

Blackwattle Small Cap Long-Short Quality Fund

June 2024

About the Fund

We aim to buy businesses with a competitive advantage and good corporate governance, priced below intrinsic value at the right price.

We are fundamental investors, using deep bottom-up research to identify the best Small-Cap opportunities. Our process identifies both high/emerging quality companies underappreciated by the market for long positions, and low/declining quality companies overvalued by the market for short positions. Active risk management is a core part of our approach with capital preservation considered in every layer of our investment process.

Our process aims to provide the framework to outperform the benchmark throughout the economic cycle and under various factor leadership scenarios. Reflecting this, the fund aims to deliver lower volatility, smaller drawdowns, and higher risk-adjusted returns.

Blackwattle Investment Partners

Blackwattle is a new generation, highly aligned, Australian investment manager investing in quality businesses and people.

Alignment

Shared staff ownership, zero personal trading, profit and personal salary reinvestment, and most importantly significant personal investment alongside our clients.

Quality

We aim to buy businesses that have a forward advantage, trustworthy aligned management, priced below intrinsic value.

Trust

We believe that honesty and transparency builds trust with our clients, stakeholders, and community.

Invest Better. Live Well.

Key Information

Fund Name	Blackwattle Small Cap Long-Short Quality Fund
Inception Date	November 2023
Typical number of stocks	30-60 Long, 10-30 Short
Cash limit	50% (typically +10% to -10%)
Cash Distributions	Semi annually
Redemptions	Daily
Objective	The Fund aims to outperform the S&P/ASX Small Ordinaries Accumulation Index (after fees and before taxes) over the long term

Portfolio Managers



Daniel Broeren

20+ years investment experience. Extensive long and short experience. Most recently Portfolio Manager, Watermark Funds Management (Australian Long/Short). Previously Portfolio Manager of the Invesco Small Companies Fund.



Robert Hawkesford

20+ years investment experience. Most recently in a small team at Ellerston Capital managing the institutional Australian Small Cap portfolio. Member of Ellerston's ESG and Broker Review Committees.

Fund Performance¹

Blackwattle Small Cap Long-Short Quality Fund Performance (net of fees) as at 30 June 2024

	1 month	3 months	6 months	2 Years p.a.	5 Years p.a.	10 Years p.a.	Inception p.a. ²
Fund (Net)	-1.34%	-2.56%	2.84%	-	-	-	6.52%
Benchmark³	-1.39%	-3.61%	0.68%	-	-	-	4.98%
Active Return	0.05%	1.04%	2.16%	-	-	-	1.54%

¹ Returns are calculated after fees have been deducted and assume distributions have been reinvested. Returns are normalised for the removal of unallotted applications, following the transition of Investment Manager of the Fund. No allowance is made for tax when calculating these figures. Past performance is not a reliable indicator of future performance. Source: Apex. ² The inception date for the Fund is 21 November 2023. ³ S&P/ASX Small Ordinaries Accumulation Index. There was a six-month transition period beginning 21 November 2023 and ending 21 May 2024, following the transition of Investment Manager of the Fund. During this transition period, the Fund Benchmark was 50% cash rate as determined by the Reserve Bank of Australia and 50% S&P/ASX Small Ordinaries Accumulation Index. Returns are normalised for the removal of unallotted applications, following the transition of Investment Manager of the Fund.

Top 5 Holdings



Market Commentary

The ASX Small Ordinaries Accumulation index fell -1.39% in June, driven by Small Resources which fell -8.02%. Within Resources, the largest declines were in Uranium and Lithium companies. Small Industrials rose 1.43%, led by more defensive areas of the market including Financials, Staples, and Healthcare. The key economic data point for the month was Australian monthly inflation for May, which came in hotter than expected at 4.0%. This was the highest inflation print for six months and a reacceleration from 3.6% in April. In response, Australian government bond yields rose sharply and expectations for the direction of RBA rates over the next six months swung from cuts to hikes. Australia stands in contrast to other developed markets like the US, UK and Europe where rate cuts are still firmly on the agenda.

Portfolio Commentary

The Blackwattle Small Cap Long-Short Quality Fund outperformed the ASX Small Ordinaries Accumulation index by 0.05% in June.

Key Contributors to performance in June were Spartan Resources (SPR), Light & Wonder (LNW), and a short position in the technology sector. Spartan Resources is a gold company in the process of exploring and developing its flagship Dalgaranga Gold Project in WA's Murchison region. The project contains a collection of high-grade deposits, still open at depth and producing outstanding drill results, less than 1km from their existing processing plant and infrastructure.

Spartan's share price rose 31.3% in the month as nearby ASX-listed Ramelius Resources built a 'strategic investment' of 17.9% in the company, highlighting the quality of Spartan's assets and raising the prospect that M&A could be on the cards.

Light & Wonder was also a key contributor, as strong early performance data became available for the launch of its highly anticipated Dragon Train game in North America. However, what was somewhat surprising was that the success of Dragon Train has been followed up by the launch of two other games that have also debuted very strongly. It has become clear to investors that LNW are now starting to demonstrate the benefits of the turnaround work that has been underway for some time. They are building a machine that creates new content, rather than relying on the success of one or two games. This is a strong competitive advantage that drives enduring value.

Given deteriorating economic indicators, which we discuss further in the outlook, the portfolio has been positioned toward quality growth companies with defensive demand characteristics. However, we do hold selective short positions in the technology sector for stock-specific reasons. One of the fund's highest contributors for June was a short position on a company with services linked to the data centre sector. We expect the company to miss expectations into 4Q25 and FY25 as revenue ramps up slower than costs.

Key Detractors to performance for June were holdings in the battery minerals sector (LRS and PMT), and Beach Energy (BPT). The lithium commodity price continues to follow a volatile trading pattern, re-testing lows seen in February. Perversely, when considering investments in the resources sector, the risk is the lowest when commodity prices are falling toward the lower end of the cost curve for mining companies with tier-one assets. At current spodumene lithium prices, few hard rock miners are generating much free cash flow today. As such, we continue to maintain modestly sized holdings in the lithium sector. In our view projects with superior economics like Latin Resources and Patriot Metals are well placed to ride out near-term volatility in the Lithium price.

Beach Petroleum's share price fell after the company reset medium-term production expectations as part of the company's June strategy day. Incoming CEO Brett Woods (Ex-Santos) has been hand-picked by Kerry Stokes to drive a company-wide transition of Beach from an accident-prone explorer/developer to a lean, cash-generative producer. As part of his mandate, Woods used his first strategy day to pare back lower returning projects. Importantly, however, on 20 June the Australian Energy Market Operator (AEMO) convened an emergency meeting with the gas industry, highlighting that gas supplies may be insufficient to meet demand this winter season. Spot prices for gas have subsequently spiked to double the usual rate. Given the long lead-times for renewable generation we are likely to see sustained higher energy prices in the meantime. We expect domestic gas producers to benefit from periods of above-average peak pricing as coal generation is wound back over the next decade. As such, we see the resetting of Beach's production expectations to be a hard floor for future returns from the company.

Outlook

The portfolio is currently very balanced with no large tilts or biases to any one sector. We remain overweight quality growth businesses with more defensive demand profiles. A recent peaking of US bond yields also supports valuations for long-duration assets. We have a mild bias towards defensives over discretionary in the Consumer sector where we are overweight Staples, driven by bottom-up ideas in Agriculture, and underweight Discretionary as we see increasing risks in consumer confidence driven by inflation and the threat of a new round of RBA rate hikes. The portfolio has an overweight position in Resources. The recent pullback in commodities has created opportunities to add to holdings in bulk resources and metals, in particular.

Dan & Rob

How to Invest

To invest click on the link www.blackwattlepartners.com/invest/ or call 02 7208 9922.

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