L1 CAPITAL

L1 Long Short Fund Limited

Investor Letter | DECEMBER 2020

The Company's NTA increased 34.4% for the quarter (ASX200AI +13.7%) and 29.5% for the 2020 calendar year (ASX200AI 1.4%)[1].

The Company had its best quarter and year on record driven by strong stock picking across a wide range of sectors. Returns were further supported by the positive vaccine announcements in November.

The vaccine results from Pfizer, Moderna and AstraZeneca were exceptionally strong, indicating high efficacy and safety levels from Phase 3 trial data. We believe the vaccine news and roll-out will trigger an enduring rotation into value and cyclical stocks (which lagged the market dramatically in 2020). This should be a major positive tailwind for performance in 2021 and beyond.

2020 in Review

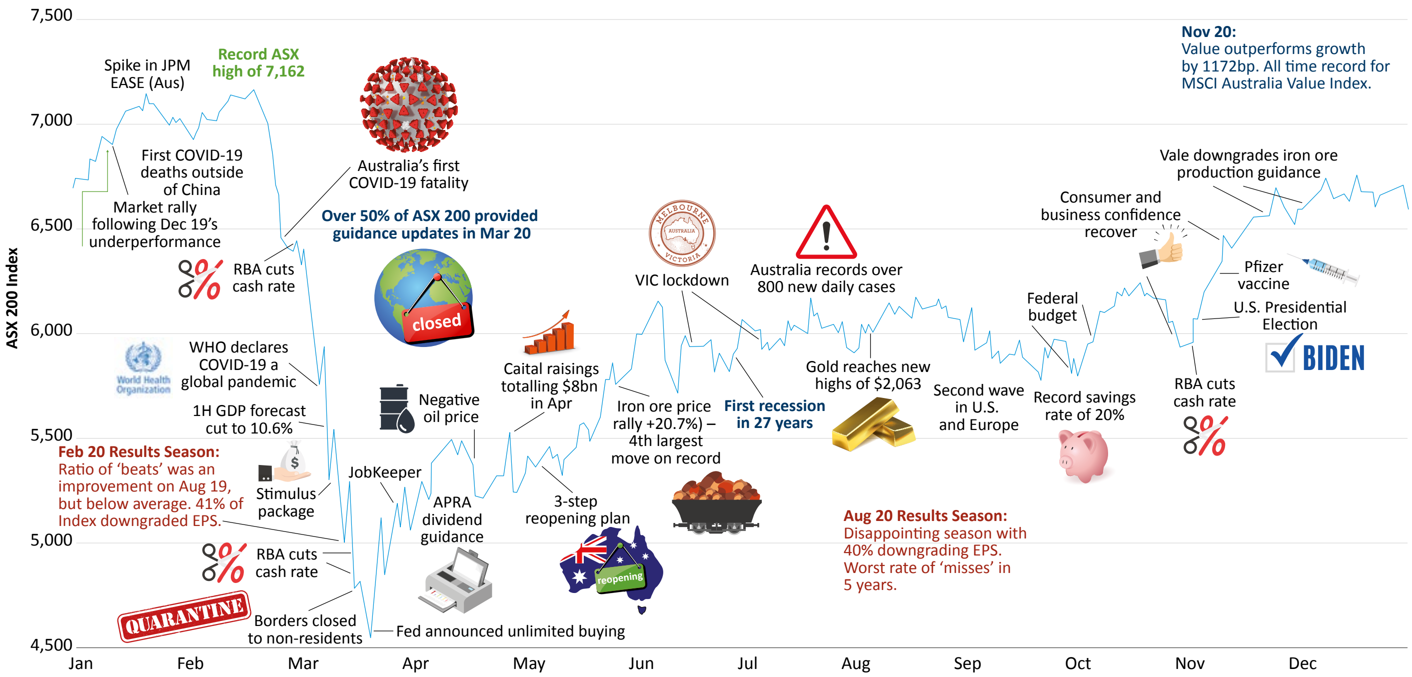
As we turn the corner on what has been one of most volatile years of our investment careers, we have been reflecting on our positioning throughout the year, the key decisions we made and the outcomes for our investors.

First, we would like to sincerely thank our investors and advisors who have supported us through this extraordinary year. We could not be more pleased that your consistent faith in us has been rewarded with such strong performance. Our investment team worked incredibly hard this year to navigate the crisis, identify the best opportunities and assess the timing and likelihood of vaccine success. 2020 represents the second consecutive calendar year where the portfolio has delivered net returns above 25%.

2020 was certainly "unprecedented" in many respects, with market volatility at extreme levels as we dealt with a prolonged period of elevated risks from the COVID-19 pandemic, global trade wars, Brexit, U.S. election uncertainty and more (Figure 1 below provides a pictorial representation of some of these key events). While the ASX 200 ended the year broadly flat versus the prior period, this has masked the extraordinary level of volatility we have seen during the year. The ASX 200 had more +/– 3% days in 2020 (22) than the previous 11 years combined (and the most recent year exceeding 2020 was during the GFC in 2008 at 40 times).

We have also seen both the fastest bear market and the fastest bull market recovery in history play out over the past 9 months. The market sold-off sharply as economies were closed down globally in March due to COVID-19 and rebounded strongly thereafter as governments and central banks unleashed a torrent of fiscal and monetary support, lockdowns eased and confidence in the development of effective vaccines increased. As a comparison, the GFC took nearly 24 months to reflect a similar downturn and subsequent recovery.

Figure 1 – 2020 Pictorial Review



Source: JP Morgan, Bloomberg Finance LP, Shutterstock as at 31 Dec 2020

1 *The Company is L1 Long Short Fund Limited. Net performance is calculated using the movement in NTA pre-tax. Performance is shown net of all applicable fees and charges. Past performance should not be taken as an indicator of future performance.*

Given the extraordinary challenges posed by the pandemic, as well as the extreme headwind to our investment style (with value and cyclicals continuing to remain out of favour) we are very pleased that our rigorous research on both company specific stock selection and the COVID-19 pandemic have been able to produce robust returns for our investors. Moreover, this result reinforces our optimism that despite the enduring uncertainty that we expect in 2021, we will continue to be able to identify high quality companies that are significantly undervalued and misunderstood by the market.

We started 2020 off with a bias to cyclical stocks as we believed cyclicals had highly compelling valuations and leading indicators for global growth were starting to inflect positively (given an improving macroeconomic environment, rising bond yields, supportive ISM/PMI data, rising oil and copper prices, etc.). In the early stages of the COVID-19 pandemic in January, we reduced some of our cyclical exposure by exiting positions in Energy and Travel-related names and adding a few short positions linked to China and the Travel sector. The changes we made were helpful but insufficient to protect the portfolio during the aggressive March sell-off. In hindsight, we made the mistake of thinking the COVID-19 pandemic would be largely confined to Asia (similar to MERS/SARS) rather than a truly global pandemic (similar to the Spanish Flu of 1918). This had a detrimental impact on our performance in the first quarter.

Once we better understood the magnitude of the COVID-19 impact, we quickly pivoted our thinking to take advantage of the crisis and make the most of what we saw as a “once in a decade” investment opportunity. The pandemic had resulted in an extreme sell-off that had made valuations the most attractive we had seen since the depths of the GFC. The investment team made an enormous effort to identify the best opportunities available through this sell-off and we began aggressively buying these stocks from mid to late March onwards, during the height of investor panic. Looking back, these decisions were instrumental in driving the strong portfolio performance we have seen since March 2020 and can be distilled to four key factors:

1. **Buying (or adding to) numerous oversold stocks close to the market lows.**

   Based on our detailed research process, we either bought or added to stocks across a wide range of sectors from March 2020 onwards at very attractive levels. Some of the key stocks we invested in are further outlined below:

   - Large Caps: Transurban, Qantas, Tabcorp, Oil Search, Downer, Scentre Group, Star Entertainment, Unibail-Rodamco-Westfield, Safran and SES.
   - Small Caps: Lovisa, Webjet, Hotel Property Investments, ALS, Karoon, Eclipx, Perenti, Empire State Realty Trust and Bed Bath & Beyond.

   All of these positions have had very large rallies since we invested.

2. **Increasing our net long by more than 35% (from 72% at the end of Feb to an average of 108% since then).**

   At a time when many investors were liquidating their shares due to COVID-19 fears (or margin calls/redemptions), we took advantage of these buying opportunities, increasing our net long exposure to the highest level in the history of the Long Short Strategy. We continue to believe equities look very attractive as we head into 2021, especially compared to bonds, cash and property.

3. **Exiting many short positions after the share prices collapsed in March.**

   We closed 10 short positions near the market lows in March (34 shorts in February versus 24 by April) and shifted a greater proportion of our short book to index short positions.

4. **Strong stock picking within sectors.**

   We had numerous examples of selecting a top performing stock within a given sector e.g. Chorus in Telcos, Transurban in Infrastructure (since exited), Nine Entertainment in Media, Lovisa in Retail, Mineral Resources in Mining, West African Resources in Gold, Hotel Property Investments in Property, Star Entertainment and Eagers Automotive in Consumer Discretionary.

Equity Market Outlook

From a market outlook perspective, we continue to believe the market environment is one of the best we have seen in many years, with numerous exciting stock specific opportunities.

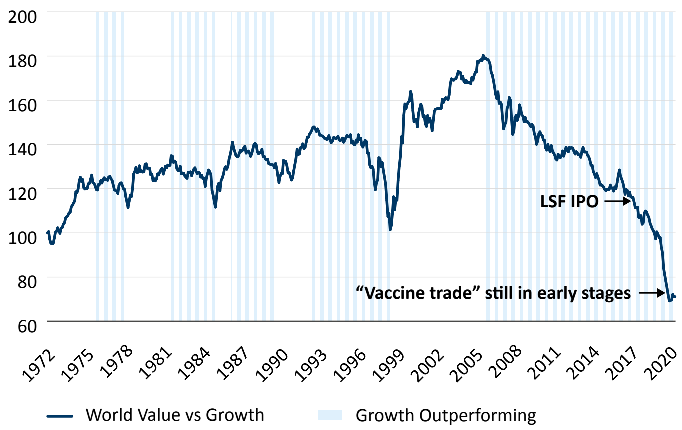
Equities continue to look far more attractive than other asset classes. Cash and most investment grade bonds globally now yield less than inflation, suggesting continued scope for a rotation to equities that should gather pace as the economic outlook becomes clearer.

Based on our detailed research on the pandemic, we have high conviction that there is path back to a “normal” (pre-COVID) way of living in the second half of 2021 (refer to page 10 for further detail). We believe this gradual recovery, together with the unprecedented level of fiscal and monetary support underway will turbo-charge global growth over the next twelve months to the strongest level it has been in more than a decade.

If growth and the recovery in corporate earnings comes through stronger than expected, this will trigger a further rotation into value and cyclical stocks (given their enormous underperformance versus growth/momentum stocks as a result of COVID-19). As the economy begins to accelerate, companies with strong EPS growth will no longer be confined to the ultra-high P/E growth names, making a rotation into cyclicals more compelling. It is for this reason that we believe we have only just seen the start of the “vaccine trade”. Most institutional investors continue to be defensively positioned and cautious on the vaccine roll-out and the path to a normal, operating environment. As the recovery becomes more certain, we expect these investors to further transition their portfolios away from “COVID winners” (such as Technology, Healthcare, Iron Ore, Supermarkets and Discretionary Retail) to “COVID losers” (such as Travel, Energy, Casinos, Shopping Centres, Base Metals, Financials and Infrastructure stocks).

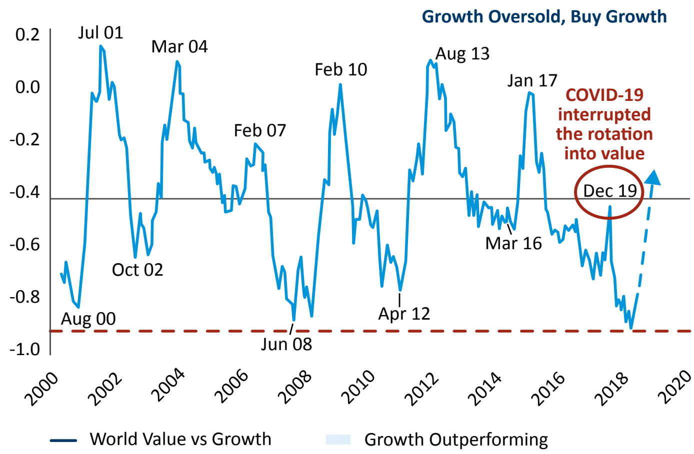
Figure 2 below shows the relative performance of growth versus value stocks over the past 50 years and highlights that the current period of underperformance by value stocks is by far the largest and longest on record. Put simply, there is no period on record that comes close to what we have experienced in recent years. The reversal that began in November 2020 on the positive vaccine news is still miniscule in the context of recent history.

Figure 2 – MSCI World Value vs. Growth performance



Source: Datastream, Goldman Sachs Global Investment Research. Relative price performance in local currency to 31 December 2020. MS basket data current as at 31 December, 2020.

Figure 3 – Momentum correlation with growth and value



Source: JP Morgan Research as at 9 December 2020.

Figure 3 outlines the correlation in performance of momentum versus growth and value. The graph illustrates how COVID-19 interrupted the rotation we had started to see and for which we had positioned the portfolio in late 2019/early 2020. As we enter a phase of economic recovery in 2021 (which typically favours the outperformance of value/cyclical stocks) we believe the set-up is very promising for a stabilisation or reversal of this trend which should likely be a significant tailwind to performance.

Another reason to be positive on equities is that we believe we are on the cusp of a major M&A cycle, which is something we have not seen since 2007 and which will further bolster market performance. We had started to see early signs of M&A accelerating in 2019, however, COVID-19 interrupted the cycle as companies abruptly moved into cash preservation mode.

We believe a number of factors have aligned to create an optimal backdrop for M&A in 2021:

- Corporate transformation/consolidation considerations have accelerated as COVID-19 has re-shaped the way many industries operate.
- Private equity investors have raised massive amounts of money that needs to be deployed.
- Debt markets remain conducive with interest rates at very low levels and covenant-lite loans on offer once again.
- Industry funds have become much larger and are taking a more direct role in takeovers.
- There is likely to be significant pent-up activity as the pandemic has resulted in some deals being delayed.

Portfolio Positioning

We remain extremely positive about the medium term outlook for the portfolio, given the unusually large number of stocks that have significant upside to valuation.

While we build our portfolio "bottom-up" from our stock research (selecting stocks that represent the best combination of value and quality), when we step back and look at the major themes and opportunity sets we see at present, they broadly fall into four buckets.

Key Themes

1) **Monopoly Real Assets** – companies such as Chorus, Atlas Arteria, Aurizon and Vinci.

   These companies look incredibly attractive at present. In general, they own monopoly or privileged assets that cannot easily be replaced or substituted. They are expected to generate dividend yields (or free cash flow yield) of at least 6-7% p.a. in coming years with continued growth in dividends beyond that. Some also offer the potential for additional capital management given they currently have under-geared balance sheets. In a world where long-term bond yields continue trading around 0-1%, we believe these stocks represent an extremely attractive alternative for investors seeking safe yield.

2) **COVID-hit Stocks** – companies such as Unibail-Rodamco-Westfield, Downer, Star Entertainment and Qantas.

   While a number of these stocks have rallied strongly over the past quarter, we see potential for further substantial gains ahead. Many of these companies continue to trade far below their pre-COVID-19 levels implying a large, permanent fall to their earnings and cashflows. We do not believe this is likely and expect many of these stocks will recover most of their losses over the next year as the COVID-19 vaccines are distributed and the economic recovery becomes more tangible.

3) **Resource-related stocks at a cyclical low point** – companies such as Teck Resources, Warrior Met Coal, Oil Search and Cenovus Energy.

   We are contrarian investors and like to buy high quality cyclical stocks at a low point in their cycle (and equally, we look to short stocks at a cyclical peak). Commodities such as oil, coking coal and to a lesser extent copper, have all reached an extreme cyclical low over the past year and share prices are now reflecting an unsustainable situation, where a large proportion of the world's production is simply not viable at current pricing.

4) **Conglomerates with high quality assets and a valuation catalyst** – companies such as CK Hutchison, News Corporation and SES.

   When investing in conglomerates we look for three main factors before investing, namely: a selection of high quality, market leading assets, a material discount to the sum of the parts valuation of these assets and most importantly an upcoming catalyst that will result in the market better reflecting this underlying value. We believe each of the stocks below has a major positive catalyst in 2021:

   - **CK Hutchison** – Recently announced sale of their strategic portfolio of 28,500 telco towers in Europe for 33x EV/EBITDA (delivering more than 40% of CK Hutchison's market cap in cash, despite those assets contributing only 4% of group earnings). We expect highly accretive buybacks (and/or higher dividends) to follow receipt of the cash proceeds.
   - **News Corporation** – Potential restructure/demerger of the digital real estate assets (e.g. REA and Move). There is enormous upside to fair value for News Corporation in a restructure or demerger scenario.
   - **SES** – The C-Band deal (whereby SES' satellite spectrum is being provided to the FCC in return for US$3.2b after-tax in payments over the next 3 years), which is equivalent to ~75% of SES' market cap. For more detail on SES, see page 9.

   Adding to our excitement about the portfolio is the extreme dispersion in stock valuations we are currently seeing. The market has been dominated by macro and thematic events over the past few years (e.g. U.S./China trade war, Brexit, COVID-19, U.S. election uncertainty, etc.) which has created larger than usual stock specific valuation anomalies. We believe the next few years should prove to be a particularly conducive environment for stock pickers with our ability to position long and short enabling us to take full advantage of the opportunity.

Key Stock Contributors for the Quarter

Lovisa (long +37%) is one of the most exciting retail stocks in Australia, having established itself as a truly global, high growth, fast-fashion business. Lovisa sells affordable jewellery to fashion-conscious young females and the pandemic caused a collapse in demand for fashion jewellery. We built our position after the shares had collapsed as a result of falling same store sales trends (down 32% when management updated the market in June), as socialising and parties were effectively banned globally due to COVID-19. Our view was that Lovisa was very well placed to survive the crisis, based on its healthy, net cash balance sheet and extremely high operating margins. We also expected the competitive landscape to dramatically improve, with Lovisa's main Australian competitor, Colette, having gone into administration and its new owners planning to close roughly 75% of their stores. In Europe, Lovisa recently bought out a major competitor (Beeline GmbH) and effectively paid nothing for the business (consideration was a mere €70). Lovisa is also fortunate to have Brett Blundy, arguably Australia's best retailer, as its chair and 40% shareholder, along with the Founder and highly-regarded CEO, Shane Fallscheer, who is also a 3.8% shareholder. We believe Lovisa has the potential to become a major global fashion brand, like H&M or Zara, driven by its strong customer loyalty, attractive margins, high returns on capital and a relatively weak set of competitors.

Qantas (long +20%) shares rose with the positive vaccine news in November, as well as a re-opening of state borders in much of Australia. We believe Qantas is exceptionally well positioned as the world emerges from the worst aviation crisis ever. The company is set to enjoy a rapid recovery in earnings in FY22 due to huge pent up leisure travel demand, improved market share (given Virgin's new strategy of operating a smaller, more profit-focused network) and an improved cost base (facilitated by its $1b cost out program over the next 3 years). We participated in Qantas' capital raise back in June at $3.65/share and continued increasing our position subsequently (today's share price is around $4.80). We have long viewed Qantas as one of the world's highest quality airlines, with its dominant industry position, high-growth loyalty (frequent flyer) division and outstanding management team.

Webjet (long +30%) shares rallied strongly with the potential for a solid uplift in domestic and international travel in 2021. Webjet operates through two segments: (i) the B2C OTA (Online Travel Agency) division, where webjet.com.au is the leading online travel booking portal in Australia and New Zealand, and (ii) the B2B hotels division, which is the second largest and the fastest growing "bed bank" operator globally. Bed banks act as online intermediaries between hotels that are looking to fill hotel rooms and travel providers that are looking to source rooms for end consumers. Webjet has been impacted significantly by the pandemic, which reduced its revenue to close to zero and caused a material working capital unwind as customers had to be refunded up-front, at the same time as supplier receipts were delayed and, in certain cases, became unrecoverable due to many smaller travel agents going out of business. We participated in the recapitalisation of the company at ~$1.70/share in April during the peak of the crisis (today's share price is around $5.00). We continued increasing our stake after the raise as we were confident Webjet would emerge from the pandemic as a better business with a stronger industry position. Webjet now has one of the most robust balance sheets in the industry, has cut its operating costs significantly and is better positioned with many of its competitors having either closed or scaled back operations materially. Webjet is led by a high quality, experienced and passionate management team and we believe the company is well placed to deliver strong earnings growth as pent up demand for leisure travel becomes evident over the next 1-2 years.

Oil Search (long +40%) shares rose strongly over the period driven by an ~18% increase in crude oil prices and a broader rotation to energy stocks (energy was the best performing sector on the ASX for the December quarter, recovering some of the underperformance from the prior quarter). Oil Search is one of the highest quality energy stocks listed in Australia, with its low cost of production, long life assets, attractive growth options and partnership with a high quality operator (Exxon Mobil). Oil Search has a large stake in two very substantial growth projects in PNG and Alaska. Whilst little value is currently factored into the share price, we believe as oil prices recover further, and with a possible change in government in PNG, there are potential catalysts for these projects to deliver meaningful value over the medium term. Furthermore, we expect broader consolidation in the oil and gas industry as a response to the difficult macroeconomic conditions, with Oil Search a likely target given its high quality asset base. While we expect continued share price volatility in the near term, we believe that Oil Search is very well placed over the medium to long term to benefit from a recovery in oil prices.

CIMIC (long +31%) shares rallied after announcing the sale of a 50% interest in its mining services business (Thiess) to Elliot Advisors for an enterprise value of ~$4.3b. The cash proceeds of ~$1.7-$1.9b from the sale will enable CIMIC to return the balance sheet to a net cash position and provide capital management optionality going forward. The sale enhances CIMIC's leverage to the infrastructure construction cycle, with ~70% of earnings generated from Construction and Services Activities (up from ~50% previously). CIMIC has a dominant market position in the delivery of large-scale infrastructure projects, with the majority of its construction work linked to government projects. The upcoming pipeline remains substantial, with CIMIC noting in its results update that it was bidding for ~$470b of work to be delivered from CY21 onwards. We expect this pipeline will increase as governments look to boost infrastructure spending to help stimulate economies post COVID-19. We believe CIMIC is materially undervalued, trading on a normalised P/E of only ~10.7x despite this structural industry tailwind and its industry leading positions across construction and mining services.

Nine Entertainment (long +33%) had a strong quarter as advertising markets improved on the back of a recovery in economic activity and key advertisers returning to the market. Segments that are supporting this trend include Auto, Government and e-Commerce. As a result, available advertising inventories on TV were substantially reduced, driving an improvement in yields and creating a positive environment for Nine's revenues. This dynamic underpinned upgrades to company guidance and consensus estimates during the quarter. The improving economic backdrop was also supportive for Nine's digital advertising businesses such as 9Now (live streaming and catch up TV) which continues to see audience growth and is attracting an increasing share of media spend. Nine's other key Digital businesses of Stan and Domain remain well positioned for growth going forward. During COVID-19, Stan has been able to consolidate its position as the #2 streaming service in Australia (behind Netflix), and is on track to be a meaningful earnings contributor to the broader Group from FY21. Looking forward, we expect media spend will continue to recover as the economy re-opens further and companies seek to reinvest in their brands. Nine is particularly well positioned to benefit from this across its traditional media assets, while also benefiting from structural growth across its key digital properties.

Safran (long +38%) shares rallied strongly because of the improved outlook for air travel. Safran's key business is the sale of jet engines and parts for narrow-body Airbus and Boeing planes. 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 now has the most reliable and youngest engine fleet, which provides incredible predictability and visibility regarding its long term earnings outlook. Even during the depths of the crisis, while virtually every aerospace competitor and airline was loss-making, Safran continued to generate more than €1b of free cash flow, highlighting the outstanding resilience and quality of its business. We believe Safran is likely to triple its earnings per share over the next few years, based on an anticipated strong recovery in air travel, the benefits of its €2b+ cost out program and a potential re-start of its share buyback program. Safran represents everything we look for in a great long term investment: a highly cash generative business, with huge barriers to entry, best in class management, accelerating operating trends and an under-geared balance sheet.

Lyft (long +78%) is a ride-sharing company in the U.S. that competes with Uber. Since its IPO in 2019, the company has suffered from regulatory uncertainty (from California's push to reclassify drivers as employees) and question marks over its ability to compete effectively with Uber. Together with the COVID-19 pandemic curtailing demand, the stock had declined over 60% when we initiated a position in October. Our thesis was that with Uber and Lyft both prioritising profitability and no new competitors emerging, market share would remain stable while demand would recover rapidly post-COVID. Our thesis was further supported by early polling ahead of the U.S. elections which indicated that California would pass driver reclassification legislation, permanently enshrining drivers' contractor status as part of the Prop 22 ballot. The November vaccine news and the passing of the Prop 22 ballot have resulted in the shares nearly doubling since we first invested. Despite this strong performance, we continue to see substantial upside in Lyft. We believe Lyft can generate significant earnings growth over the medium term with the ability to generate consistent top-line growth above 30% and deliver long term EBITDA margins of ~25%.

Unibail-Rodamco-Westfield (URW) (long +111%) shares rallied strongly on the back of positive vaccine news along with shareholders blocking the Board's proposed €3.5b rights issue. As we have mentioned in prior reports and presentations, we believed the proposed capital raising was very poorly structured and timed, and we worked hard behind the scenes, together with a consortium of activist shareholders (led by Aermont Capital), to block the capital raising. With URW not facing an imminent covenant breach and having sufficient liquidity to meet debt rollovers during the next few years, we believed conducting a capital raise at an 80% discount to Net Tangible Assets (NTA), was a terrible option for shareholders. We fully endorse Aermont's proposal to sell some non-core U.S. assets as a superior alternative. URW shares rallied 41% on the day of the capital raise being blocked and ended up rallying strongly over the rest of the quarter given the prospect of a strong recovery in shopping centre foot traffic as the vaccine rolls out through Europe and the U.S. We continue to see large upside in URW shares, given the enormous share price discount to NTA, much improved decision making with Aermont representatives joining the board and the prospect of improving operating trends through 2021. As a further validation of the decision not to raise equity, in late November, management raised €2b of bonds with an average cost of debt of 1% and an average debt maturity of more than 8 years.

Empire State Realty Trust (ESRT) (long +52%) is a New York-focussed office REIT with approximately half of its portfolio value comprising arguably the "world's most famous building": the Empire State building. We initiated our position in June after a substantial fall in the share price post the onset of COVID-19, seeing an exciting opportunity to invest in an iconic property asset at incredibly depressed pricing. Around half the revenue from the Empire State building is derived from the famous observatory, which is currently open with restrictive capacity limitations. Both the observatory and the wider office portfolio have benefited from a huge capex improvement program over the past 5 years. Moreover, they look set to outperform the broader New York City office market over the coming years as the city recovers from the impacts of COVID-19. We believe the observatory is underappreciated by REIT investors despite a long history of strong compound revenue growth which should continue post recovery. ESRT remains well capitalised to overcome near term headwinds, with significant liquidity headroom and no debt maturities due until 2024. Even with the strong share price rally over the quarter, ERST still trades close to 35% below is pre-pandemic share price of ~US$14 and we believe there is significant upside to come as the New York City office market recovers and tourist visits to the observatory re-commence at full capacity.

Bed Bath & Beyond (BBBY) (long +19%) is a major U.S. retailer that has been struggling from many years of mismanagement, poor capital allocation and a lacklustre customer experience. Mark Tritton (a fellow Australian) was appointed CEO in November 2019 and has spent the past year replacing senior management with a proven team of high calibre executives that are now set to overhaul all aspects of the business. Tritton is an exceptional retail executive who had been instrumental in the turnaround of Target U.S. (he was the Head of Merchandising). At the time we bought in to BBBY in July 2020, the company was widely expected to go bankrupt. Short interest was an astounding 60%, almost every sell-side analyst rated the stock a "sell" or "neutral", and the shares had already fallen from US$75 in 2015 to less than US$5 by March 2020. We believed the shares had enormous upside even if the new management team only delivered on their initial cost out targets and non-core asset sales. BBBY has since been a very strong performer for the portfolio with the new management team demonstrating early signs of success on the turnaround program and the share price almost doubling from our initial entry price of around US$9.20. At its strategy day in October 2020, BBBY announced a target of delivering ~US$850-$1,000m EBITDA in 2023 which remains well above current consensus forecasts of ~US$650m indicating the level of scepticism that remains in the market. Despite the rally in the shares, we continue to see large upside in the stock as management execute on numerous areas of low hanging fruit such as better product sourcing, higher quality private label products, more efficient supply chain, closing loss-making stores, cutting head office costs, selling non-core assets, etc. BBBY sold its last non-core asset in mid-December (Cost Plus World Market) and announced a US$150m share repurchase concurrent with the sale. We expect management will flag further large scale buybacks going forward that will demonstrate both balance sheet strength and management's optimism in the future of the business.

SES (long +27%) is a French satellite network provider that supplies data and video connectivity to broadcasters, telecommunications companies, governments and airlines globally. SES also owns a 45% economic interest in C-Band spectrum that is critical to the future development of 5G services in the U.S. SES was impacted by the broad-based sell off in value and COVID-19 affected stocks in the June quarter which we utilised to significantly add to our position. The shares have recovered strongly in the December quarter after SES reported solid Q3 results that were ahead of market expectations and reaffirmed its full year guidance. Even with the recent rally, we believe SES remains extremely undervalued. The market currently ascribes limited value to the company's C-Band spectrum, which is set to deliver ~US$3.2b in payments (after tax) over the next 3 years, amounting to ~75% of the current market cap.

Cenovus Energy (long +49%) is an integrated energy company that develops, produces and markets crude oil, natural gas liquids and natural gas, primarily in Canada. Cenovus shares rose as the oil prices continued to recover and as discounts for their production compared to the WTI price narrowed, driving strong free cashflow generation in Q4 after very weak Q2 and Q3 performance. We increased our shareholding after Cenovus announced the acquisition of Husky Energy in late October 2020, to create the third largest Canadian oil and natural gas producer. We see strong strategic merit in the combination which unites high-quality and low-cost oil sands and heavy oil assets with extensive midstream and downstream infrastructure. The transaction should be highly accretive and lead to substantial synergies, increased scale, more stable cash generation and reduced group leverage.

Star Entertainment (long +22%) rose after announcing a solid trading update in October, which indicated that group domestic revenue from 1 July to 15 October was ~70% of the prior period and the balance sheet position had improved with the repayment of ~$145m of debt during the September quarter. The company is exploring value maximisation options such as the sale of the car park concession at its Sydney casino, a transaction that could generate in excess of $200m and accelerate its debt repayment profile. Star has an attractive outlook given the scarcity value of its casino licenses and the transformative impact of the Queen's Wharf development in Brisbane. We believe this is an underestimated driver of medium term earnings growth. In our view, Star's market cap of ~$3.5b hugely undervalues the asset base, licenses and likely cash flow generation of the company. While the market is very focused on the short term risks around COVID-19 disruption, we believe the medium term outlook for Star looks exceptional.

News Corp (long +21%) shares rose after reporting strong first quarter FY21 results with all key divisions materially ahead of market expectations. News Corp held an investor day for the Dow Jones division (including the Wall Street Journal) which further highlighted the robust growth potential in the business with the opportunity to double subscribers over the medium term. The Dow Jones division remains significantly undervalued in our assessment, with an implied stand-alone valuation of ~US$7b if we applied a similar multiple to comparable listed peer, the New York Times. Even with the increase in share price this year, we believe News Corp remains significantly undervalued. On a sum of the parts basis, we believe the media, U.S. real estate and publishing assets (including the above-mentioned Dow Jones division) are currently valued at roughly zero. News Corp management are taking progressive steps to better highlight the underlying value of these assets and simplify the corporate structure, which we expect will continue to unlock value going forward.

Key Stock Detractors for the Quarter

We exited a number of company-specific short positions near the market lows in March and have steadily increased our weighting to index short positions over the last few quarters as a hedge against our long book. Company-specific shorts have become more difficult given that the sectors that are trading at the loftiest share prices are those that have been huge COVID-winners, such as parts of the technology, healthcare, iron ore and consumer discretionary sectors. In general, we struggle to identify a clear negative catalyst (to establish a short position), given these stocks typically have a high degree of earnings certainty, strongly positive EPS revisions and no need to raise capital.

Gold equities were impacted by a broad-based sell off over the quarter as investors rotated out of safe-haven assets towards value and cyclical stocks on the positive vaccine news. This impacted our long positions in St Barbara, Resolute Mining and West African Resources. Fortunately, our short positions in the gold sector provided a helpful offset.

COVID-19 Update: Vaccine success and the upcoming global rollout

Back in our June and September quarterly reports, we flagged our belief that the likelihood of COVID-19 vaccine success was much higher than the consensus view and that the timing was likely to be much faster as well. In July 2020, the Australian Financial Review summarised our views:

FINANCIAL REVIEW

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Room for hope

24 July, 2020

A vaccine could be closer than many think, according to fund managers Raphael Lamm and Mark Landau from Melbourne-based L1 Capital.

They say they have conducted an enormous amount of detailed research on the prospects for a vaccine and have come away more positive than the consensus view.

"We are more positive than the market on both the likelihood of a safe and efficacious vaccine and also about the likely time frame," they said in a note to investors this week.

"Our head of healthcare research at L1 Capital is Dr Andrew Lin, who is a medical doctor as well as being fluent in Mandarin.

"We have been in direct contact with most of the leading vaccine companies, such as Pfizer/BioNTech, Moderna, AstraZeneca, Inovio, Novavax, Sinovac, CanSino Biologics and numerous other promising biotech companies both in the Western world and China.

"We believe that by the fourth quarter of 2020, we will have Phase 3 data available from Sinovac (China's most advanced vaccine player), Moderna, Pfizer/BioNTech and AstraZeneca/Oxford University, which should give equity markets comfort that there is some light at the end of the tunnel.

"The typical narrative we hear that a vaccine will take 3-5 years to come to market (because that has always been the case historically), is simply not recognising that this is the first time in a century that we have had a full-blown global crisis that has induced every government, regulator and vaccine company to expedite the entire vaccine development process, with unlimited global resources being thrown at it.

"Importantly, in the leading group of vaccine companies alone, there are a wide range of strategies being pursued (such as mRNA, Adenovirus, In-activated virus,DNA plasmid and glycoprotein) which provides numerous 'shots on goal' for success.

"While there is still uncertainty as to the exact percentage efficacy that will be achieved (and the durability of any vaccine), we believe it will be enough to enable people to resume near-normal activities, such as visiting a shopping centre, going to a cafe, working from the office and taking a flight."

Source: Australian Financial Review, Chanticleer "Iron Ore Miners Do Heavy Lifting", 24 July 2020

In November, less than 12 months after the virus was officially identified (and sequenced), we received the exciting news that multiple vaccine companies had passed their phase 3 trials, with exceptionally strong efficacy and safety data. The Company enjoyed its strongest month of performance on record in November, as we had positioned the portfolio for vaccine success, with numerous asymmetric bets on dramatically oversold "COVID-losers".

Our year-long research focus included intensive reviews of the fast-emerging scientific evidence along with more than 100 primary interviews with top executives and researchers from all the leading vaccine makers (across both the Western world and China), along with key government and regulatory personnel and frontline clinicians from China, Italy, France and the U.S. This in-depth research allowed us to become positive on the vaccines back in June, meaning we had considerable time to fine tune the portfolio to benefit from the eventual vaccine trial results.

The key catalyst was better than expected announcements from phase 3 trial results at Pfizer, Moderna and AstraZeneca. Notably, all three of these leading western vaccines achieved high protection from COVID-19 and very few side effects of concern, as summarised in Figure 4 below.

Figure 4: Major vaccine efficacy

Company	Type	Size of Trial	Efficacy for Infections	Efficacy for Severe Disease
Pfizer	mRNA	43,000	95%	89%*
Moderna	mRNA	30,000	94%	100%
AstraZeneca	Adenovirus	12,000	70%	100%

* *Small numbers of severe COVID-19 cases in trial (only 1 case in vaccine arm).*

Please note that due to differences in trial design and execution between the two mRNA vaccines and AstraZeneca's, it is difficult to compare them in a head to head fashion. For example, the AstraZeneca trial proactively tested patients on a periodic basis (which could decrease reported efficacy rates due to inclusion of transient infections) whilst Pfizer and Moderna relied on testing from patients with symptoms. Another mitigating factor is the 2 week pause in the AstraZeneca trial to investigate the cause of two adverse events, which may have disrupted timing of the second dose of the vaccine for some patients. In the coming month, we expect to receive further data from the U.S. arm of the AstraZeneca trial which will allow for more direct comparisons to the other two vaccines.

Nevertheless, it is pleasing to see that the three major western vaccines were all able to almost completely prevent severe infections. Once enough of our population is vaccinated, this should allay fears of our hospital/ICUs being overrun. This has been the key public health objective before governments are comfortable to exit lockdowns and temporary COVID restrictions. Given the high degree of protection from infections, we believe that the vaccinated individuals will also be much less likely to spread COVID-19 as they should be able to rapidly clear transient infections.

Looking forward, our vaccine research continues to give us high conviction that is there is a path back to a "normal" (pre-COVID) way of living in the near term:

- Existing western vaccines are likely to remain efficacious due to their ability to induce antibodies against emerging "mutant" strains of the virus.
- Positive final trial announcements over the coming months from a range of additional manufacturers, including Johnson & Johnson, Novavax, Sinovac and Sinopharm, are likely to result in the successful release of more vaccines enabling widespread global inoculation on an accelerated timetable.
- The intensive vaccine rollout underway in the U.S., U.K., China and Israel, and the planned roll-out of the Pfizer vaccine in Australia in March, with the AstraZeneca vaccine to closely follow, reinforces our view that vaccines will be widely available to the public in the developed world by mid-2021, with the developing world 6-12 months behind.
- The focus on vaccinating high risk populations (such as front line healthcare workers, aged care residents and workers, etc.) first, will ensure those most at risk are protected early in the vaccine roll-out.
- The co-ordinated efforts of big pharma, biotechs, regulators and governments around the world will ensure vaccine supply shortages are overcome quickly.

We continue to believe the outlook for COVID-19 will improve dramatically over the next year and there is clear line of sight to a return to "normal" towards the back half of the year. Our portfolio remains positioned to capture the continued recovery in hard hit sectors, such as Travel, Energy, Industrials, Mining, Shopping Centres and Infrastructure (Tollroads, Airports). Whilst many of these "reopening" positions have rallied strongly recently, most remain well below their pre-COVID levels despite often enjoying better competitive positioning and having better balance sheets than pre-pandemic. We expect further upside in these sectors as the vaccine is widely distributed and the economic recovery becomes more tangible.

L1 Long Short Fund Limited

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L1 Capital Overview

L1 Capital is a global investment manager with offices in Melbourne, Sydney, Miami and London. The business was established in 2007 and is 100% 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. L1 Capital manages money for a range of clients including large superannuation funds, pension funds, financial planning groups, asset consultants, family offices, high net worth individuals and retail investors.

L1 Capital uses a fundamental, bottom-up research process to identify investments with the potential to provide attractive risk-adjusted returns. The L1 Capital investment approach is largely style-neutral with modest value and contrarian characteristics. The firm launched its flagship L1 Capital Australian Equities Fund in August 2007.

Since inception, the L1 Capital Australian Equities Fund has been one of the best performing large cap, long only funds in Australia, outperforming the S&P/ASX200 Accumulation Index by 3.0% p.a. (after fees).

Board of Directors

Andrew Larke	Independent Chair
John Macfarlane	Independent Director
Harry Kingsley	Independent Director
Raphael Lamm	Non-Independent Director
Mark Landau	Non-Independent Director

Service Providers

Prime Broker	Morgan Stanley, Credit Suisse (Europe)
Administrator	Mainstream Fund Services
Auditor	EY

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Information contained in this publication
L1 Long Short Fund Limited 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. The portfolio is managed by L1 Capital Pty Ltd, which has established a reputation for offering clients best of breed investment products. L1 Capital manages money for a range of clients including large superannuation funds, endowment funds, financial planning groups, asset consultants, family offices, high net worth individuals and retail investors.