Equus Point Capital Market Neutral Strategy

Performance Update 30 June 2021

Net Returns	1m	3m	6m	1Yr	2yr pa	Incept pa
Equus Point Capital	1.78%	2.43%	8.93%	12.32%	3.93%	4.70%
Cash	0.01%	0.02%	0.05%	0.15%	0.41%	0.65%
Excess v Cash	1.77%	2.41%	8.88%	12.17%	3.52%	4.06%

Risk Characteristics	
Volatility	7.85%
Beta	0.11
Correlation to S&P/ASX 200	0.26
Sharpe Ratio	0.52

Commentary

The Strategy returned 1.78% after fees for the month. Please note that with the Fund closed during May 2020, the results for the month are simulated returns.

On a gross basis stock selection generated 2.35% alpha for the month, with long exposures contributing 2.73% alpha and a modest short exposure contributing -0.89% alpha. Our beta positioning contributed 0.51% alpha.

The volatility of returns since inception is 7.9% annualized versus 18.3% for the S&P/ASX 200 Accumulation Index.

Positive alpha contributions from stock positions included:

- Materials (+1.33%)
  - Iluka +0.43%
  - Mineral Resources +0.38%
  - Boral +0.20%
  - Pilbara Minerals +0.14%
- Healthcare (+0.76%)
  - Pro Medicus +0.66%
- Industrials (+0.67%)
  - Reece +0.44%
  - NRW Holdings +0.16%
  - Seek +0.13%
- Consumer Discretionary (+0.30%)
  - Premier Investments +0.19%
  - Dominos +0.21%

Negative alpha contributions included:

- Information & Technology (-0.72%)
  - Altium -0.61%
  - Codan -0.14%
- Communication Services (-0.54%)
  - TPG -0.30%
- Financials (-0.28%)
  - Magellan (short position) -0.28%
  - Virgin Money UK -0.19%

Recently we were approached about how our investment process and stock selection could be applied to a long only portfolio. Specifically, the brief required:

- A long only portfolio,
- No leverage,
- No borrowing and shorting of stock,
- Concentrated portfolio, and
- Futures permitted for the purposes of equitizing cash holdings.

We explored this briefly in our January monthly report. Where the following analysis differs from the prior work is the focus on a more concentrated portfolio and the use of futures to equitize any cash balance.

The following analysis is for the period from Jun 2000 to Jun 2021 on a net basis (being after commission and before any management fees).

	Strategy	XJOAI
Return	3438.51%	430.66%
Return pa net	18.50%	8.27%
Excess	10.23%	
Volatility	15.12%	13.30%
Downside Volatility	10.31%	10.82%
Reward / Risk	1.22	0.62
Sharpe	0.98	0.34
Sortino	0.99	
Tracking Error	10.10%	
Information Ratio	1.01	
Drawdown	-31.98%	-47.18%
Drawdown Length	29	70
Drawdown Length Average	7	18
Beta	0.86	1.00
Correlation	0.75	1.00
Hit Rate	66.7%	63.9%
Average Return	1.52%	0.74%
Av Positive	3.93%	2.99%
Av Negative	-3.29%	-3.25%
Av Up Markets	3.59%	2.99%
Av Down Markets	-2.14%	-3.25%
Monthly Max	14.6%	10.2%
Monthly Min	-12.8%	-20.7%
VaR Monthly @ 95% CI	-5.66%	-5.57%
VaR Annual @ 95% CI	-6.37%	-13.61%
12m Maximum	68.83%	44.70%
12m Minimum	-29.26%	-39.95%
Ratio 12m Positive Return	87%	74%
Ratio 12m Positive Excess v XJOAI	80%	

At face value these are attractive results. Granted the model would suggest annualized volatility greater than that of the S&P/ASX 200 Index, but this is more than compensated with excess returns and superior risk adjusted returns.

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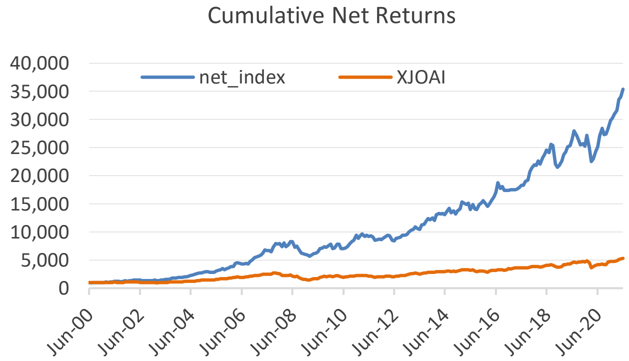
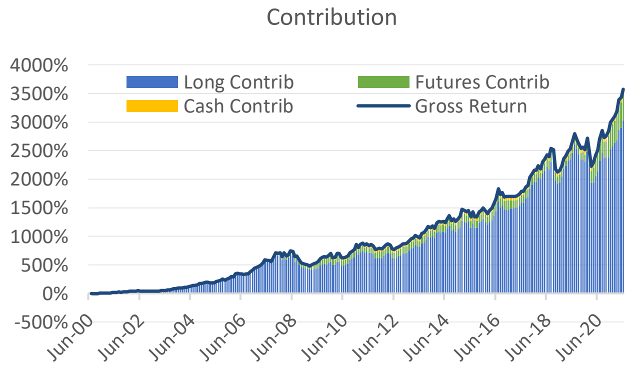
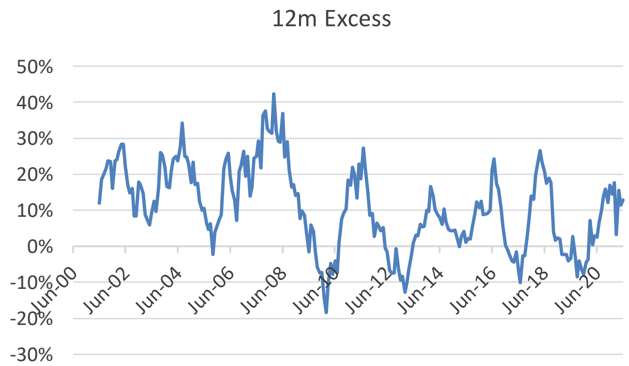
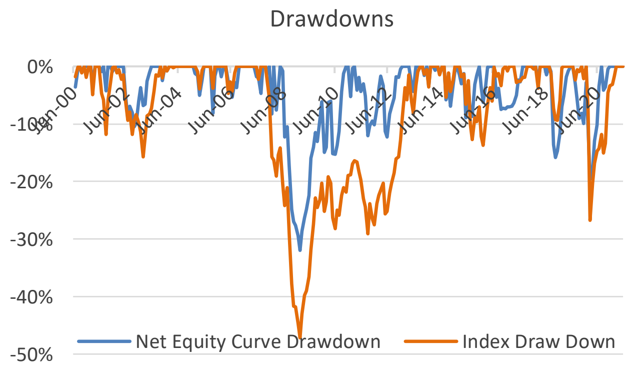
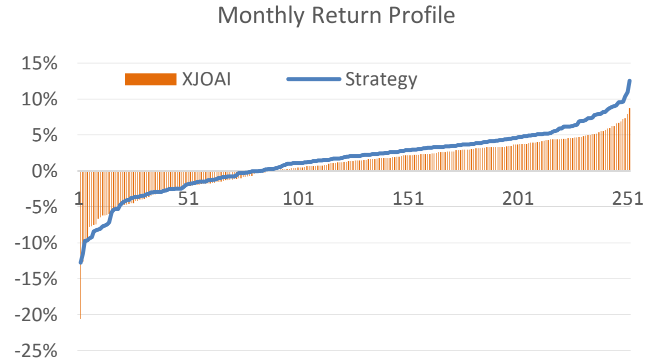
Regular readers would know we are proponents of using charts to demonstrate the nature of concepts and how a portfolio behaves. To that end the following charts break down the results of this concentrated long only model.

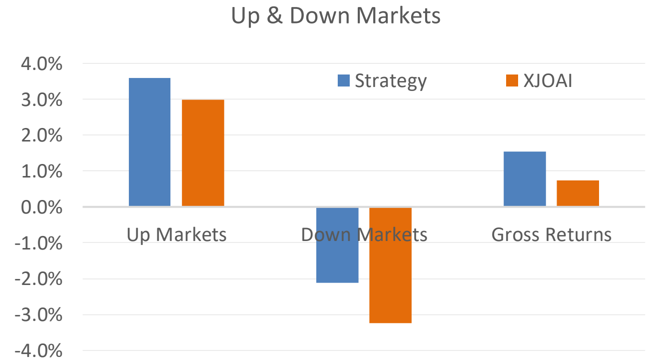


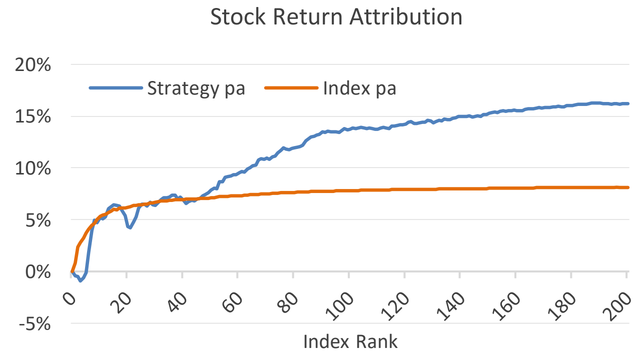








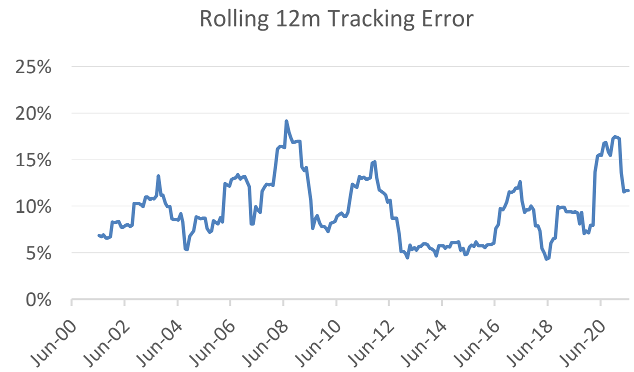


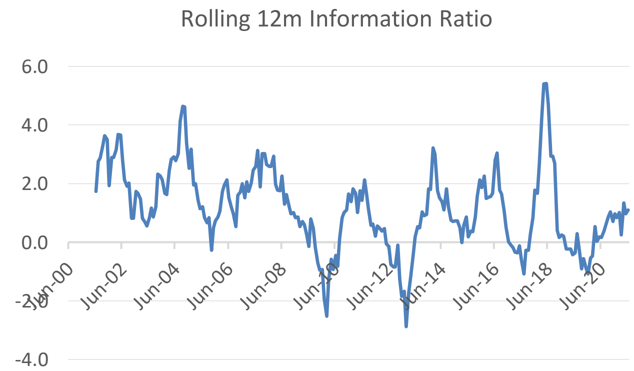


There are four issues with such a portfolio that perhaps require further consideration:

- Tracking error
- Active share
- Portfolio turnover and tax considerations
- Capacity

Firstly, the tracking error (defined as the volatility of excess returns) for such a portfolio is 10%. To put this into perspective the tracking error for a typical index fund would be less then 0.5% and an actively managed equity fund would have a tracking error from anything from 4% for a broad-based fund to 8% for a concentrated fund. The tracking error is certainly beyond the typical tracking error one might experience for a mainstream equity product. That said, the tracking error reflects the strategy adding value in positive markets and preserving capital in down markets. In effect, investors are rewarded by accepting the elevated tracking error given an average information ratio 1.0 (defined as excess returns divided by tracking error). Note also how the large tracking error in the chart below has corresponded with periods of market declines – periods where this strategy would have preserved capital.

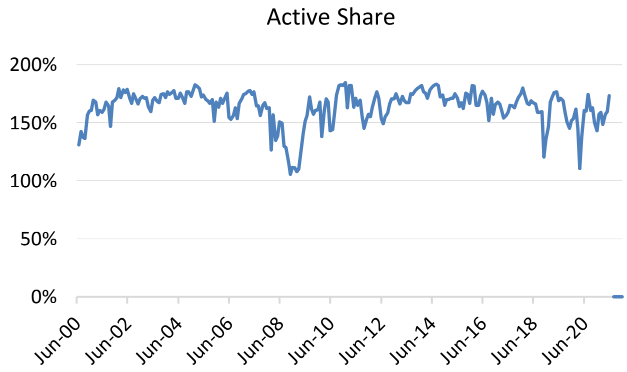


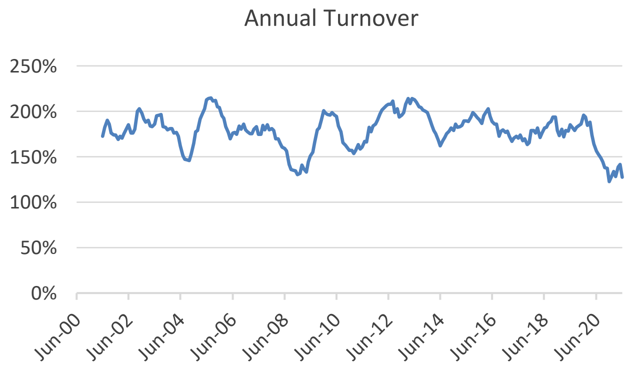


Secondly, the model is a concentrated portfolio with a high active share component. Active share is defined as the sum of the absolute difference between a portfolio's stock weights and index weights. Typically, an index fund might have an active share of less than 5% and standard active funds might have an active share of 60% to 120%.

Attributing returns across the index (based on index rank – see chart on previous page) it is apparent that the model derives much of its returns from mid and small caps, a product of taking positions that vary substantially from the index – and hence the high active share component. Put simply, the model does not hug an index.

With annual turnover greater than 100% one would need to would consider the tax implications of a strategy that yields a large degree of its return stream from realized capital gains. Such a strategy as part of a broader exposure to equities (say an index fund where a buy and hold approach yields low turnover) or within the right tax environment (such as a super fund or pension fund) would help to offset these tax issues.





Finally, one would need to address the issue of capacity. A strategy that requires a higher degree of turnover needs to find a balance between portfolio size and being able to achieve excess returns. The larger a portfolio becomes, employing a high turnover strategy that derives a large part of its returns from mid and small market cap stocks will incur costs associated with market impact. One needs to balance those market impact costs and available liquidity with fund size.

If a manager decides to focus on growing the fund, then returns must naturally suffer or the manager is forced to invest in more liquid stocks (i.e. become more of an index hugging portfolio). This might be good for the manager given he/she derives fees from funds under management. Alternatively, if the manager was focused on maximizing the potential for out-sized returns and limited fund size, then that is clearly to the benefit of investors.

In summary, one needs to balance the pros of the model (high headline returns, high risk adjusted returns and shallower drawdowns) with the cons (higher tracking error, higher turnover and tax implications). That said, as a part of a broader exposure to Australian equities and a capacity constrained focus, such a strategy would prove valuable for the investor seeking a product that is materially different to standard equity products.

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Net Monthly Performance

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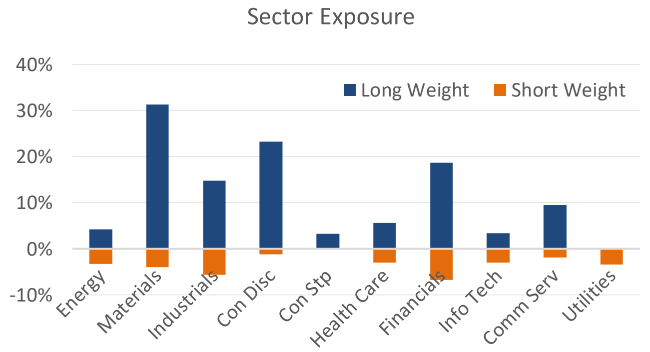
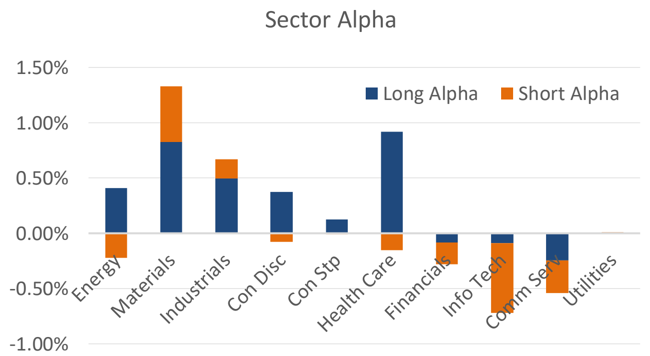
Gross Monthly Performance

Asset	Positions	Weight	Contrib	Alpha
Long	79	113.9%	5.13%	2.73%
Short	33	-32.0%	-1.72%	-0.89%
Futures		-66.3%	-1.06%	0.51%
Cash		18.1%	0.00%	0.00%
		100.0%	2.35%	2.35%
Cash				0.01%
Excess				2.34%

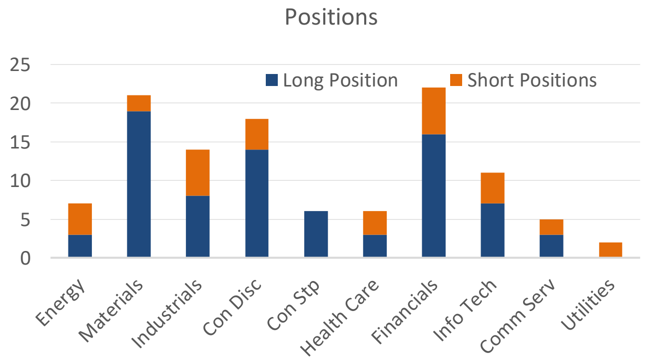


Exposure and Gross Monthly Alpha

Sector Name	Long Weight	Short Weight	Active Weight	Alpha Contrib
Energy	4.19%	-3.34%	0.85%	0.19%
Materials	31.36%	-3.90%	27.46%	1.33%
Industrials	14.73%	-5.57%	9.16%	0.67%
Cons Disc	23.19%	-1.13%	22.06%	0.30%
Cons Staples	3.23%	0.00%	3.23%	0.13%
Health Care	5.65%	-2.98%	2.67%	0.76%
Financials	18.72%	-6.74%	11.98%	-0.28%
Info Tech	3.35%	-2.97%	0.39%	-0.72%
Comm Serv	9.52%	-1.94%	7.59%	-0.54%
Utilities	0.00%	-3.44%	-3.44%	0.01%
Stock Total	113.94%	-32.00%	81.94%	1.84%
Futures			-66.28%	0.51%
Cash			18.06%	0.00%
Total			100.00%	2.35%

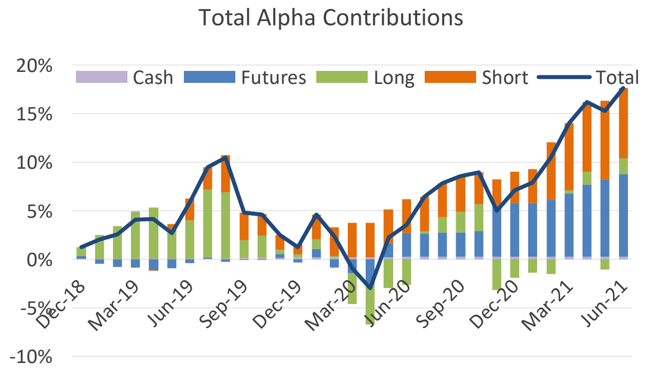


Net exposure including futures	15.7%
Gross exposure excluding futures	145.9%
Gross exposure including futures	212.2%



Major Alpha Contributors

Name	Weight	Contrib	Alpha
Top Five Contributors			
Pro Medicus	2.90%	0.70%	0.66%
Reece Limited	3.73%	0.51%	0.44%
Iluka Resources	2.72%	0.49%	0.43%
Soul Pattinson & Co.	3.60%	0.48%	0.40%
Mineral Resources	2.60%	0.44%	0.38%
Bottom Five Contributors			
Magellan Financial	-3.16%	-0.37%	-0.28%
Origin Energy	-2.00%	-0.38%	-0.29%
TPG Telecom Ltd	-1.79%	-0.33%	-0.30%
Oz Minerals Limited	2.34%	-0.26%	-0.32%
Altium Limited	-2.19%	-0.67%	-0.61%



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Investment Manager

Equus Point Capital is a boutique fund manager focused on producing meaningful risk adjusted returns from the Australian equities market. Equus Point was founded in 2017.

Equus Point's investment process is systematic, designed to produce a return stream irrespective of market direction over the long term, with low volatility and uncorrelated to traditional asset classes.

Strategy Objective

To deliver absolute returns above the RBA Official Cash Rate over a rolling five-year period, with low volatility and a low correlation to traditional asset classes.

Investment Philosophy

Equus Point uses a systematic approach to investing, seeking to harvest meaningful risk adjusted returns from behavioral biases in the Australian equities market. The strategy uses both long and short positions coupled with index futures to achieve a market neutral portfolio that seeks to produce positive returns irrespective of equity market direction and uncorrelated to traditional assets. Equus Point's robust risk management approach limits to portfolio's beta positioning, portfolio volatility, individual stock positioning, and long and short portfolio positioning.

The Strategy employs a proprietary systematic investment process. The Fund invest exclusively in Australian equities and equity derivatives.

We believe in the following:

- In the short to medium term behavioral biases of investors can influence stock prices leading to both momentum and reversion effects. Momentum is where stocks with positive historical returns tend to be rewarded with a continuation of positive returns, and stocks with negative historical returns tend to underperform with a continuation of negative returns. Reversion is where stock prices initially overshoot before returning to a perceived fair value.
- Meaningful risk adjusted returns can be achieved through a portfolio of both long and short positions seeking to harvest positive and negative momentum.
- Managing the risks of the potential for stock price reversion, stock volatility, portfolio volatility and beta exposure are a core part of the investment process.
- Market neutral positioning between long and short portfolios is ensured using index futures to offset residual beta risks.
- Combining the above dynamics with acceptable leverage delivers a portfolio that is designed to provide superior risk adjusted returns through market cycles.

Benefits of the Strategy

1. A systematic strategy with a disciplined focus on risk management.
2. Attractive risk adjusted returns over the long term.
3. Low volatility return stream uncorrelated to traditional asset classes over a rolling five-year time frame.
4. Expected to preserve capital in volatile and negative equity markets.

Further information: www.equuspointcapital.com
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