



L1 CAPITAL

# L1 Long Short Fund Limited

Monthly Report | JULY 2022

- The L1 Long Short Fund (LSF) portfolio returned -3.3%<sup>1</sup> in July (ASX200AI 5.7%).
- The portfolio has returned 21.0%<sup>1</sup> p.a. over the past 3 years (ASX200AI 4.3% p.a.).
- Global markets rallied in July primarily due to a surge in 'expensive defensives' and speculative technology stocks. We continue to believe these parts of the market are overvalued and risky and remain comfortable not holding these stocks.

Equities rallied in July, largely due to a fall in global bond yields. Rising recession concerns led to a reduction in medium-term interest rate expectations, with the market anticipating that the Fed would have to pivot earlier than previously expected.

Portfolio performance over the past two months has been disappointing, however we are consoled by the fact that this portfolio positioning has helped us deliver strong returns in recent years. The portfolio has returned 21.0% p.a. over the past three years compared to 4.3% for the ASX200 Accumulation Index. Our approach is to stay focused on the outlook for companies and industries over the next two to three years and to accept that share prices can be detached from fundamentals in the short term. This volatility provides opportunities for us to adjust our exposure and to benefit from erratic short term share price moves.

At present, investors have crowded into defensives, which ironically, has made those stocks risky (and expensive). We see numerous outstanding opportunities in cyclical companies that are now pricing in a severe economic downturn. We have used this sell-off to add to several of our highest conviction positions, including BlueScope, Capstone, MEG, Cenovus and Qantas (which were outlined in detail in our [June Quarterly Report](#)).

We believe copper and oil stocks are particularly oversold. Despite a 30-40% share price fall in our offshore copper positions over the past two months, expectations for the price of copper over the next three years have barely changed. The sell-off is not consistent with the prevailing market tightness and the strong demand growth we expect as the energy transition gains momentum.

Similarly, oil prices have fallen ~14% over the past two months, despite the oil market remaining physically tight. Our oil stocks have declined more severely than that and are now trading on 20-30% free cash flow yields and implying a US\$60-\$70 per barrel long-term oil price, compared to spot prices of ~US\$95 per barrel.

Returns (Net) <sup>1</sup> (%)	L1 Long Short Portfolio	S&P ASX 200 AI	Out-performance
1 month	(3.3)	5.7	(9.1)
3 months	(16.4)	(6.0)	(10.3)
6 months	(6.3)	1.7	(8.0)
1 year	4.3	(2.2)	+6.4
2 years p.a.	36.6	12.1	+24.4
3 years p.a.	21.0	4.3	+16.8
LSF Since Inception p.a.	9.9	7.8	+2.1
Strategy Since Inception <sup>2</sup> p.a.	20.0	6.9	+13.1

We typically take a 2-year view, not a 2-month view, and remain confident that the fundamentals of our stocks remain firmly intact. We also remain comfortable having less exposure to high P/E stocks, which are still trading at a ~45% premium to their 20-year average, while low P/E stocks are trading at a ~15% discount to their 20-year average.

**While the market remains volatile and our performance has experienced some short-term headwinds, we remain confident that we are in a stock pickers' market and that our stock selection and flexible portfolio design will drive performance over the medium term.**

Key contributors to portfolio performance during the month of July were:

**Safran (Long +14%)** shares rose following a strong first half result and ~20% increase to full year free cash flow guidance. This is an exceptional result considering the headwinds impacting the company, including supply chain disruptions, cost inflation and COVID-19 restrictions in key markets such as China. In our view, Safran is the highest quality aerospace business globally, given it controls 60% market share of all jet engine sales for narrow-body aeroplanes and it has the most reliable and youngest engine fleet, which provides incredible predictability and visibility regarding its long term earnings outlook (from parts and maintenance of those engines).

1. All performance numbers are quoted net of fees. Net returns are calculated based on the movement of the underlying investment portfolio. Figures may not sum exactly due to rounding. Past performance should not be taken as an indicator of future performance. 2. Strategy performance and exposure history is for the L1 Long Short Fund Limited (ASX:LSF) since inception on 24 Apr 2018. Prior to this date, data is that of the L1 Capital Long Short Fund – Monthly Class since inception (1 Sep 2014). NOTE: Fund returns and Australian indices are shown in A\$. Returns of U.S. indices are shown in US\$.



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Safran remains well positioned to drive earnings growth going forward through its cost out program, which supports ~200bps in margin expansion and a continued recovery in global air travel as key markets such as China re-open. Furthermore, Safran has a robust balance sheet with flexibility to pursue capital management initiatives to drive additional shareholder returns. We believe the company is significantly undervalued, with ~50% upside if the shares simply recover to pre-COVID-19 levels.

**St Barbara (Long +50%)** shares rallied in July following strong Q4 FY22 results which included positive cashflow generation and solid mining production. St Barbara's flagship Gwalia mine is well-positioned to improve performance after a period of reinvestment and repositioning with further scale efficiencies achievable through its expanded mill. Similarly, its Simberi mine has resolved former operational issues and is now well-placed for a potential sale, which would both reduce group capex requirements and provide an incremental cash injection. We believe there are several catalysts that could unlock value at St Barbara over the next 12 months, including a streamlining of its asset base, consolidation of the Leonora gold district and improved operational execution across its key mine sites. The company is one of the cheapest gold names globally on a price per ounce of resources and reserves basis with significant upside potential.

Key detractors to portfolio performance during the month of July were:

**Alibaba Group (Long -21%)** shares fell in July as investor sentiment weakened regarding China's economic recovery. We believe Alibaba's earnings are likely to have bottomed in Q2 and should see a gradual recovery as China's retail spend improves post the harsh lockdowns in the prior quarter. Alibaba remains a high-quality business with sustainable leading positions in both e-Commerce and Public Cloud. We believe structural growth in these areas, supported by a broader economic recovery in 2023 and the exit of smaller unprofitable competitors in some of Alibaba's key markets (e.g. online grocery) will support earnings growth going forward.

**F45 (Long -50%)** shares fell sharply following a substantial earnings downgrade and the resignation of their CEO. Tighter financing conditions in the U.S. have reduced the ability of franchisees to open new gyms in the last few months.

**Capstone Copper (Long -11%)** shares fell over the month as copper prices continued to remain under pressure. The market is concerned about a reduction in copper demand from a potential U.S. recession as well as growth in new supply from several new copper projects and expansions to be delivered in 2022 and 2023. We believe these concerns are overdone and there will be a major copper supply shortfall in the medium to longer term, as the copper-intensive global energy transition gains momentum.

Capstone is a fast-growing copper mining company focussed in the Americas with four producing mines, one undergoing a major expansion (with capex largely fixed under a lump sum contract) and one awaiting final investment decision. The company currently has no net debt and is well funded to complete the currently approved project pipeline (even in a more adverse copper price environment). We expect Capstone to double production over the medium term with the commencement and ramp-up of the Santo Domingo copper and cobalt project. The company has a capable management team that has emphasised long-life projects as well as low-cost expansion opportunities. Capstone is currently trading on less than 4x consensus FY24 P/E, when the projects currently under construction will be in full production.



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## Strategy Returns (Net)<sup>3</sup> (%)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
<b>2014</b>	-	-	-	-	-	-	-	-	(2.42)	3.03	2.85	1.61	<b>5.17</b>
<b>2015</b>	0.59	9.14	2.42	1.71	3.73	(0.86)	3.30	2.06	5.51	8.49	8.11	4.62	<b>60.52</b>
<b>2016</b>	5.81	0.59	5.47	2.46	2.78	(0.89)	3.22	3.92	0.46	(0.13)	0.55	2.22	<b>29.61</b>
<b>2017</b>	2.51	1.87	3.15	1.03	4.18	1.70	2.62	1.69	1.93	2.54	0.89	3.56	<b>31.40</b>
<b>2018</b>	0.56	(0.47)	(1.64)	(1.32) <sup>3</sup>	(4.05)	(5.96)	1.01	(5.34)	(2.06)	(3.90)	(2.60)	(5.95)	<b>(27.74)</b>
<b>2019</b>	4.26	5.11	0.16	3.05	(2.73)	3.87	0.63	0.40	2.54	3.46	0.36	2.06	<b>25.46</b>
<b>2020</b>	(7.75)	(6.85)	(22.93)	23.16	10.94	(2.12)	(1.69)	9.99	0.63	(2.37)	31.94	4.29	<b>29.50</b>
<b>2021</b>	(0.17)	9.00	(0.14)	5.11	4.07	(0.52)	1.75	5.10	4.86	2.32	(7.36)	3.66	<b>30.29</b>
<b>2022</b>	2.79	6.87	1.34	3.44	0.06	(13.39)	(3.34)						<b>(3.70)</b>

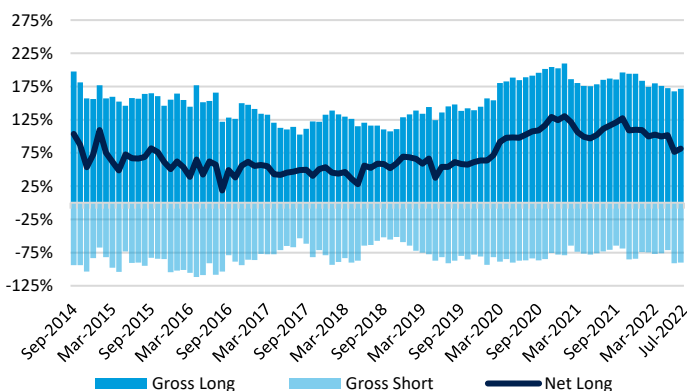
## Portfolio Positions

Number of total positions	79
Number of long positions	59
Number of short positions	20
Number of international positions	28

## Net & Gross Exposure by Region<sup>3</sup> (%)

Geography	Gross Long	Gross Short	Net Exposure
Australia/NZ	106	74	32
North America	38	15	23
Europe	22	0	22
Asia	4	0	4
<b>Total</b>	<b>170</b>	<b>89</b>	<b>81</b>

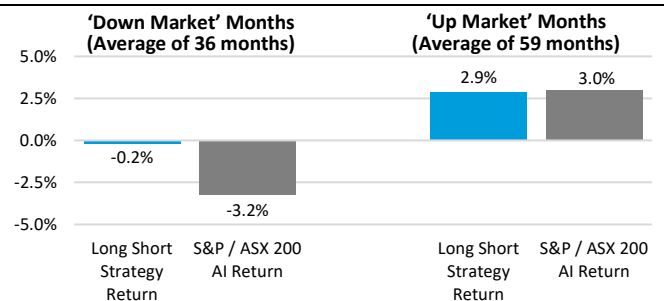
## Historical Strategy Exposures<sup>3</sup>



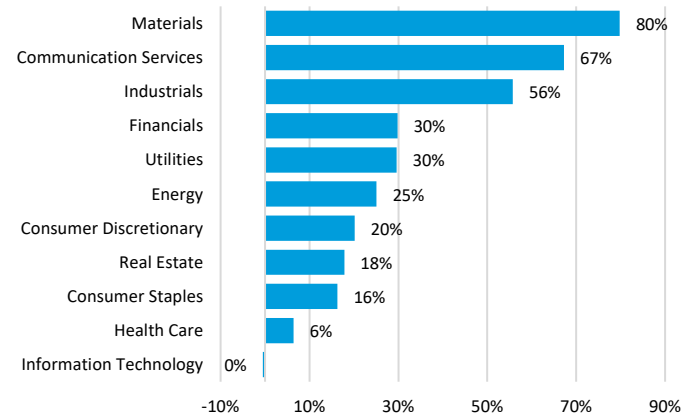
## Company information as at 31 July 2022<sup>4</sup>

Share Price	\$2.52
NTA before tax	\$2.6123
NTA after tax	\$2.6887
Shares on issue	611,62,437
Company market cap	\$1.54b

## Strategy Performance Since Inception<sup>3</sup> (Net)



## Sector Contribution Since Strategy Inception<sup>3</sup> (Net)



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## Key personnel

<b>Andrew Larke</b>	Independent Chair
<b>John Macfarlane</b>	Independent Director
<b>Harry Kingsley</b>	Independent Director
<b>Raphael Lamm</b>	Non-Independent Director
<b>Mark Landau</b>	Non-Independent Director
<b>Mark Licciardo</b>	Company Secretary
<b>Registry</b>	Link Market Services Limited
<b>Company website</b>	<a href="http://www.L1LongShort.com">www.L1LongShort.com</a>
<b>LinkedIn</b>	Follow us on 

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## Company Information – LSF

<b>Name</b>	L1 Long Short Fund Limited
<b>Structure</b>	Australian Listed Investment Company (ASX:LSF)
<b>Inception</b>	24 April 2018
<b>Management Fee</b>	1.44% p.a. inclusive of GST and RITC
<b>Performance Fee</b>	20.0%
<b>High Watermark</b>	Yes

## L1 Capital (Investment Manager) Overview

L1 Capital is a global investment manager with offices in Melbourne, Sydney, Miami and London. The business was established in 2007 and is owned by its senior staff, led by founders Raphael Lamm and Mark Landau. The team is committed to offering clients best of breed investment products through strategies that include long short Australian equities, international equities, activist equities, a global multi-strategy hedge fund and U.K. residential property. The firm has built a reputation for investment excellence, with all L1 Capital's strategies delivering strong returns since inception. The team remains dedicated to delivering on that strong reputation through providing market-leading performance via differentiated investment approaches with outstanding client service, transparency and integrity. L1 Capital's clients include large superannuation funds, pension funds, asset consultants, financial planning groups, family offices, high net worth individuals and retail investors.



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### Information contained in this publication

L1 Long Short Fund Limited, managed by L1 Capital Pty Ltd, has been established to invest in a portfolio of predominantly Australian and New Zealand securities, with up to 30% invested in global securities. The Company has the ability to both buy and short-sell securities, which provides a flexible strategy to deal with changing stock market conditions. The objective is to deliver strong, positive, risk-adjusted returns to investors over the long term.

### Disclaimer

This communication has been prepared for L1 Long Short Fund Limited (ACN 623 418 539) by its investment manager, L1 Capital Pty Ltd (ABN 21 125 378 145 and AFS Licence 314302). L1 Capital Pty Ltd has prepared this publication in good faith in relation to the facts known to it at the time of preparation. This publication contains general financial product advice only. In preparing this information, we did not consider the investment objectives, financial situation or particular needs of any individual investor, and you should not rely on the opinions, advice, recommendations and other information contained in this publication alone. This publication has been prepared to provide you with general information only. It is not intended to take the place of professional advice and you should not take action on specific issues in reliance on this information. We do not express any view about the accuracy or completeness of information that is not prepared by us and no liability is accepted for any errors it may contain. Past performance is not a reliable indicator of future performance.

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