

Product Review

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

About this Review

ASSET CLASS REVIEWED	PROPERTY AND INFRASTRUCTURE
SECTOR REVIEWED	AUSTRALIAN LISTED PROPERTY
TOTAL FUNDS RATED	15

About this Fund

ASIC RG240 CLASSIFIED	NO
FUND REVIEWED	PENGANA HIGH CONVICTION PROPERTY SECURITIES FUND
APIR CODE	PCL8246AU
PDS OBJECTIVE	TO OBTAIN RETURNS GREATER THAN THE S&P/ASX 300 A-REIT (AUD) TR INDEX OVER ROLLING THREE YEAR PERIODS AFTER FEES.
INTERNAL OBJECTIVE	AIMING FOR 2% P.A. (AFTER FEES) OUTPERFORMANCE OF THE BENCHMARK OVER ROLLING THREE YEAR PERIODS.
STATED RISK OBJECTIVE	NONE
DISTRIBUTION FREQUENCY	QUARTERLY
FUND SIZE	\$16M (APRIL 2023)
FUND INCEPTION	11-03-2020
ANNUAL FEES AND COSTS (PDS)	0.93% P.A.
PERFORMANCE FEE	15% OF EXCESS RETURN ABOVE BENCHMARK (AFTER FEES & COSTS)
RESPONSIBLE ENTITY	PENGANA CAPITAL LIMITED

About the Fund Manager

FUND MANAGER	PENGANA CAPITAL LIMITED
OWNERSHIP	PENGANA CAPITAL GROUP LTD (ASX CODE: PCG)
ASSETS MANAGED IN THIS SECTOR	\$16M (APRIL 2023)
YEARS MANAGING THIS ASSET CLASS	3

Investment Team

PORTFOLIO MANAGER	AMY PHAM
INVESTMENT TEAM SIZE	3
INVESTMENT TEAM TURNOVER	NIL
STRUCTURE / LOCATION	CENTRALISED / SYDNEY

Investment process

INVESTMENT STYLE	HIGH CONVICTION, BENCHMARK UNAWARE
BENCHMARK	S&P/ASX 300 A-REIT ACCUMULATION INDEX
TYPICAL STOCK NUMBERS	10-20
STOCK LIMITS	20% INDEX STOCKS OR EQUAL TO INDEX WEIGHT IF >20%; 2-5% NON-INDEX STOCKS
REGION / SECTOR LIMITS	<10% GLOBAL REITS AND REAL ESTATE-RELATED STOCKS
CASH LIMIT	20%

Fund rating history

MAY 2023	INVESTMENT GRADE
MAY 2022	INVESTMENT GRADE

What this Rating means

The 'Investment Grade' rating indicates that Lonsec has conviction the financial product can generate risk adjusted returns in line with relevant objectives. However, if applicable, Lonsec believes the financial product has fewer competitive advantages than its peers.

Strengths

- Two senior personnel have previously worked closely together and have good experience in the analysis of Australian property securities.
- The Fund is a high conviction portfolio of quality stocks that is differentiated from peers by holding a higher proportion of off-benchmark stocks in line with the Manager's growth philosophy.
- Strong component of ESG factored into the valuation process.
- Small FUM allows the Manager to be a nimble investor and take meaningful positions in non-benchmark stocks.

Weaknesses

- The Fund has a relatively short track record and to date has underperformed both the Benchmark and peer median.
- Unlike some more highly rated A-REIT managers, the investment team does not have access to a direct commercial property business in the Manager's wider business.
- Some business risk with small FUM, but has support of the ASX-listed Pengana Capital Group.

Fund Risk Characteristics

	LOW	MODERATE	HIGH
BUSINESS SUSTAINABILITY RISK			●
CAPITAL VOLATILITY			●
FOREIGN CURRENCY EXPOSURE	●		
SECURITY CONCENTRATION RISK		●	
SECURITY LIQUIDITY RISK	●		

Risk categories are based on Lonsec's qualitative opinion of the risks inherent in the financial product's asset class and the risks relative to other financial products in the relevant Lonsec sector universe.

BIometrics

Aggregated risks

	1	2	3	4	5	6	7
STD RISK MEASURE							●

A Standard Risk Measure score of 7 equates to a Risk Label of 'Very High' and an estimated number of negative annual returns over any 20 year period of 6 or greater. This is a measure of expected frequency (not magnitude) of capital losses, calculated in accordance with ASFA/FSC guidelines.

We strongly recommend that potential investors read the product disclosure statement Lonsec Research Pty Ltd ABN 11 151 658 561 • AFSL No. 421 445 • This information must be read in conjunction with the warning, disclaimer, and disclosure at the end of this document. This report supersedes all prior reports.

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

	LOW	MODERATE	HIGH
RISK TO INCOME			●

Features and benefits

	LOW	MODERATE	HIGH
COMPLEXITY		●	
ESG		●	

Fee profile

	LOW	MODERATE	HIGH
FEES VS. UNIVERSE			●
FEES VS. ASSET CLASS		●	
FEES VS. SUB-SECTOR			●

Fee BIOMetrics are a function of expected total fee as a percentage of expected total return.

What is this Fund?

- The Pengana High Conviction Property Securities Fund ('the Fund') is a long-only, high conviction Australian property securities fund. The objective is to obtain returns greater than the S&P/ASX 300 A-REIT TR Index ('the Benchmark') over rolling three year periods after fees. Internally, it aims to outperform the Benchmark by 2% p.a. (after fees) over rolling three year periods.
- Pengana Capital Limited ('Pengana' or 'the Manager') is the Fund's Responsible Entity and Investment Manager. Pengana seeks investment opportunities in Australian real estate investment trusts (A-REITs), funds management businesses and property developers. The Fund can also invest up to 10% of the portfolio in international property securities and property-related businesses, although to date this has been limited.
- The investable universe comprises around 50 stocks (30 from the A-REIT index and 20 selected non-index stocks). Pengana seeks to pick the 'best-of-breed' property managers, with quality assets that will generate a sustainable free cash flow, backed by a strong balance sheet to support future growth.
- The portfolio is reasonably concentrated when compared to the wider peer group, with a maximum of 20 stocks. The Fund is relatively 'benchmark unaware' and therefore has a relatively high 'Active Share' (which is a measure of the difference between the portfolio composition and the Benchmark). The Fund also has a high proportion of stocks from alternative property sub-sectors (approximately 23% compared to the Benchmark's 6% at the time of this report).
- The Manager generally has a long-term investment approach (portfolio turnover expected to be 40%-50%) and expects to be fully invested, but permits a cash holding of up to 20%.
- While the product is not an 'ethical' fund, the Manager has a focus on ESG factors incorporated into its assessment of stocks as part of the overall valuation process (30% weighting).
- The Fund's PDS dated 13 December 2022 disclosed Annual Fees and Costs ('AFC') totalling 0.93% p.a. This value comprises (1) Management Fees and Costs of 0.70% p.a.; (2) Performance Fee Costs of 0.10%; and (3) Net Transaction Costs of 0.13%. In line with RG97, some fees and costs have been estimated by the issuer

on a reasonable basis. Actual fees and costs may vary to these estimates.

- The Fund charges a performance fee of 15% of the excess return above the Benchmark (after fees and costs), payable half yearly. Pengana is one of the few funds in Lonsec's A-REIT/Real Assets sector to directly charge a performance fee at the Fund level. The performance fee is an estimate based on the average over five years.
- The Fund charges buy/sell spreads set at 0.25%/0.25% upon exit when buying and selling units directly with the Unit Registry. These spreads can be subject to change, most notably during periods of market volatility, and can be sourced from the Manager's website. Additionally, spreads on the ASX may be different to these spreads.

Using this Fund

This is General Advice only and should be read in conjunction with the Disclaimer, Disclosure and Warning on the final page.

- Lonsec notes that the Manager has produced a Target Market Determination (TMD) which forms part of the Responsible Entity's Design and Distribution Obligations for the Fund. Lonsec has collected the TMD that has been provided by the Manager and notes that this should be referred to for further details on the Target Market Summary, Description of Target Market and Review Triggers.
- As a 'long only' Australian property securities product, the Fund would form part of the growth component of a balanced portfolio. The Fund is suitable for medium and high-risk profile investors with a 5+ year investment time horizon.
- While the Fund aims to invest in A-REITs that deliver reliable long-term cash flows, the Fund is also subject to equity market risk. This means movements (both positive and negative) in the share prices of the underlying securities in the portfolio will affect the Fund's returns. Investors should therefore be aware that the Fund may experience periods of negative returns and that there is a risk of potential capital loss being incurred on their investment.
- Lonsec notes that in general, Australian listed property and infrastructure funds exhibit relatively high levels of concentration risk compared to broader Australian equity strategies, reflecting the concentrated nature of the benchmark.
- The Manager has the ability to take significant active positions away from the Benchmark. Investors should therefore be aware that the Fund has the potential to deliver returns that deviate materially from the Benchmark.

Suggested Lonsec risk profile suitability

SECURE	DEFENSIVE	CONSERVATIVE	BALANCED	GROWTH	HIGH GROWTH
	●	●	●	●	●

For guidance on appropriate asset allocations and risk profiles, refer to the latest Lonsec Strategic Asset Allocation Review and Risk Profile Definitions on our website.

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

Changes Since Previous Lonsec Review

- Where a security has a weighting of >20% of the Benchmark, the Manager now has the ability to invest up to the index weight of the security.
- There have been no other material changes since the previous review.

Lonsec Opinion of this Fund

People and resources

- Pengana Capital's Australian property securities investment team comprises three members, which is typical for the peer group. Chief Investment Officer Nick Griffiths heads the Investment Committee which has oversight of the strategy and meets monthly on a formal basis. The A-REIT team members are employed by Pengana Capital and utilise the central resources of the firm based in Sydney.
- Amy Pham is the Portfolio Manager and has 27 years of experience in property securities investment. Prior to establishing the A-REIT strategy at Pengana in February 2020, Pham spent six years at Charter Hall Maxim (previously Folkestone Maxim) as an Analyst/Portfolio Manager, responsible for a high conviction A-REIT mandate. Pham contributed to the strong performance of the Charter Hall Maxim Property Securities Fund over a number of years, but was not the responsible portfolio manager. As such, Lonsec considers Pham to have a relatively limited track record as a front-line A-REIT portfolio manager. Lonsec notes the composite strategy performance track record provided by the Manager, consisting of an amalgam of the performances of the Fund, 'simulated' Portfolio and broader High-Conviction mandate dating back to August 2017, shows performance to be just ahead of the Benchmark after adjusting for the high cash holding in the first two months of the actual Fund. Pham holds ultimate accountability for the Fund.
- Jade Ong is an Investment Specialist with 19 years of experience in property securities investment and has strong credentials as part of Macquarie's real estate corporate advisory team in London and Sydney. Ong also worked for several years as Assistant Portfolio Manager alongside Pham on a property securities fund at IAG. Ong joined Pengana in June 2020 as an Investment Specialist. Ong is also responsible for the ESG data collection and the assessment is undertaken in conjunction with the other team members.
- Sam Craig joined Pengana in December 2021 as an Investment Analyst. He has seven years of property and finance experience, having most recently worked as a Senior Researcher in direct property at Charter Hall.
- The A-REIT team interact with the wider Australian Equities team at Pengana, by attending a weekly meeting where knowledge on stocks is shared by both teams. Company visits are also sometimes undertaken on a joint basis. The investment decisions of both teams remain separate and each may hold different A-REIT stocks.
- The A-REIT team has extensive industry contacts and receives input from direct property groups; real estate research and transaction groups; property securities broker research; and economists. However, Pengana

does not have a direct property business of its own, where some competing A-REIT Managers have the benefit of these close ties.

- The Pengana A-REIT team does not have a dedicated trader, with this task mainly performed by Pham, backed by Craig. This has the potential to be distracting for the Portfolio Manager in particular. However, this is a low turnover strategy and trading activity is relatively infrequent.
- While there is no direct equity ownership in the property securities business, in Lonsec's view there is sufficient alignment of interests between the investment team and investors. Subject to the achievement of key criteria, Pham and Ong are eligible for a profit share of the business after a period of three years, and Lonsec notes they have both also invested their own money into the Fund.
- As sole Portfolio Manager, Pham is considered to pose a high level of key person risk given the nascent nature of the strategy and her central role in its management. While this is mitigated to some extent by the profit share arrangement, Lonsec believes an equity share structure would create better alignment with investor interests.

Research and portfolio construction

- Pengana follows a logical, structured and repeatable investment process that Pham has utilised in previous roles at other fund managers. The Manager begins with a 'top-down' qualitative assessment of secular themes/trends that are driving growth within the property sector, with a view on picking the best 'core' and 'growth' property sub-sectors. Pengana analyses a range of macroeconomic, demographic and real estate market factors while drawing upon research from a range of sources. This is similar to some of its competitors with a small amount of funds under management. That said, Lonsec highlights that unlike some peer A-REIT managers, the Pengana team does not have access to a direct commercial property business in the Manager's wider business.
- This is complemented by a detailed fundamental 'bottom-up' analysis of both quantitative and qualitative factors, which are equally weighted. The team maintains proprietary financial models which combine these factors into a 'Valuation Ranking Model' to help select the most attractive stocks for the portfolio compared to current pricing. Lonsec observes that the team's reliance on broker research has significantly lessened to the point where the team has now developed proprietary models for over 80% of the stocks in its Australian investable universe, with some additional models for overseas stocks. Domestic stocks not currently modelled have clearly identified higher quality peers. The key drivers of these models are now all assessed in-house.
- The component of ESG in the valuation process is one of the highest in the A-REIT sector and differentiates Pengana to some extent. However, it should be reiterated that the Fund is not an 'ethical' fund, with the only exclusions purely based on ESG factors are those on corporate governance. Nevertheless, the ranking model will be skewed towards stocks that are assessed as rating highly on ESG factors by the Pengana A-REIT team. Companies with exposure to

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

‘unethical’ sectors (e.g. alcohol, tobacco, gambling or fossil fuels) are marked down in terms of the ‘E’ and ‘S’ scores in the valuation model, based on the level of income that is generated in these sectors.

- Ong and Craig share the detailed modelling duties, with the investable universe split between them (Ong 40%; Craig 60%). While there is reasonable consistency in the process, in Lonsec’s view it relies more heavily on the experience and conviction of the investment team and may favour small and mid-cap stocks.
- There is a clear link between research and portfolio construction, where the Manager aims to build a concentrated portfolio picking ‘best of breed’ stocks, with quality assets to generate sustainable free cashflow and strong balance sheets to support future growth. To this end, stock allocation is based on the Manager’s level of conviction combined with an element of sector diversification. In keeping with the ‘benchmark unaware’ philosophy, Lonsec notes the Manager is differentiated from peers by holding a higher proportion of off-benchmark stocks.

ESG Integration

- Lonsec’s ESG integration assessment considers how rigorous, robust and structured the ESG process for the Fund is as well as how well it integrates into the overall investment process and the Manager’s overall policy and reporting framework. The assessment is not intended to assess the underlying holdings of the Fund’s portfolio or the Manager’s adherence to any form of impact, green / sustainable or ethical standards.
- At the corporate level, Lonsec views Pengana’s overall ESG policy framework and disclosure as lagging peers. The Manager has an articulated commitment to their integration of ESG within their investment process with evidence of a policy framework and improved public positioning. The ESG policy is publicly available and remains rather generic compared to peers. Pleasingly the policy lightly touches on the engagement framework, however no reporting on engagement outcomes is publicly available. While the Manager does not provide any details on their proxy voting policy, voting records for certain funds are publicly available.
- Within the management of this specific Fund Lonsec notes:
 - Lonsec considers the Manager sources ESG data within their investment process in a structured and thorough manner. The Manager enhances their external data subscriptions with a proprietary survey of portfolio companies designed to elicit more detailed and tailored information. Data to enable strong compliance checking is accessed although data collection is not as systematised as with some leading managers.
 - There are clear signs of robust ESG elements as a core component of the Manager’s research process. Pleasingly the Manager’s research process generates a proprietary score allowing downstream measurement at the portfolio level. Research is stored in a less robust manner than seen with leading peers.

- There are clear links from the Manager’s research to the stock selection process through structured adjustment of price targets to account for outsized ESG risks.
- There is monitoring of ESG characteristics of the portfolio across a number of ESG and sustainability dimensions, however this plays a limited role in overall portfolio construction. There are no Portfolio level ESG based limits or targets in place for the Fund.
- Engagement is a clear component of the Manager’s approach which is prioritised in a structured manner. Engagements are tracked and the success of that engagement is noted, however in a less robust manner than in many peers. The Manager is able to demonstrate ESG based engagements.
- Compliance Monitoring of ESG factors is deemed adequate however overall transparency provided to investors is lagging. Pleasingly, voting on the Fund is directed by the Fund’s portfolio manager directly.

Risk management

- While Pengana has some limits in place with regards to portfolio holdings, Lonsec notes these risk limits are very broad relative to peers, with large single stock limits and the ability to invest up to 10% in global REITs and property-related stocks.
 - The Fund is ‘benchmark-unaware’, reasonably concentrated (maximum of 20 stocks) and comprises a high proportion of stocks from alternative property sub-sectors. This means that the Fund’s performance is likely to at times vary considerably from that of the Benchmark.
 - The Fund is also able to take concentrated bets in smaller capitalisation stocks. As such, the Fund can potentially take on much higher active risk in comparison to sector peers. In this respect, risk management is largely embedded in the Manager’s stock selection process, which has a strong focus on the qualitative elements of the company.
 - In late 2022, the Manager made adjustments to their risk limits where if a security has a weighting of >20% of the Benchmark, the Manager now has the ability to invest up to the Benchmark weight of the security. Lonsec understands this change is designed to neutralise the effect that benchmark-dominating stocks such as Goodman Group and Charter Hall Group can have on Tracking Error. However, this increases portfolio concentration risks in such large cap names.
 - Unlike many peers, the team has no separate trader. The Manager has pre-trade compliance systems to prevent the Portfolio Manager from undertaking trades which will breach the Fund’s mandate.
 - The bias to small-mid capitalisation stocks in the portfolio adds a degree of liquidity risk and may detract from relative performance in some down markets.
 - While there is daily oversight of the strategy by the Pengana Investment Committee, it only meets on a monthly basis to review the strategy’s performance.
- ## Capacity
- As the A-REIT strategy was inceptioned relatively recently (March 2020) by Pengana, Funds under

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

Management ('FUM') is small at \$16m as at April 2023. The Pengana business has over \$3bn in total FUM, some of which is also invested in A-REITs but these are separately managed, which is sufficient to support the growth of the strategy.

- The Manager has a stated estimated capacity for the A-REIT strategy to currently be around \$1.6b-\$1.7b, which represents approximately 1.0% of the A-REIT 300 Index market capitalisation. Capacity is a relative tailwind for the Fund at present levels.
- Total capacity limits differ from manager to manager due to variances in investment styles, biases and trading strategies. Lonsec's general view is that greater FUM makes it more difficult to trade in and out of stock positions without material market impact (particularly in smaller stocks). However, there are some inherent advantages in having a large fund including: greater access to management; priority access to deal flow; and bigger dedicated team sizes. Thus Lonsec carefully weighs up a fund's investment style and objectives when considering the issue of capacity.

Fees

- Lonsec considers the total fee load for the Fund (AFC of 0.93% p.a.) to be relatively in-line with peers given the presence of a 15% performance fee.
- In terms of structure, Lonsec is generally supportive of having a low management fee plus a performance fee (rather than a high management fee) on the grounds the Fund needs to outperform the Benchmark for the Manager to be paid a share of the outperformance. Any negative performance by the Fund must be made up before a performance fee is payable.

Product

- The Fund is relatively straight forward listed A-REIT strategy and should not generally pose any meaningful operational challenges to implement. However, it may invest down the market cap spectrum which may pose some operational and liquidity challenges at times of market dislocation given the daily liquid nature of the Fund.
- Additionally, Lonsec notes that the Fund uses an internal Responsible Entity ('RE'), and while an external RE model is preferred, this RE relationship has been stable since the inception of the Fund and is used for other Pengana strategies.
- Lonsec notes that the Manager has disclosed in its PDS that the Fund incurred net transaction costs of 0.13% under the RG97 reporting regime. Hence, Lonsec considers this aspect to have room for improvement.
- The current size of the Fund is \$16m (March 2023), and while Lonsec acknowledges the strategy is still relatively nascent and building FUM traction, there is an elevated level of wind-up risk until the strategy achieves scale.

Performance

- The Fund aims to outperform the the S&P/ASX 300 A-REIT (AUD) TR Index ('the Benchmark') by 2% p.a. (after fees) over rolling three-year periods. Lonsec notes the Fund was inception in March 2020.
- Over the three-year period to 31 March 2023 (all figures net of fees), the Fund delivered a return of

10.3% p.a., underperforming the Benchmark by -3.9% p.a., and below the 14.4% p.a. peer median return. As such, the Fund has failed to deliver on its performance objective.

- Over the one-year period to 31 March 2023 (all figures net of fees), the Fund returned -16%, underperforming the Benchmark by -1.9%, and worse than the -13.2% peer median return. Top contributors to performance included overweight positions in Lifestyle Communities, Qualitas and Peet (all non-index), and underweight positions in Shopping Centres Australasia and Goodman Group. Top detractors were overweight positions in Centuria Capital, Arena and Charter Hall, an underweight position in Vicinity Centres, and a non-index position in Healthco.
- From a risk perspective, the Fund has exhibited volatility (as expressed in standard deviation of returns) slightly above the peer median over all assessed time periods. However, the Fund's Sharpe Ratio and worst drawdown figures are inferior to the peer group median.

Overall

- Lonsec has maintained the Fund's rating of 'Investment Grade' at this review. The investment team is led by two experienced property securities investors with a history of working together and supported by an analyst with direct property experience. The high conviction portfolio is differentiated from peers by holding a higher proportion of off-benchmark stocks. The strategy has an ample runway from a capacity perspective.
- However, the Fund has a relatively short track record and to date has underperformed both the Benchmark and peer group median. Unlike some more highly rated A-REIT managers, the investment team does not have access to a direct commercial property business in the Manager's wider business. Finally, while the Manager is gaining FUM traction, the A-REIT strategy is still sub-scale and thus poses some wind-up risks.

People and Resources

Corporate overview

- Pengana Capital Ltd ('PCL') is the Responsible Entity and investment manager of the Fund. PCL is a subsidiary of Pengana Capital Group, a boutique investment manager established in February 2003 which is listed on the Australian Stock Exchange (ASX Code: PCG) with a market capitalisation of \$141m as at March 2023. The Directors and staff own approximately 45% of the business.
- In June 2017, Pengana Holdings Ltd merged with Hunter Hall International to form Pengana Capital Group.
- In January 2020, Pengana acquired 67% of Lizard Investors LLC, a Chicago-based asset management firm that specialises in small to mid-capitalisation equities.

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

Size and experience

NAME	POSITION	EXPERIENCE
		INDUSTRY / FIRM
AMY PHAM	PORTFOLIO MANAGER	27 / 3
JADE ONG	INVESTMENT SPECIALIST	19 / 3
SAM CRAIG	INVESTMENT ANALYST	7 / 1

The Pengana A-REIT team comprises three people, with the oversight provided by the Chief Investment Officer and Investment Committee. The size of the team is typical for managers of Australian property securities funds.

Amy Pham (Fund Manager) joined Pengana in February 2020 and established this A-REIT strategy. Pham has 27 years of experience as an analyst and portfolio manager in Australian property securities investment. Pham spent six years at Charter Hall Maxim (previously Folkestone Maxim) as an Analyst/Portfolio Manager, responsible for a high conviction A-REIT mandate. This team won several industry awards. Pham has also held senior positions including Head of Property Securities at IAG; Portfolio Manager at Deutsche Asset Management; and Portfolio Manager at Perpetual Funds Management. She began her career as a quantitative analyst at Legal and General. Pham holds a Bachelor and Honours degree in Economics from the University of New England and University of California Davis.

Jade Ong (Investment Specialist) has 19 years of experience in property funds management and corporate finance. Prior to joining Pengana in June 2020, Ong was a senior member of Macquarie Capital's real estate corporate advisory team in London and Sydney for nine years. During this time Ong worked closely with A-REIT clients advising on mergers and acquisitions, direct asset sales and private capital transactions. Ong was also an Assistant Portfolio Manager of IAG's property securities fund, working alongside Pham. Ong holds Bachelor of Laws and Bachelor of Commerce degrees, graduating with honours from the University of Sydney.

Sam Craig (Investment Analyst) has seven years of experience in property and investment markets. Prior to joining Pengana in December 2021, Sam worked in the research team at Charter Hall and was responsible for cross-sector quantitative and thematic research, transaction and funds management support, as well as performance reporting for Charter Hall's largest investors. Sam holds undergraduate degrees in Finance and Law from the University of Adelaide. He is also a Chartered Financial Analyst charterholder.

comprising another 20. The Fund's mandate includes investment in A-REITs, Real Estate Developers, Fund Managers and other property-related businesses as well as global listed REITs (although there are none of the latter in the current portfolio).

Research inputs

- Company financial reports
- Meetings with company / ESG Questionnaire
- Property inspections
- Broker research
- Macroeconomic inputs
- Direct real estate research and industry contacts

Valuation approach

The Manager's value model uses the following Quantitative factors (50% of the total) to assess the relative value of each security:

- Forecast dividend yield
- Earnings growth
- Five year Price/Net Present Value (NPV)
- Weighted Average Lease Expiry
- Gearing (Loan-to-Value Ratio; Interest Cover Ratio)
- Price to Net Tangible Value (NTAV); or Net Asset Value (NAV)

The other 50% comprises Qualitative research factors, split between the ranking of the quality of Management/ Assets (20%) and the ranking of ESG factors (30%).

These factors are combined in a Valuation Ranking Model to enable the selection of the most attractive stocks for the portfolio compared to current pricing.

The primary focus of the valuation process related to the company's ability to generate sustainable free cashflow and a strong balance to support future growth.

Pengana's ESG assessment focus is the highest proportion of the A-REIT managers' valuation model to provide a comprehensive view of the risk/return characteristics of the opportunities for investment.

The majority of the team's valuation effort is produced internally, having developed proprietary models for 41 of the 50 stock Australian investable universe, with a further three models for overseas stocks. Domestic stocks not currently modelled have clearly identified higher quality peers. Key drivers of these models are now all assessed in-house.

Pengana has a focus on Alternative property sectors and hence the internal modelling effort is on small to mid-cap stocks not well covered by brokers and large institutions.

Research Approach

Overview

KEY SCREENS	GOOD CORPORATE GOVERNANCE
STOCKS IN UNIVERSE	A-REIT 300; NON-INDEX AUST. AND INTERNATIONAL
NO. STOCKS FULLY MODELLED / RESEARCHED	50
BOTTOM UP	80-85%
TOP DOWN	15-20%

Universe

The main targets for investment are the 30 stocks in the S&P/ASX 300 A-REIT Index, with non-index local stocks

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

ISSUE DATE 30-05-2023

Portfolio Construction

Overview

BENCHMARK	S&P/ASX A-REIT 300 TR INDEX
RETURN OBJECTIVE (INTERNAL)	BENCHMARK + 2% P.A. (NET OF FEES) OVER THREE-YEAR PERIODS
RISK OBJECTIVE (INTERNAL)	N/A
INVESTMENT STYLE	QUALITY
PORTFOLIO APPROACH	BENCHMARK UNAWARE
PORTFOLIO DECISIONS	PORTFOLIO MANAGER
TYPICAL NO. OF HOLDINGS	10-20
MARKET CAPITALISATION BIAS	MID-CAP
EXPECTED PORTFOLIO TURNOVER	40-50% P.A.
% OF PORTFOLIO IN TOP 10 HOLDINGS	75% (APRIL 2023)
OBSERVED ACTIVE SHARED	51% (APRIL 2023)

Portfolio construction is based on the outcome of the above Valuation Model Ranking, assessed on a risk/reward basis. It involves a macro/top-down overlay for the construction of the portfolio. Pengana focuses on diversifying into growth sectors driven by secular trends (such as childcare; seniors living; healthcare; data centres; transport; and agriculture). The Manager believes these property sectors will provide defensive sustainable growth and diversification away from core real estate sectors (i.e. office, retail; industrial).

Guidelines for portfolio construction:

- Minimum market capitalisation of each stock \$50m;
- Create a diversified portfolio of eligible securities (10-20 long positions);
- Individual stock positions are sized on the level of conviction, relative risk/reward profiles and market liquidity;
- Single security exposure for index stocks (0-20%), although where a security has a weighting of >20% in index, the maximum weighting is index weight;
- Single security exposure for non-index stocks (A-REITs outside the S&P/ASX A-REIT 300) 2-5%;
- Avoid over concentration of single factor risk;
- Constantly subjected to Pengana's A-REIT investment philosophy, process and buy/sell decisions;
- Ideas tested against existing holdings.

Buy Decisions:

- Based on fundamental quality first, then valuation;
- Non fundamental factors (eg: appetite for risk, M&A, other);
- Risk/reward assessment, no matter how compelling.

Sell Decisions:

- If either Qualitative or Valuation criteria are compromised or misjudged;
- Stocks assessed as fully-valued with better risk/reward opportunities elsewhere in the universe.

Risk Management

Risk limits

SEPARATE RISK MONITORING	YES
STOCK (INDEX) LIMIT	<20% HOLDING WITHIN THE PORTFOLIO OR EQUAL TO INDEX WEIGHT IF >20%
STOCK (NON-INDEX) LIMIT	2-5% HOLDING WITHIN THE PORTFOLIO
REGION / SECTOR LIMITS	<10% GLOBAL REITS AND REAL ESTATE-RELATED STOCKS
CASH LIMIT	MAXIMUM 20% (LONG-TERM AVERAGE 0-5%)

The portfolio construction process relies on a number of broad built-in 'hard' risk limits providing a framework for stock positioning, allocations outside of the Index or to cash, and liquidity.

Risk monitoring

The Manager has strong risk tools in place and portfolio risk is actively reviewed by a separate team to ensure compliance with investment policies and guidelines.

Risks

An investment in the Fund carries a number of standard investment risks associated with investment markets. These include performance, liquidity, counterparty, market and tax risk. These and other risks are outlined in the PDS and should be read in full and understood by potential investors. Lonsec considers the following to be the major risk:

Market Risk

Investments in equity markets are subject to numerous factors which may have an impact on the performance of an investment (both positive and negative). Unexpected changes in economic, technological, structural, regulatory or political conditions can have an impact on the returns of all investments within a particular market.

Investment Risk

From time to time, there may be falls in the value of the Fund's investments due to specific factors including changes to management, product distribution, investor confidence, internal operations or the company's business environment

Currency risk

Should the Fund invest in international REITs, there will be an element of foreign currency risk in the portfolio against the Australian dollar. Currently there are no overseas holdings.

ANALYST: BALRAJ SOKHI | APPROVED BY: PETER GREEN

Pengana High Conviction Property Securities Fund

Quantitative Performance Analysis - annualised after-fee % returns (at 31-3-2023)

Performance metrics

	1 YR		2 YR		3 YR		5 YR	
	FUND	PEER MEDIAN	FUND	PEER MEDIAN	FUND	PEER MEDIAN	FUND	PEER MEDIAN
PERFORMANCE (% PA)	-15.95	-13.20	0.14	0.82	10.27	14.38	-	-
STANDARD DEVIATION (% PA)	29.22	26.74	23.53	21.51	21.07	21.78	-	-
EXCESS RETURN (% PA)	-1.93	0.74	-1.08	-0.40	-3.93	0.33	-	-
OUTPERFORMANCE RATIO (% PA)	50.00	50.00	50.00	45.83	47.22	50.00	-	-
WORST DRAWDOWN (%)	-24.30	-23.06	-31.36	-27.61	-31.36	-27.61	-	-
TIME TO RECOVERY (MTHS)	NR	NR	NR	NR	NR	NR	-	-
SHARPE RATIO	-0.62	-0.59	-0.04	-0.01	0.45	0.61	-	-
INFORMATION RATIO	-0.71	0.23	-0.27	-0.27	-0.58	0.11	-	-
TRACKING ERROR (% PA)	2.73	2.73	3.94	3.06	6.81	3.97	-	-

PRODUCT: PENGANA HIGH CONVICTION PROPERTY SECURITIES FUND

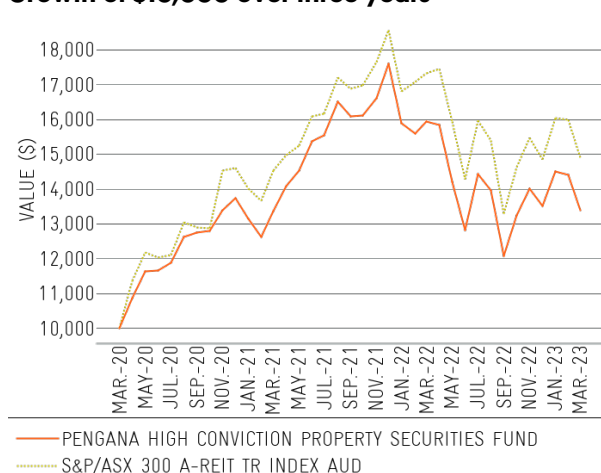
LONSEC PEER GROUP: PROPERTY AND INFRASTRUCTURE - AUSTRALIAN LISTED PROPERTY

PRODUCT BENCHMARK: S&P/ASX 300 A-REIT TR INDEX AUD

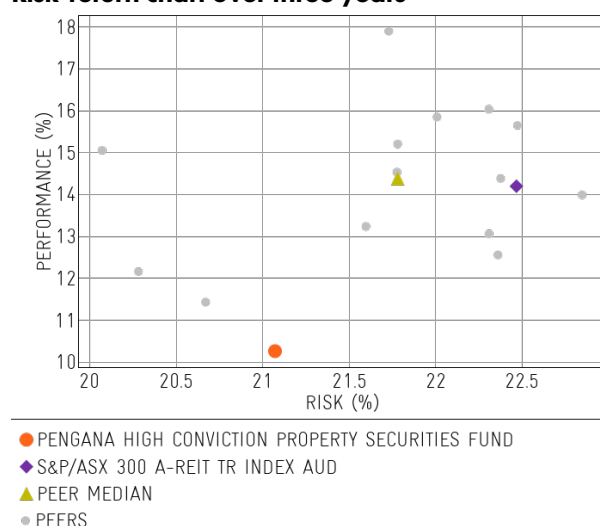
CASH BENCHMARK: BLOOMBERG AUSBOND BANK BILL INDEX AUD

TIME TO RECOVERY: NR - NOT RECOVERED, DASH - NO DRAWDOWN DURING PERIOD

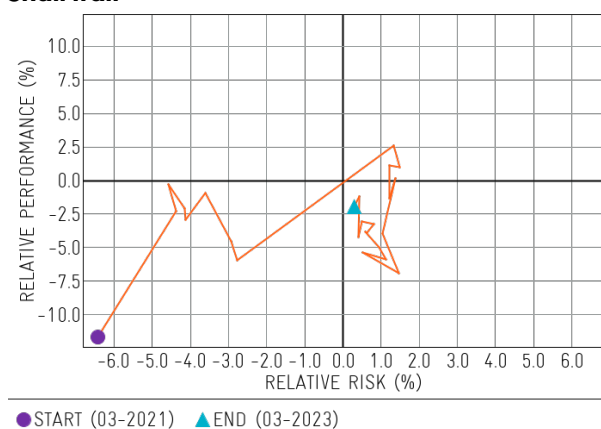
Growth of \$10,000 over three years



Risk-return chart over three years



Snail trail



Outperformance consistency



Pengana High Conviction Property Securities Fund

Glossary

Total return 'Top line' actual return, after fees
Excess return Return in excess of the benchmark return
Standard deviation Volatility of monthly Absolute Returns
Tracking error Volatility of monthly Excess Returns against the benchmark (the Standard Deviation of monthly Excess Returns)
Sharpe ratio Absolute reward for absolute risk taken (outperformance of the risk free return (Bank Bills) / Standard Deviation)
Information ratio Relative reward for relative risk taken (Excess Returns / Tracking Error)
Worst drawdown The worst cumulative loss ('peak to trough') experienced over the period assessed
Time to recovery The number of months taken to recover the Worst Drawdown
Snail Trail A trailing 12-month relative performance and relative risk measurement over the benchmark. The trail is generated using a 12-month rolling window over the specified period

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