



Key Details

ASX code	LSF
Share price	\$1.435
Market capitalisation	\$914m
Shares on issue	636,639,144
Listing date	24 April 2018

The L1 Long Short Fund returned 0.6% in September (ASX200AI -3.7%).

The Fund returned 8.8% over the quarter (ASX200AI -0.4%).

Despite the Fund's strong recent performance, we believe the portfolio remains exceptionally attractive at present given larger than usual valuation anomalies.

After five months of gains, global markets declined in September (S&P500 -3.8%, FTSE100 -1.5%, Euro Stoxx 50 -2.3%, Nikkei +2.3%) on concerns of a pause in the global recovery as agreement on a further U.S. fiscal stimulus package continued to be delayed and the COVID-19 second wave outbreaks impacted Europe. The ASX200AI returned -3.7% in September, underperforming most offshore markets. The strongest sectors were Healthcare (+0.9%), Industrials (-0.3%) and Property (-1.5%), while Energy (-11.1%), Information Technology (-6.8%) and Consumer Staples (-6.6%) were very weak.

The Fund performed well in September, particularly considering the broad-based sell off in cyclical and value names over the month. Stock selection was again a key driver with several contrarian stock opportunities delivering strong gains after positive updates.

Some of the key contributors to Fund performance in September were:

Bed Bath & Beyond (BBBY) (long) (+27%) has been a very strong performer for the Fund over the past 3 months. BBBY 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 earlier this year, 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 \$75 in 2015 to less than \$5 by March this year. We bought in at around \$9.20 in July, believing that 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 its strategy day on October 28, where management is expected to lay out their plans for improving sales trends, enhancing the digital offering, reducing costs and outlining their capital management plans. Despite the rally in the shares since March (to around \$15 by month end), we continue to see very large upside in the stock given 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). We also expect management will flag large scale buybacks that will demonstrate both the balance sheet strength and the optimism management sees in the future of the business.

Net Performance*

	NTA pre-tax
One month	0.63%
Three months	8.82%
One Year	2.15%
Two Years (p.a.)	3.17%
Total return since inception	(11.24%)

*Source: Mainstream Fund Services. Net performance is defined as the movement in NTA pre-tax. Performance is shown after all applicable fees and charges. Past performance should not be taken as an indicator of future performance.

Teck Resources (long) (+25%) shares rallied strongly over the month driven by early signs of recovery in the coking coal market. Increasing seaborne demand from India and China following a recovery in domestic steel production drove an 18% increase in coking coal prices in September. Teck is one of the world's highest quality mining companies with very low-cost operations in coking coal, copper and zinc. All of Teck's main assets are situated in low risk jurisdictions, such as Canada, the U.S. and Chile. Teck is currently building one of the world's largest copper mines (QB2) at a time when the world is gradually becoming short copper, due to ongoing grade declines at the world's largest mines. Copper demand continues to enjoy secular growth due to rising living standards across Asia. We established a position in the company with the view that Teck was well positioned to benefit from a recovery in copper and coking coal prices over the medium term, as spot prices were close to marginal cash cost for many mines and incremental supply has proven difficult to bring on in a timely manner. We have started to see early signs of this recovery and continue to believe Teck is exceptionally well placed to benefit from this going forward. Despite the strong performance in September, we continue to believe Teck is materially undervalued. Even at today's depressed commodity price assumptions, Teck trades on a P/E of only 9.2x FY21 (consensus earnings) and 4.7x EV/EBITDA, despite a large cost out program still to come over the next few years.

Peet Limited (long) (+20%) shares rallied strongly with a strategic real estate fund manager (360 Capital) becoming a substantial shareholder. Peet is a developer of master planned residential communities with a primary focus on the first home buyer. We provided a detailed note on Peet in our December 2019 quarterly report which called for a change in strategy for the company to focus on the funds management business and transition to a capital-light development model. We welcome further strategic interest in Peet and continue to believe the company is significantly undervalued. We continue to engage with the Board and see a path to a much higher share price assuming a well-executed change in strategy as we outlined in our December quarterly report.

Some of the key detractors to fund performance in September were:

Oil Search (long) (-19%) shares fell over the period driven by a -6% decline in crude oil prices and broader transition away from energy stocks (energy was the worst performing sector on the ASX in September). Oil Search is one of the highest quality energy stocks listed in Australia, given 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 and, as oil prices recover, we believe the market will likely reincorporate meaningful value for these projects in group valuations. Furthermore, we believe the more difficult economic backdrop in PNG is likely to incentivise the PNG Government to resolve their differences with the joint venture to enable this project to proceed (subject to market conditions). While we expect continued share price volatility in the near term, we believe that Oil Search is extremely well placed over the medium to long term to benefit from a recovery in oil prices.

Unibail Rodamco Westfield (URW) (long) (-27%) shares declined sharply after the announcement of a €9b capital reset plan to strengthen the balance sheet including, €4b in asset disposals and a €3.5b capital raise with terms to be announced post EGM approval in the December quarter. URW operates the highest quality portfolio of retail shopping malls in Europe and the U.S. The company acquired Westfield for \$32b in December 2017 in a cash and scrip offer which increased their proforma gearing from ~33% to close to ~40% of LTV. We established a position in the company in May after the shares had already fallen more than 65% since January. Our valuation views incorporated a potential capital raise to bolster the balance sheet until restrictions eased, however, we believe the company's reset plan was poorly structured and timed in light of market conditions. URW does not have any covenant breaches likely in the near-term, with positive data points in both foot traffic and rent collection rates likely as we move into 2021. Furthermore, the announcement of a future capital raise without confirmation of the exact date or key terms has created an overhang on the stock for an extended period. We believe URW shares are materially undervalued, trading at an 80% discount to latest reported Net Tangible Asset Value and at a substantial discount to the likely asset value post equity raise, further devaluations and asset sales. Further clarity on the equity raise terms, execution of the asset sale program and a continued recovery in foot traffic should all act as share price catalysts over the next 6-12 months.

We remain extremely positive about the medium term outlook for the portfolio, given the unusually large number of stocks in the Fund that presently have more than 50% upside to valuation. As the market becomes more confident that an effective COVID-19 vaccine or treatment is coming, we expect to see a large share price recovery in many of these oversold companies, along with a major rotation into value and cyclical stocks that would act as a further tailwind to performance.

Portfolio Exposures (month end)

Number of positions	92
Number of long positions	70
Number of short positions	22
Gross long exposure (%)	197%
Gross short exposure (%)	87%
Gross exposure (%)	284%
Net exposure (%)	110%

Overview and Investment Philosophy

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, pension funds, financial planning groups, asset consultants, family offices, high net worth individuals and retail investors.

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Investment Guidelines

Typical number of positions	50-100 securities
Geographic exposures	Max 30% gross outside of Aust/NZ
Net exposure limits	Max 150% of NAV; typically 30-90%
Gross exposure limits	Max 300% of NAV; typically 150%-300%

Net Tangible Assets Per Share (as at 30 September 2020)*

NTA pre-tax	\$1.7752
NTA post-tax	\$1.8658

*Source: Mainstream Fund Services. The NTA pre-tax is calculated before the provision for deferred tax on unrealised gains and losses on the investment portfolio. The NTA post-tax is calculated after all taxes.

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

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