

Fund performance

As at 31 March 2021	3 Month	6 Month	FYTD	1 Year	Since Inception (Annualised) ²
Blue Orbit Australian Small Cap Systematic Alpha Fund ¹	4.37%	16.25%	23.37%	51.92%	2.97%
Benchmark ³	2.09%	16.20%	22.80%	52.15%	9.10%
Excess Return	2.28%	0.05%	0.57%	-0.22%	-6.13%

1. Returns shown are Net of Fees. Returns shown for the Lead Series (October 2019).

2. Inception Date is 11 October 2019.

3. Benchmark is the S&P/ASX Small Ordinaries Accumulation Index.

In a rather volatile quarter, the *Blue Orbit* Australian Small Caps Systematic Alpha Fund returned a healthy 4.4%, outperforming its Benchmark, the S&P/ASX Small Ordinaries Accumulation Index, by 2.3%. A measure of the quarter's volatility was that on three separate occasions the market rapidly gained 3%, or more, only to give up most, if not all, of those gains. The final bounce back saw the Fund's Benchmark finish the quarter up 2.1%. Catalysts for the rapid market rises included the approval of a USD\$2t plus COVID-19 relief package in the US (with a further multi-trillion dollar infrastructure plan in the works), a strong domestic February reporting season, rising commodity prices and the general trend of better than expected economic data across the globe.

As the Australian reporting season unfolded it quickly became apparent that the Australian economy (and to a certain extent the broader global economy) had weathered the COVID-19 storm, and companies were well advanced in recovering lost profits. Aiding the recovery was the continuing growth in business and consumer confidence post the arrival of COVID-19 vaccines, and the continuation of expansionary monetary and fiscal policies. This backdrop was the primary driver of companies exceeding profit expectations and issuing positive guidance during reporting season. Further, fears of an economic cliff in Australia at the completion of JobKeeper subsided, as job ad numbers continued to climb with a corresponding fall in the unemployment rate.

Regarding the three intra-quarter sell offs, the main concern was that economic growth was recovering too quickly and inflationary pressures would eventually reappear after a 10+ year absence. These concerns saw bond traders push the yield on the US 10-Year above 1.7%, from a low of 0.5% at the height of the COVID-19 economic collapse. Each time the equity markets sold off in response to the climbing bond yields, central banks across the globe increased their bond purchases to relieve the pressure. These coordinated actions pacified equity investors and market indices bounced back on each occasion. Amongst all the volatility, commodity prices, oil, iron ore and rare earths in particular, continued their strong run, before fading slightly in late March as the prospects of a sustained economic recovery grew. The one exception was the gold price, which continued on its downward trend despite rising inflationary expectations. Given the number of stocks leveraged to commodity prices, these movements had a considerable effect on the performance of the Australian stock market and ultimately the Fund.

Notwithstanding the Australian small caps index posting positive returns for the quarter, they were modest in comparison to its larger local counterpart. The S&P/ASX 100 index returned 4.96% for the quarter, partially due to not feeling the full brunt of the late quarter moderating of commodity prices. Additionally, with a strengthening domestic economy including a very buoyant housing market, the large cap domestic banks outperformed. However, in general the Australian market underperformed international markets in AUD terms, with the MSCI World index growing by 6.3% (in AUD). In the US, the S&P 500 returned 7.5% (in AUD) with value stocks outstripping growth stocks by a considerable margin (+11.6% vs +3.3%, both in AUD). Unlike the Australian market, the US market continued to see small cap stocks outperform, with the Russell 2000 delivering a return of 14% (in AUD) to eclipse the Russell 1000, which returned only 7.2% (in AUD). Other markets to see strong growth during the quarter, despite renewed lockdowns, were the European markets. The FTSE 100 (UK) was up 7.7% (in AUD) and the German DAX was up 6.5% (in AUD).

Australian Small Caps Systematic Alpha Fund (Wholesale)

March Quarter Performance Report as at 31 March 2021



GICS Sector Attribution: March Quarter

Sector Attribution	ASX Small Systematic			S&P/ ASX Small Ordinaries			Attribution		
	Average Weight	Total Return	Contribution To Return	Average Weight	Total Return	Contribution To Return	Allocation	Selection + Interaction	Total
Consumer Discretionary	18.89%	10.47%	1.87%	17.11%	6.52%	1.07%	0.06%	0.76%	0.82%
Information Technology	7.40%	18.97%	1.27%	6.65%	-0.76%	-0.09%	-0.02%	1.35%	1.32%
Financials	10.90%	1.60%	0.09%	13.63%	6.86%	0.90%	-0.19%	-0.54%	-0.73%
Communication Services	6.66%	15.41%	1.03%	5.79%	9.93%	0.56%	0.10%	0.33%	0.43%
Consumer Staples	6.71%	14.72%	0.94%	6.98%	9.06%	0.62%	0.02%	0.33%	0.35%
Energy	0.69%	-3.20%	-0.05%	2.38%	-5.91%	-0.14%	0.12%	0.00%	0.11%
Utilities	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Real Estate	9.87%	-0.99%	-0.11%	12.25%	0.03%	0.00%	0.02%	-0.09%	-0.07%
Materials	22.88%	2.73%	0.52%	21.58%	0.74%	0.16%	-0.03%	0.43%	0.40%
Health Care	5.69%	8.96%	0.48%	6.73%	-2.28%	-0.17%	0.06%	0.61%	0.67%
Industrials	9.33%	-17.38%	-1.60%	6.91%	-11.66%	-0.81%	-0.34%	-0.58%	-0.93%
Cash	0.99%	13.88%	0.14%	0.00%	0.00%	0.00%	0.11%	0.00%	0.11%
Total	100%	4.57%	4.57%	100%	2.09%	2.09%	-0.11%	2.59%	2.49%

Amongst the volatility of the first quarter, the *Blue Orbit* Australian Small Caps Systematic Alpha Fund outperformed. Driving this outcome was superior stock selection, while attribution from sector allocation was negligible. The negative effects of an overweight holding to the Industrials sector (-11%) and an underweight to Financials (+6.9%) were offset by an overweight to both the Consumer sectors – Discretionary (+6.5%) and Staples (+9%) – and an underweight to Healthcare sector (-2.3%). The Fund also generated material outperformance with the removal from the index of three previously suspended stocks, Freedom Foods, Phoslock Environmental Technologies, and FAR. Prior to their suspension, the Fund did not have a position in any of the stocks due to their poor financial and trend characteristics. Further, prior to its suspension Freedom Foods negative price momentum, increasing price volatility and short interest reached critical levels meaning it was classified as a Torpedo (a Blue Orbit overlay that recommends the sale of a stock or ban on purchasing it).

Stock specific gains came from the Fund's selection in the underperforming Information Technology (IT) (-0.8%) and outperforming Consumer Discretionary sectors. From the IT sector, the Fund was overweight stocks with positive free cash flow, namely Codan (+39.1%) and Hansen Technologies (+47.3%), while being underweight the unprofitable Megaport (-22.2%). In the Consumer Discretionary sector, the Fund was overweight Harvey Norman (+26.4%) and Eagers Automotive (+7.1%), plus underweight Kogan (-36.1%). Offsetting, to a certain degree, some of these gains were an underweight to PointsBet (+4.5%) and Flight Centre (+13.5%). Further trimming some of the Fund's outperformance were some poorly performed overweight stocks in the Industrials sector, including NRW Holdings (-31.4%), McMillian Shakespeare (-9.9%), and Monadelphous (-21.1%). The Fund also suffered from underweight holdings in the Financials sector, namely Zip Co (+39.5%), Virgin Money UK (+44.7%), and Pinnacle Investments (+31.6%). This underperformance was partly offset by an overweight in Platinum Asset Management (+25.7%) and an underweight in Omni Bridgeway (-18.4%).

Alpha Signal Attribution

The Blue Orbit Systematic Alpha process combines four individual Alpha Signals – Quality, Trend, Defensive and Value developed using proprietary internal quantitative research processes. The four individual Signals are well diversified with low to negative correlations, and designed to outperform in differing market environments.

The Diversified Alpha Signal is the combination of the individual underlying Alpha Signals, and forms the main input into the formation of the Systematic Alpha Model. In turn, the Fund trades towards the model portfolio provided by the Systematic Alpha Model. This model is a theoretical target, and its returns do not include fees or transaction costs.

Alpha Signal Returns	3 Months Return	3 Months Excess
S&P/ASX Small Ordinaries - Total Return	2.09%	
Blue Orbit Alpha Signal Returns ¹		
Quality Alpha Signal	2.78%	0.69%
Trend Alpha Signal	9.60%	7.51%
Defensive Alpha Signal	2.58%	0.49%
Value Alpha Signal	2.25%	0.17%
Diversified Alpha Signal	4.54%	2.45%
Systematic Alpha Portfolio (Model)	5.57%	3.48%

1. Returns shown are for theoretical, calculated Signal and factor portfolios, and are not live or investible products. Returns are calculated using FactSet, and do not include any fees or transaction costs.

Given the design principle of the Fund, regardless of the market conditions the expectation is that a majority of Alpha Signals will outperform, thereby minimising the effects of any underperforming Signal(s). During the March quarter the Trend Signal was the standout performer (outperformance of 7.5% over the Benchmark). With the exception of the Value Signal, the remaining Signals generated modest outperformance. The outperformance of the various Alpha Signals, and the Trend Signal in particular, drove the outperformance of the Diversified Alpha Signal for the quarter. The March Fund rebalance involved a modification to the portfolio construction process where the Value Alpha Signal's weighting was reduced within the overall Diversified Alpha signal. The decision was based on Blue Orbit's signal timing research, which indicates that the recent outperformance of value stocks is unlikely to continue as markets normalise post the two significant step-ups in 2020.

Defensive Alpha Signal

In a turbulent quarter, the Defensive Signal was true to label generating modest outperformance. Assisting the Signal's performance was the strong lift in dividends in the Signal's investment universe during the February reporting season. Allocation and stock selection were equally responsible for the Signal's outperformance. The allocation gains came from underweights position in Healthcare and Materials, and an overweight allocation to the REIT sector. Countering these gains was an overweight allocation to the Industrials sector. Headlining the stock selection gains were certain overweights in the Consumer Discretionary and Industrials sector, namely Harvey Norman, Premier Investments (+12.5%), Super Retail (+15.1%), and Reece Limited (+11.6%). Mitigating some of the outperformance were underweight positions in travel stocks (Flight Centre, SeaLink Travel (+38.2%) and Corporate Travel (+12.1%)) and being overweight the poorly performed CIMIC (-39.7%) and Service Stream (-27.8%). Poor positioning -- overweight gold and underweight rare earths and iron ore -- in the Materials sector was detrimental for the Signal's performance. Also diminishing performance were underweight positions in the financial stocks, Virgin Money UK and Zip Co.

Quality Alpha Signal

The Quality Alpha Signal had a mixed quarter, and ended March with a slight outperformance. However, ultimately selection gains more than compensated for allocation losses. Overweight allocations to the Industrials and IT sector, and an underweight to the Financials sector were the main contributors to the sector underperformance. The largest selection gains came via the Healthcare and IT sectors. The largest contributors within the Healthcare sector were ProMedicus (+21.2%) and Clinovel Pharmaceuticals +21.3%) (both overweight positions) and an underweight in Polynovo (-30.2%). Further outperformance gains came from the overweight IT stocks Codan, and Hansen Technologies, and underweight Megaport. On the negative side of the ledger, the Signal missed some of the larger outperformers in the Materials sector, specially Lynas Rare Earths (+55.0%) and Iluka Resources (+11.4%), while being overweight gold producer Silver Lake (-16.5%). The overweight Consumer Discretionary sector holdings of Temple and Webster (-17.8%), Kogan (-36.1%) and Red Bubble (-13.5%) contributed to the reduction in the Signal's outperformance.

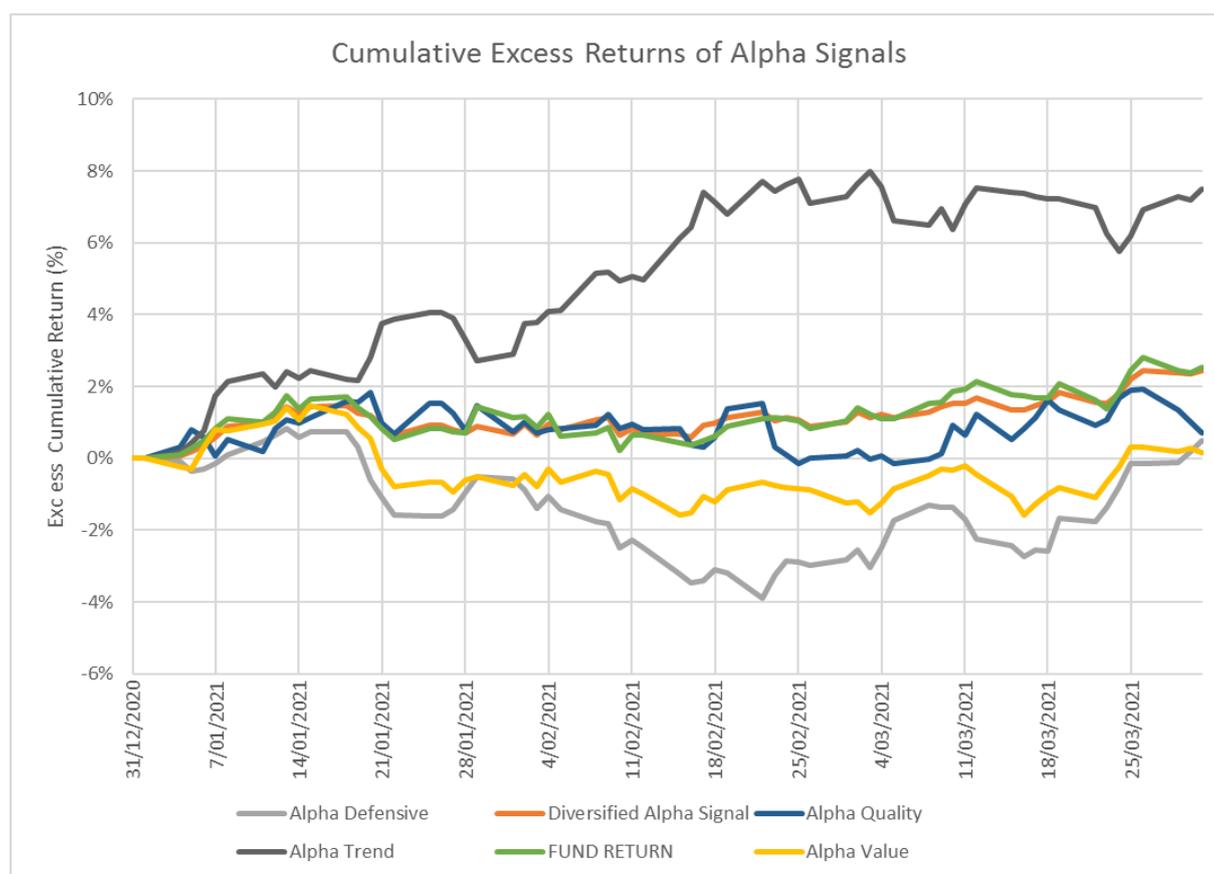
Value Alpha Signal

Going into the December quarter, the market conditions were such that the Value Signal's contribution to the portfolio construction process was increased. However, by the end of the March quarter market conditions had changed and the weight of the Value Alpha Signal within the Diversified Alpha Signal was gradually reduced to zero. The decision to wind back the Signal's contribution comes from Blue Orbit's research, which shows that unlike other global markets, Australian small cap value stocks tend to have shorter, intermittent periods of outperformance, and that Value should only be turned on when our signals indicate that we are in such an environment. Therefore, by the end of March, Blue Orbit determined that conditions indicate that Value should be switched off within the overall process.

In terms of performance during the March quarter, the Signal's relative performance was effectively flat. Nullifying the outperformance from stock selection was the Signal's sector allocation. The main allocations losses were an over (under) weight to the Industrials (Financials) sector. Healthcare and IT sector selections drove the stock selection gains. Noticeable selections gains were underweights Polynovo, Nanosonic (-29.0%) – Healthcare, and overweight Hansen Technologies, and underweights Megaport and Brain Chip (-21.8%). Selections from the Materials and Financial sectors proved problematic, including underweight positioning in Lynas Rare Earths, Zip Co, and Virgin Money UK.

Trend Alpha Signal

The Trend Signal had a very strong quarter due to its overweight positions in many of the quarter's outperforming stocks. The Materials, Financials, and Consumer Discretionary sectors were the major sources of the stock selection gains, however the signal outperformed across every GICS sector with the exception of Health Care. Within the Materials sector, the Signal was overweight iron ore and rare earth miners Lynas Rare Earths, Mineral Resources (+33.4%) and Pilbara Mining (+167.1%). While in the Consumer Discretionary sector, it was overweight a host of travel related stocks, for example Sea Link and Corporate Travel, plus overweight in ASX100 entrant IDP Education. Outperforming overweight positions from the Financials sector included Virgin Money UK, Zip Co, and Credit Corp (+80.3%).



Source: Blue Orbit. FactSet

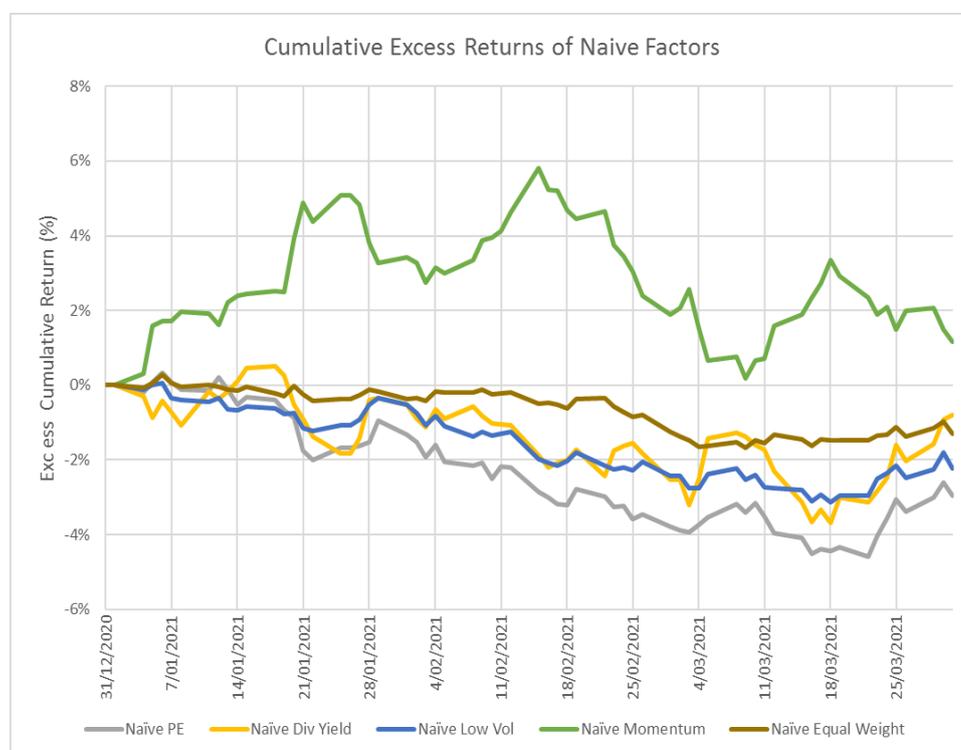
Diversified Alpha Signal

Consistent with the strong across the board performance of the individual Alpha Signals, the Diversified Alpha Signal outperformed over the quarter. Stock selection was the driving force behind the outperformance, with gains mainly coming from the Materials, IT and Consumer Discretionary sectors. Standout selections included an underweight to Resolute Mining (-44.7%) and Megaport, while being overweight Champion Iron (+63.1%), Codan, and Hansen Technologies. However, the signal was underweight travel stocks and rare earth miners, thereby costing some outperformance. Further tempering the performance gains was an overweight allocation to the Industrials sector and an underweight to the Financials sector.

Naïve Factor Returns

Naïve Factor Returns	3 Months Return	3 Months Excess
S&P/ASX Small Ordinaries - Total Return	2.09%	
Naïve Factor Returns ¹		
Naïve Dividend Yield Factor	1.30%	-0.79%
Naïve Equal Weight	0.79%	-1.30%
Naïve Low Volatility Factor	-0.15%	-2.24%
Naïve Momentum Factor	3.24%	1.16%
Naïve PE Factor	-0.87%	-2.96%

1. Returns shown are for theoretical, calculated Signal and factor portfolios, and are not live or investible products. Returns are calculated using FactSet, and do not include any fees or transaction costs.



Source: Blue Orbit. FactSet

The returns for the naïve factor portfolios were rather unexceptional for the month. Their underwhelming performance contrasted with the strong outperformance of Blue Orbit's Alpha Signals, thereby reflecting the value of the Blue Orbit investment process over a more traditional simple factor approach.

The thematic of investors backing winners and an increasing appetite for dividends underwrote the outperformance of naïve momentum and dividend yield factors. A more noticeable performance (or lack thereof) came from the equal weight portfolio. In the preceding 12 months, this factor had recorded much stronger performance, driven by the market bounces in April and November. However, for the Equal Weight factor within Australian Small Caps, these periods of outperformance tend to be an exception rather than the rule, with Blue Orbit research identifying that the outperformance of the factor generally only corresponds with periods of rapid market appreciation. Clearly, the March 2021 quarter did not meet these requirements.

Conclusion

With the ramifications of the COVID-19 pandemic still reverberating through the global economy and stock markets, investors faced a volatile quarter. While it is unlikely to be the last period of volatility for the immediate future, investors appear generally predisposed to a risk on stance. Reflecting this point is the general downward trend in market volatility and the market's ability to rebound quickly after each sell-off. Looking forward, the recent strong reporting season, high commodity prices, and ongoing stimulus provide a solid foundation for the upward trend in the Australian small-cap market. The two caveats to this statement are that bond investors trigger a more sustained "taper tantrum" or the increasing rate of COVID-19 mutations overwhelm the vaccine rollouts in the major economies.

As demonstrated across the previous 12 months, the design of the *Blue Orbit* Australian Small Caps Systematic Alpha investment process can navigate a variety of market scenarios. Therefore, investors can retain a high-degree of confidence that their investment is in safe hands. Furthermore, the team continues to work through an extensive research agenda to assist in fine-tuning the investment process with the aim of generating even greater outperformance going forward.

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