0	1.4	1.8	2.2	2.7	3.2
Property, plant and equipment	A\$m	0.2	1.1	0.9	0.9	0.9	0.9
Goodwill and other intangibles	A\$m	17.6	12.5	10.1	8.1	8.1	8.1
Other assets	A\$m	20.9	20.8	22.2	21.4	21.4	21.4
Total Assets	A\$m	106.2	90.9	84.6	87.2	89.9	94.6
Trade and other liabilities	A\$m	8.7	5.7	2.5	3.1	3.7	4.4
Borrowings	A\$m	1.3	0.0	0.0	0.0	0.0	0.0
Other liabilities	A\$m	9.0	7.5	7.0	7.0	7.0	7.0
Total Liabilities	A\$m	18.9	13.2	9.5	10.1	10.7	11.4
Net assets	A\$m	87.4	77.7	75.1	77.1	79.2	83.1
Net tangible assets	A\$m	69.8	65.2	65.0	69.1	71.1	75.1
Invested capital	A\$m	63.0	63.5	66.3	63.4	63.2	63.0
Tangible invested capital	A\$m	45.4	51.1	56.3	55.3	55.1	54.9
Contributed equity	A\$m	98.9	99.0	98.7	98.7	98.7	98.7
Reserves	A\$m	35.9	26.2	50.3	50.3	50.3	50.3
Accumulated losses	A\$m	-46.9	-47.4	-73.9	-71.8	-69.7	-65.8
Non-controlling interests	A\$m	-0.4	0.0	0.0	0.0	0.0	0.0
Total equity	A\$m	87.4	77.7	75.1	77.1	79.2	83.1
Basic shares on issue	m	83.4	83.4	83.1	83.1	83.1	83.1

INVESTMENT FUNDAMENTALS		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
FuM	\$m	3,325	3,050	3,312	3,617	3,934	4,320
Management fees / FuM	%	1.08%	1.14%	1.13%	1.09%	1.08%	1.09%
Performance fees / FuM	%	0.84%	0.00%	0.00%	0.13%	0.30%	0.40%
Revenue / FuM	%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Cost to income ratio	%	57.3%	89.7%	91.0%	85.0%	80.4%	77.2%
ROE - reported	%	23.3%	5.1%	4.5%	6.7%	9.7%	12.4%
Net debt	A\$m	-24.4	-14.2	-8.7	-13.7	-16.0	-20.1
Interest cover	x	-49.6	-0.3	-4.5	-23.3	-64.1	-145.7
Gearing (net debt / EBITDA)	x	-0.77	-3.83	-2.78	-2.17	-1.57	-1.43
Leverage (net debt / invested capit)	x	-0.39	-0.22	-0.13	-0.22	-0.25	-0.32

DUPONT ANALYSIS		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
Net Profit Margin	%	25.3%	-1.4%	-1.7%	6.9%	10.4%	13.1%
Asset Turnover	x	0.65	0.36	0.40	0.49	0.59	0.67
Return on Assets	%	0.16	0.00	-0.01	0.03	0.06	0.09
Financial Leverage	x	0.91	1.19	1.15	1.13	1.13	1.14
Return on Equity	%	17.9%	-0.6%	-0.8%	3.8%	6.9%	10.0%

HALF YEARLY DATA		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
Management fees	A\$m	41.8	36.0	35.1	37.8	40.7	45.1
Performance fees	A\$m	32.7	0.0	0.0	4.4	11.3	16.5
Total fee revenue	A\$m	74.5	36.0	35.1	42.2	52.0	61.6
Net fund direct expenses	A\$m	3.1	2.9	3.1	3.2	3.4	3.5
Operating expenses	A\$m	16.3	18.2	19.1	21.7	24.5	27.1
Team profit share	A\$m	23.2	11.1	9.8	10.9	14.0	16.9
Operating EBITDA	A\$m	31.8	3.7	3.1	6.3	10.2	14.1
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Underlying profit after tax	A\$m	20.4	4.2	3.5	5.1	7.5	10.1
Reported NPAT	A\$m	18.9	-0.5	-0.6	2.9	5.4	8.1
Cash NPAT	A\$m	21.8	3.0	0.4	3.9	6.0	8.7
EPS - basic adjusted	A\$m	25.2	5.1	4.2	6.1	9.1	12.2
EPS - diluted cash	cps	20.1	2.7	0.4	3.5	5.4	7.9
EPS - diluted reported	cps	17.4	-0.4	-0.5	2.6	4.9	7.3
DPS	cps	20.0	3.0	1.0	3.0	4.0	6.0

CASH FLOW		FY22A	FY23A	FY24E	FY25E	FY26E	FY27E
Net operating cashflow	A\$m	25.2	0.1	-0.3	4.6	8.0	10.3
Investment							
Capital expenditure	A\$m	-1.6	-2.7	1.1	0.0	-0.6	-0.6
Acquisitions and growth capex	A\$m	6.2	2.4	5.0	0.0	2.0	2.0
Net cash flow	A\$m	5.8	-11.5	-7.7	3.7	2.1	3.5

Source: MST Access

Figure 2: Interims

Pengana Capital													
Year end 30-June													
INCOME STATEMENT													
	FY22A	1H23a	2H23a	FY23A	1H24a	2H24e	FY24E	1H25e	2H25e	FY25E	1H26e	2H26e	FY26E
Management fees	41.8	18.1	17.9	36.0	17.4	17.7	35.1	18.6	19.2	37.8	19.9	20.8	40.7
Performance fees	32.7	0.0	0.0	0.0	0.0	0.0	0.0	1.7	2.7	4.4	5.5	5.8	11.3
Total fee revenue	74.5	18.1	17.9	36.0	17.4	17.7	35.1	20.3	21.9	42.2	25.5	26.6	52.0
Net fund direct expenses	3.1	1.5	1.4	2.9	1.5	1.5	3.1	1.6	1.6	3.2	1.7	1.7	3.4
Operating expenses	16.3	8.3	10.0	18.2	8.3	10.8	19.1	10.3	11.4	21.7	11.7	12.7	24.5
Team profit share	23.2	5.8	5.3	11.1	5.0	4.8	9.8	5.2	5.7	10.9	6.9	7.2	14.0
Total operating expenses	42.7	15.6	16.7	32.3	14.9	17.1	32.0	17.2	18.7	35.8	20.3	21.6	41.9
Operating EBITDA	31.8	2.5	1.2	3.7	1.8	0.6	3.1	3.1	3.2	6.3	5.2	5.0	10.2
Underlying profit before income tax	29.2	3.8	2.3	6.0	3.2	1.1	5.0	3.5	3.7	7.3	5.5	5.3	10.8
Underlying profit after tax	20.4	2.6	1.6	4.2	2.2	0.8	3.5	2.5	2.6	5.1	3.8	3.7	7.5
Reported NPAT	18.9	-0.3	-0.2	-0.5	-0.9	-0.4	-0.6	1.4	1.5	2.9	2.8	2.6	5.4
Cash NPAT	21.8	0.4	2.6	3.0	-0.3	0.1	0.4	1.9	2.0	3.9	3.1	2.9	6.0
Dividends													
Ordinary Dividends (cents/shr.)	20.0	2.0	1.0	3.0	1.0	0.0	1.0	1.0	2.0	3.0	2.0	2.0	4.0
Special Dividends (cents/shr.)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total dividends (cents)	20.0	2.0	1.0	3.0	1.0	0.0	1.0	1.0	2.0	3.0	2.0	2.0	4.0
Franking	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Payout ratio (% of adj NPAT)	106%	83%	70%	78%	50%	50%	32%	50%	50%	65%	50%	50%	59%
FUM AND OTHER METRICS													
	FY22A	1H23a	2H23a	FY23A	1H24a	2H24e	FY24E	1H25e	2H25e	FY25E	1H26e	2H26e	FY26E
FUM													
Open	3,974	3,325	3,219	3,325	3,050	3,055	3,050	3,312	3,478	3,312	3,617	3,768	3,617
Flows	74	-47	-105	-152	-18								
Distributions	-149	-123	-50	-173	-80								
Mark-to-Markets	-574	95	243	338	102								
Close	3,325	3,219	3,050	3,050	3,055	3,312	3,312	3,478	3,617	3,617	3,768	3,934	3,934
Growth %	-16%	-3%	-5%	-8%	0%	8%	9%	5%	4%	9%	4%	4%	9%
Average FUM (A\$m)	3,885	3,294	3,045	3,170	3,053	3,184	3,118	3,395	3,548	3,471	3,693	3,851	3,772

Source: MST Access, Company Reports

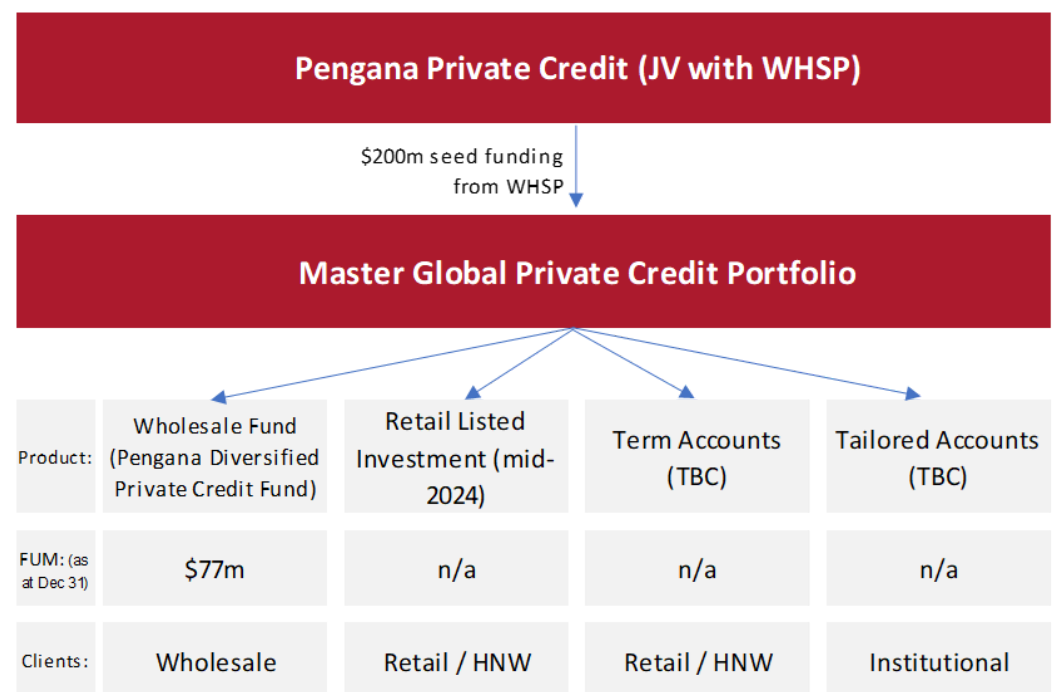
Global Private Credit (GPC)

Emerging Opportunity

In April 2023 PCG announced a joint venture with Washington H. Soul Pattinson (WHSP) to jointly own and operate Pengana Private Credit, allowing Australian investors to access institutional-grade global private credit investments. On 9 April 24, PCG has acquired Washington H. Soul Pattinson's (WHSP) share of Pengana Credit Pty Ltd (PCP). This has not affected the \$200m of seed funding WHSP has earmarked to establish a diversified portfolio of global private credit investments, (with \$77m deployed so far), and WHSP remains PCG's largest shareholder. The transaction has also allowed for simplified accounting, although PCG did not provide a breakdown of the terms or revised economics, which we expect to hear more about at its next result.

The private credit business will have an overarching portfolio and will include four products, one of which (Pengana Diversified Private Credit Fund) is live, with the remainder in the works and to be available over the next year. Pengana announced in July 2023 that it had appointed Mercer as its investment advisor on its portfolio construction.

Figure 3: Pengana Private Credit Buckets



Source: Company reports, MST Access

Expanding Product Set

Wholesale Fund

Pengana's Diversified private credit fund was launched in October 2023, and is primarily targeted towards family offices, HNW's and institutional investors. It targets returns of RBA Cash rate plus 7-9% p.a. (currently 11.35% - 13.35%).

Retail Listed Investment Structure

IPO is planned with preliminary marketing progressing well, this should go live in 1H25. The client focus is on financial advisors, direct retail, and high net-worth investors. Pengana is setting up the product where it will allow retail investors to put in a quarterly redemption, or, if they don't like the unit price, sell on market – which should theoretically mean that the vehicle should trade close to its NAV.

Term & Tailored Accounts

Pengana will allow for 12, 24, and 60-month term accounts with monthly income payments. Both products will have new age platform technology. Term Accounts will be targeted towards retail and HNW clients, with tailored accounts targeted towards institutional and larger dealer groups seeking bespoke solutions.

Product Innovation

Breaking Through the Traditional Model

The traditional model for boutique fund managers will usually begin by seeding a fund, it will then wait up to years to establish a track record, and then assuming it has performed well, will begin to sell into institutional / retail.

There are a few pain points here, particularly for smaller fund managers. There is long lead times between seeding and earning fees, it is capital intensive, and finally, the distribution framework is extremely competitive.

Pengana is breaking the chain with its innovative Global Private Credit business. We outline why below:

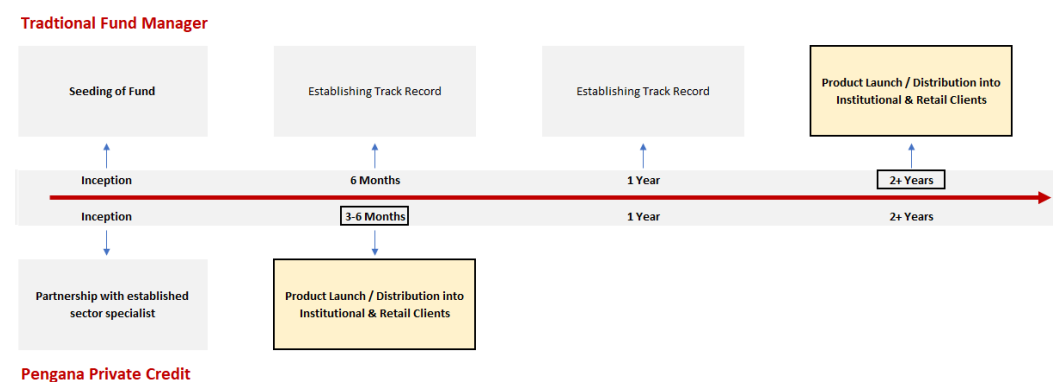
Partnerships / JV's

1. PCG had originally entered into a JV with a significant player in funds manager, Washington H. Soul Pattinson. Soul Patts provided Pengana with \$200m in seed capital which is currently being deployed. PCG now has 100% of the economics.
2. PCG also partnered and appointed Mercer as its investment consultant for the master GPC portfolio. This type of partnership has drastically reduced lead times, ultimately allowing for products to be launched within months.

Product Innovation / Distribution

1. PCG has also understood where the opportunities lie and has invested into its product platform to develop market-leading digital capabilities.
2. It has outlined four separate products (to-date), differing from a standard fund, to allow for sophisticated distribution channels, including a wholesale fund (already in market), a retail listed investment vehicle, term accounts, and tailored accounts, all to be launched imminently.

Figure 4: Inception of Fund to Launch Timeline



Source: MST Access

Updated Economics of Pengana Private Credit

Washington H. Soul Pattinson jointly owned Pengana Private Credit (50%) which was equity accounted in PCG accounts. Following the update from PCG on 9 April 24, PCG has acquired the remaining 50% from WHSP and all economic interest.

It has not provided a breakdown of revised economics, however prior to the announcement, the breakeven for Pengana was ~\$200m of FUM (excluding \$200m seed fund which will pass-through), which we assume will remain the same.

Prior to the acquisition of the remaining 50%, it was estimated that for every \$100m of external FUM above the breakeven amount, PCG would generate incremental EBITDA of ~\$1m and net profit of ~\$700k.

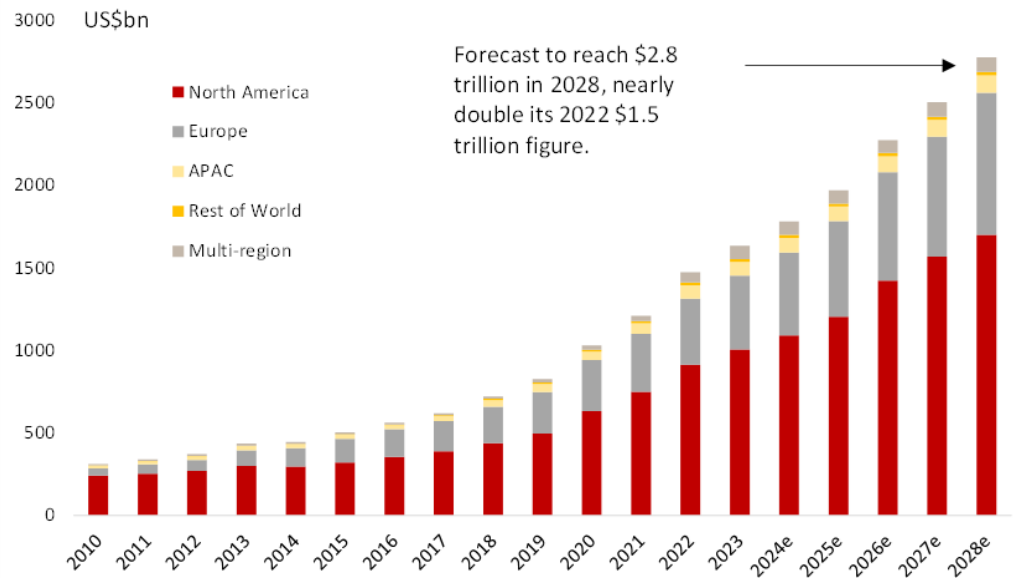
Advantages of Alternatives

Growing as an Asset Class

Global alternatives AUM is expected to increase to \$24.5 trillion by the end of 2028, according to leading alternative asset management data company Preqin. This compares to an estimated figure of \$16.3 trillion at the end of 2023.

Private credit is forecast to grow at a quicker rate, with expectations that it will nearly double in AUM by 2028, our graph below highlights the importance of Pengana providing access to global private credit, with the majority of growth to come from the US and Europe.

Figure 5: Private Debt Asset Class Forecast (Preqin est.)

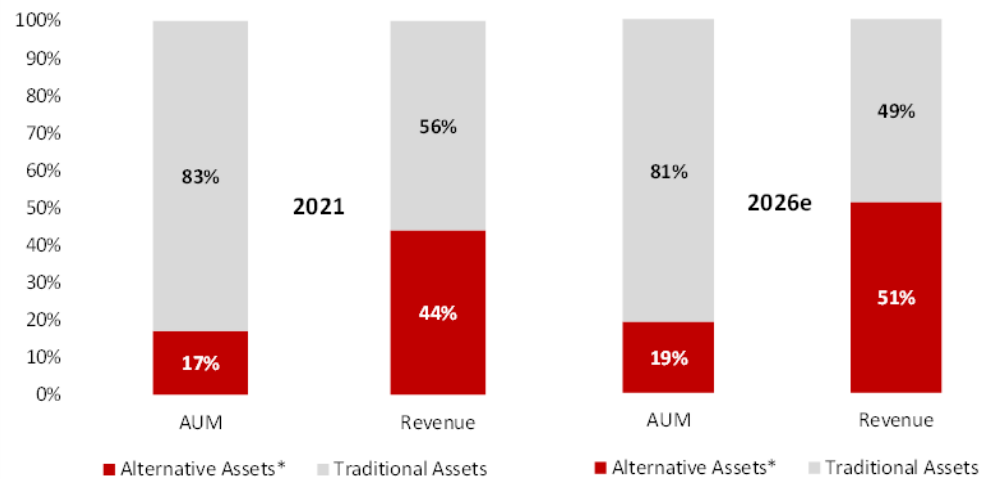


Source: Preqin, MST Access

Growing as a % of Revenue

The predicted growth in alternative AUM is largely in line with other more traditional asset classes, but the growth in revenue differs significantly. In 2021, global alternative asset AUM represented 17% of overall AUM, but it alternatives represented 44% of global overall revenue. Preqin forecast that in 2026, alternative assets will make up 19% of AUM, but 51% of total revenue.

Figure 6: Alternative Assets Share of Global Revenue % - 2021 vs 2026e



Source: Preqin, MST Access

Funds Overview

Broad Base of Funds

Pengana has both a broad scope of funds on offer, including its listed investment company (ASX:PIA) and listed investment trust (ASX:PE1), as well as significant further capacity for FUM.

The focus over the last few years has been to re-position the business for future growth at higher margins, specifically, in private markets including both private equity and private credit. We expect that over time PCG will continue to diversify its funds through new strategies and businesses.

Pengana averages a management fee of ~1.18% and a historical gross fee margin of ~1.80%, implying an average performance fee of 0.62%. We expect that the ~75% of funds under management that is subject to performance fees to revert to the mean of 0.62% over the next few years.

Figure 7: Pengana Capital Group Funds Overview

Pengana Capital Group															
	Core Funds FUM: \$1.3b				Small Cap Funds FUM: \$0.8b		Specialty Funds FUM: \$0.8b					Pengana Private Credit \$0.1b			
Fund:	Axiom International Ethical Funds	Harding Loewner International Fund	Australian Equities Fund	Pengana International Equities Ltd (ASX:PIA)	Global Small Companies Fund	Emerging Companies Fund	Pengana Private Equity Trust (ASX:PE1)	WHEB Sustainable Impact Fund	High Conviction Equities Fund	High Conviction Property Securities Fund	Alpha Israel Fund	Master Global Private Credit Portfolio			
FUM: (A\$m) at 31 December 2023	\$355m	\$43m	\$624m	\$320m	\$129m	\$709m	\$432m	\$256m	\$40m	\$18m	\$29m	Bucket 1	Bucket 2	Bucket 3	Bucket 4
Indicative Further Capacity	Very Large	Very Large	Limited	Very Large	~\$500m	Limited	Very Large	~\$800m	~\$200m	~\$700m	~\$500m	Pengana Diversified Private Credit Fund	Retail Listed Vehicle (Mid-2024)	Term Accounts (2024)	Tailored Accounts (2024)
												\$77m	n/a	n/a	n/a
												Very Large	Very Large	Very Large	Very Large

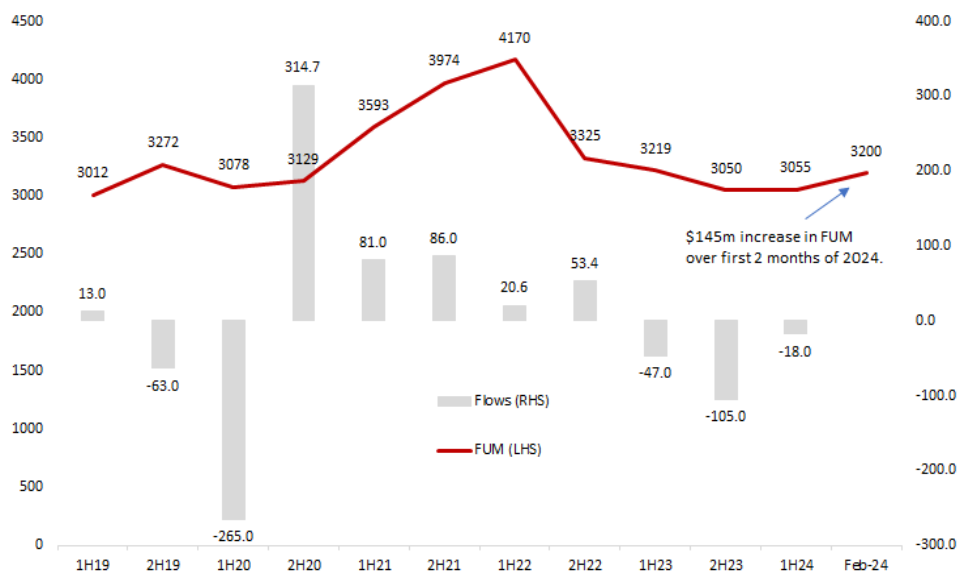
Source: Company Reports, MST Access estimates

Funds Under Management

Stabilising, anticipate net-flows turning positive on back of GPC

After significant falls in Pengana's group FUM over 2022, which included the divestment in Lizard, it has largely maintained a stable trajectory over the past 6 months. The business has undergone a repositioning and any further moderation in its non-private market fum should be counterbalanced by new growth initiatives.

Figure 8: Pengana FUM and Net-flow profile



Source: Company reports, MST Access

Valuation

Transfer of Coverage

We note that this is a transfer of coverage.

We utilise a DCF valuation methodology as detailed in the below table.

Other equity market considerations such as short sales; any likely forthcoming changes in index inclusion; depth of stock research coverage; composition of and change in the mix of investors (such as founders, board and staff, domestic institutions, foreign institutions, and retail investors) are not incorporated in our valuation; however, investors should consider such factors if they seek to develop a price target for the company.

We estimate PCG's equity beta to be 1.6. We use a risk-free rate of 3.0%, and equity risk premium at 5.0%, to achieve an overall cost of equity of 12.6%, and assume terminal growth rates of 3.0%.

Figure 9: Valuation

DCF Valuation	
WACC	12.6%
Ke (cost of equity)	12.6%
Kd (cost of debt)	4.5%
	\$m
NPV	140
Net-Cash	14
Total Valuation	154
Share Count (not incl. Treasure shares) (m)	83.4
Valuation per share (\$0.00)	1.85

Source: MST Financial

Assumptions

In our forecasted cashflow, we assume that capex will remain stable at \$0.6m per year. We also assume a risk-free rate of 3.0% and an equity risk premium of 6.0% with a beta of 1.6 to derive a cost of equity of 12.6%, and a terminal growth rate of 3.0%, resulting in a valuation of \$1.85 per share, down from the last valuation of \$2.28 per share, noting that this is a transfer of coverage.

Figure 10: MST Access NPV of Future Cashflows

	Jun 23	Jun 24	Jun 25	Jun 26	Jun 27	Jun 28	Jun 29	Jun 30	Jun 31	Jun 32	Jun 33	Perpetuity
Operating cash flow	3.7	3.1	6.3	10.2	14.1	18.8	23.4	27.5	32.1	35.3	38.1	
Stay in business capex	-2.7	1.1	0.0	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6	
Maintainable cash flow	1.0	4.3	6.3	9.6	13.5	18.2	22.8	26.9	31.5	34.7	37.5	
Tax paid	-7.1	-0.5	-2.2	-2.9	-4.3	-5.8	-7.2	-8.5	-9.9	-10.9	-11.8	
Total Cashflow	-6.1	3.7	4.2	6.7	9.1	12.4	15.6	18.4	21.6	23.8	25.6	280.6
		-161.7%	11.1%	60.2%	37.0%	36.1%	25.6%	17.9%	17.4%	10.0%	7.9%	

Source: MST Financial

Investment Thesis

Pengana Capital Group (“Pengana”) is a high growth “house of funds” style fund manager. It offers a diversified range of investment products both directly and in partnerships with leading global investment managers. This enables Pengana to provide investors with access to a wide range of attractive investment products which in many cases they would not otherwise be able to access.

Pengana shares in the economics from these offerings with the underlying investment teams. This ensures a strong incentives and alignment between investment teams and Pengana. The structure also enables Pengana to continue to expand its product offerings at a faster pace than rivals who look to keep all investment management operations in house.

This structure enables Pengana to achieve growth from multiple sources, resulting in a very high growth rate:

- Performance of existing funds, including 100% of performance fees from PIA and PE1, and sharing performance fees with its fund managers in most other funds.
- Flows from existing clients into existing funds, with retail FUM typically sticker than wholesale FUM.
- Flows from new clients into existing funds, aided by investments into distribution including fund ratings and better penetration of financial planners.
- Creation of new funds and flows into them from existing clients (i.e., cross -sell)
- Improving operating leverage on the existing cost base

Complimenting this high growth are the modest valuation metrics on which the stock trades. Given its substantial performance fees and the diversity of funds capable of earning performance fees we expect a portion are reoccurring, combined with its high growth, the stock trades on very modest forward multiples, while it also looks attractive using various intrinsic valuation methods including discounted free cashflows to equity, a dividend discount model and a generalised residual income model.

Cost base higher to harness potential of Private Credit business: Pengana has a bigger cost structure then would otherwise be necessary. Whilst it would normally be wise to look at trimming costs, Pengana is conscious of the opportunity at hand and has deliberately invested more into the business (primarily private credit, as well as the technology behind some of its products) to drive the expanded offering.

Risks and sensitivities

Strategic

Pengana Capital Group is subject to a significant number of regulatory requirements, and could suffer from adverse changes to the requirements, including in Australia:

- Anti-money laundering and counter terrorist financing requirements administered by Austrac;
- Privacy requirements administered by the Privacy Commissioner.
- Financial Service licencing and Credit licencing administered by the Australian Securities and Investments Commission (ASIC);
- Australian Consumer Law and unfair contract terms contained in the Corporations Act administered by the Australian Competition and Consumer Commission (ACCC);
- Taxation legislation administered by the Australian Taxation Office (ATO);
- Accounting standards required under the Corporations Act administered by the Australian Accounting Standards Board (AASB) and ASIC.

Pengana Capital Group operates in a competitive environment where performance can vary and new or rival offerings emerge periodically. Sometimes consolidation of fund managers occurs, such as Pengana's own merger with Hunter Hall several years ago. These risks present to investors in the form of both strategic M&A risks and general market risks.

Financial

Being a fund manager, Pengana Capital Group has a range of risks and sensitivities applicable to most companies in the financial sector. These include:

- **Investment performance** – investors seek out funds with a strong performance history, so fund performance tends to be a reasonable indicator of future flows. Furthermore, with many of Pengana's funds featuring performance fees, weak investment performance will also impact Pengana's performance fee earnings, and hence its profitability.
- **Macroeconomic conditions** – many of the following risks vary through the economic cycle. Loose monetary conditions, such as those currently being experienced, suppress many of these risks which can then emerge suddenly as macroeconomic policy tightens, and conditions deteriorate. Economic stimulus to counter COVID-19 has led to a strong market recovery following the aggressive market sell-off at the start of the pandemic. Where funds are optimised for a particular investment style, macroeconomic conditions can have a significant impact on the relative performance of that style compared to other investment styles.
- **Compliance risks** – There are many regulations that companies in the finance sector need to follow, outlined above in strategic risks, including anti-money laundering and counter terrorist financing know your customer requirements, where failure to comply with the regulatory requirements can lead to material financial penalties or litigation.

Operational

Most companies, including Pengana Capital Group, have a range of operational risks. These include:

- **Governance** – Increasingly an investment focus as part of ESG, governance risks include all matters of agency costs within the business, including delegated responsibilities and authorisations, internal controls and how conflicts of interest are addressed.
- **Key personnel** – Pengana Capital Group's ability to scale its business assumes availability of suitably qualified staff and a reliance on key personnel. This is particularly relevant for fund managers, where portfolio managers carry significant key personnel risk. Pengana's house of funds approach, and strong incentive alignment with portfolio managers are examples of the methods employed to manage this risk.
- **Information technology** - Should Pengana Capital Group's key technology infrastructure become corrupted such as from hardware failure or malware it would be highly disruptive to Pengana Capital Group's operations. Furthermore, IT hardware and software becomes obsolete after a few years and requires capital investments to be updated, otherwise the company is at high risk of becoming inefficient and being superseded by its competitors.

Personal disclosures

Joseph Licciardi and Lafitani Sotiriou received assistance from the subject company or companies in preparing this research report. The company provided them with communication with senior management and information on the company and industry. As part of due diligence, they have independently and critically reviewed the assistance and information provided by the company to form the opinions expressed in this report. They have taken care to maintain honest and fair objectivity in writing this report and making the recommendation. Where MST Financial Services or its affiliates has been commissioned to prepare content and receives fees for its preparation, please note that NO part of the fee, compensation or employee remuneration paid has, or will, directly or indirectly impact the content provided in this report.

Company disclosures

The companies and securities mentioned in this report, include:

Pengana Capital Group (PCG.AX) | Price A\$0.85 | Target price A\$1.85 | Recommendation -;

Price, target price and rating as at 10 April 2024 (not covered)*

Additional disclosures

This report has been prepared and issued by the named analyst of MST Access in consideration of a fee payable by: Pengana Capital Group (PCG.AX)

Other disclosures, disclaimers and certificates

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