

WS Lancaster Absolute Return Fund

Portfolio Manager Q3-23 Report

Introduction

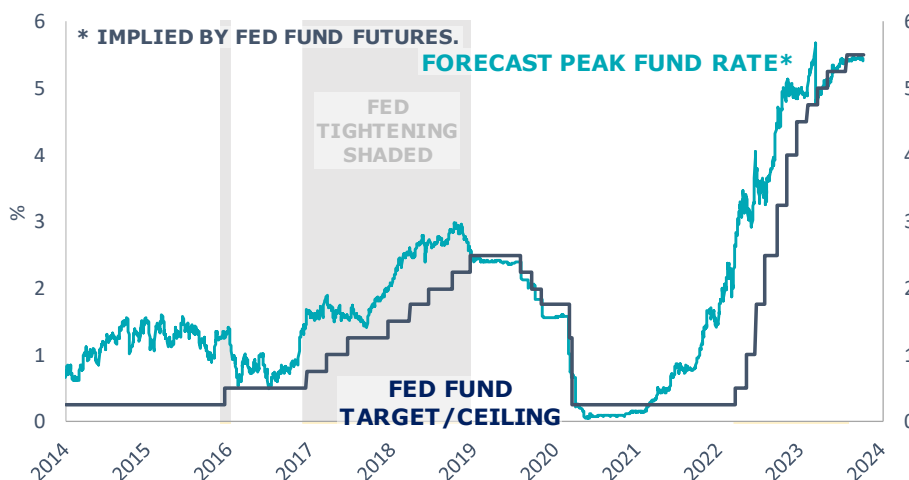
It was a good quarter for the fund, up +6.6% versus the MSCI Daily TR Net World Index +0.7% over the same period, with both long and short books making positive contributions. Performance would have been stronger if the fund had not been operating with reduced leverage for much of the period due to prime broker restrictions. By the end of the quarter though our financial third-party relationships were all working normally, the fund and investment team had successfully moved across to Lancaster Investment Management LLP and the fund exposure and trading was where we wanted it. Generally, equity markets struggled to make progress over the quarter with a backdrop of rising yield curves and weak Chinese macro.

Whilst we would not have chosen to have gone through the experience of the past few months there have been some positives to take away from it. Retrenching to high cash levels is always a healthy process to go through as you remove any emotional tethering and once the frictional cost of exiting positions has been spent it allows you to just focus purely on fundamentals. There have not been any material changes in the portfolio but we will not be re-entering into any of our micro caps and our gross exposure probably structurally reduces by c.10% as we try harder than ever to refocus on only our highest conviction ideas. It is also worth saying that having now all spent time working in the Lancaster offices we are delighted to have made it our new home.

Macro

It was a quarter where the US economy continued to surprise to the upside. This resulted in a strong quarter for the dollar, rising yield curves and rising real rates as inflation generally came down faster than expected. It is astonishing to step back and remind ourselves how large the upgrades have been for peak rates this cycle. Despite seeing the cost of capital rise so sharply the market absorbed it calmly with most financial volatility being very subdued over the summer months.

Exhibit 1: Fed target and peak rate priced by Fed Fund Futures (%)



Source: Minack Advisors

Performance

4.0% Monthly performance
-4.7% Year-to-date performance
11.6% CAGR since inception

These figures refer to the past. Past performance is not a reliable indicator of future results.

Fund details¹

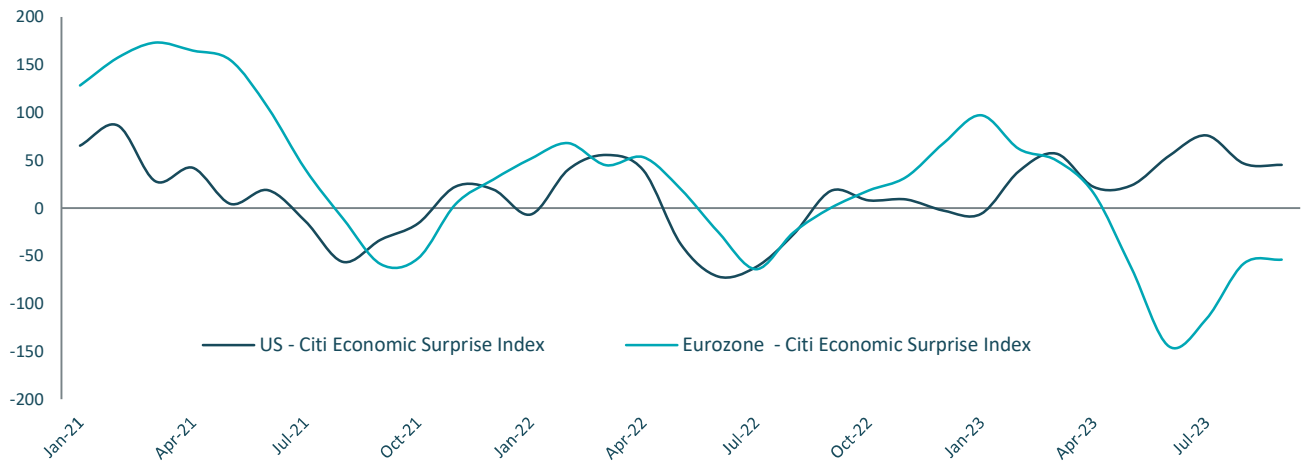
£ I Class	486.8
£ R Class	455.5
\$ I Class	2.71
€ I Class	2.65
Fund Size	£385 million
Strategy AUM	\$1,146 million
Fund Inception	11 May 2009
Class Inception	11 May 2009
Fund Type	UK Long Short UCITS

Portfolio Managers

James Hanbury
Jamie Grimston

The economic surprise index of the US which was positive throughout the quarter was in sharp contrast to the Eurozone.

Exhibit 2: US and Eurozone Citi economic surprise indices

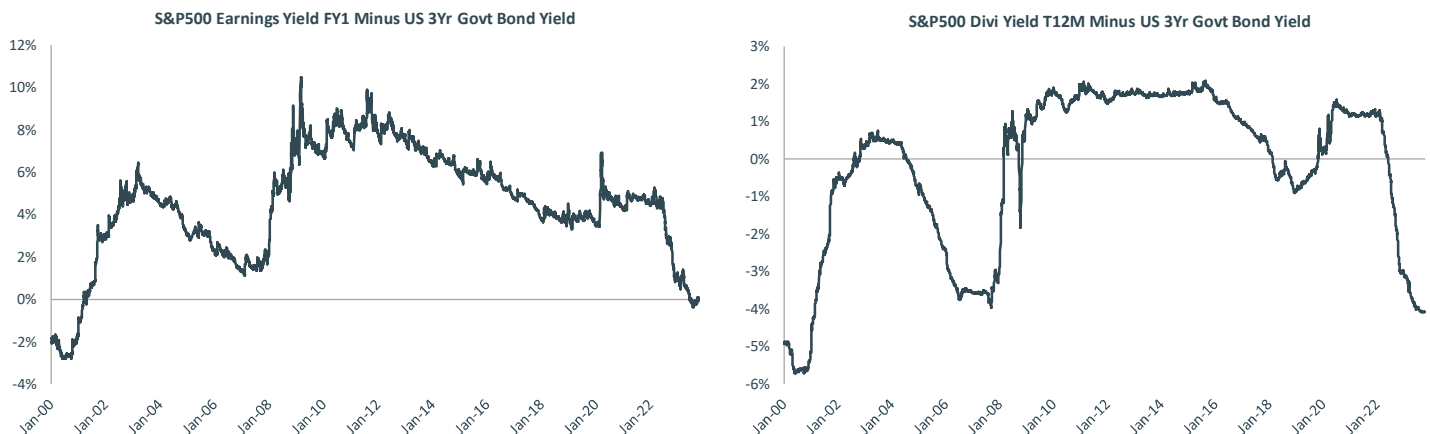


Source: Citigroup, Bloomberg

Some of the relative economic weakness in Europe is linked to weaker goods exports and lower business and residential investment. That said the US and European consumer has reacted very differently to the period of weak real earnings. The US consumer has drawn down savings much more than the consumer in Europe, likewise the US government has also helped growth more by running a larger fiscal deficit this year; c.4% of GDP higher than Europe. Both are behaviours that can't be regularly repeated and are essentially pulling forward demand. We generally prefer the political set up in Europe versus the US, where it is proving to be quite dysfunctional. A future headwind unique to the US is that student loan payments (principal and interest) will start in October after a 3 year holiday. These student loans represent \$1.6 trillion in aggregate with 43m borrowers and average payments will be \$413 per month. A consumer survey done by the Federal Reserve last year found that 37% of Americans lacked the savings to cover an unanticipated \$400 expense. What we don't know is how well consumers have factored this in.

Generally, a stronger than expected economy should be a good backdrop for equities yet the US stock market is not well set up for a 'higher for longer' rate environment due to the starting point of its headline multiples. Furthermore, the US stock market now has strong competition for capital from cash. For many years now QE drove the mentality of 'there is no alternative' but the charts below show this now not to be the case. Equity risk premiums have fallen dramatically and the spread between earnings yields and dividends vs cash returns have now gone negative. In the short term the market focuses on quarterly results yet with yield curves where they are, there is now a structural weight on the market for the first time in many years. We believe the US stock market is far more vulnerable to higher rates than Europe due to the difference in the relative multiples of each market.

Exhibit 3: spread between the earnings yield (l) and dividend yield (r) of the US market and the 3 year cash rate from 2000

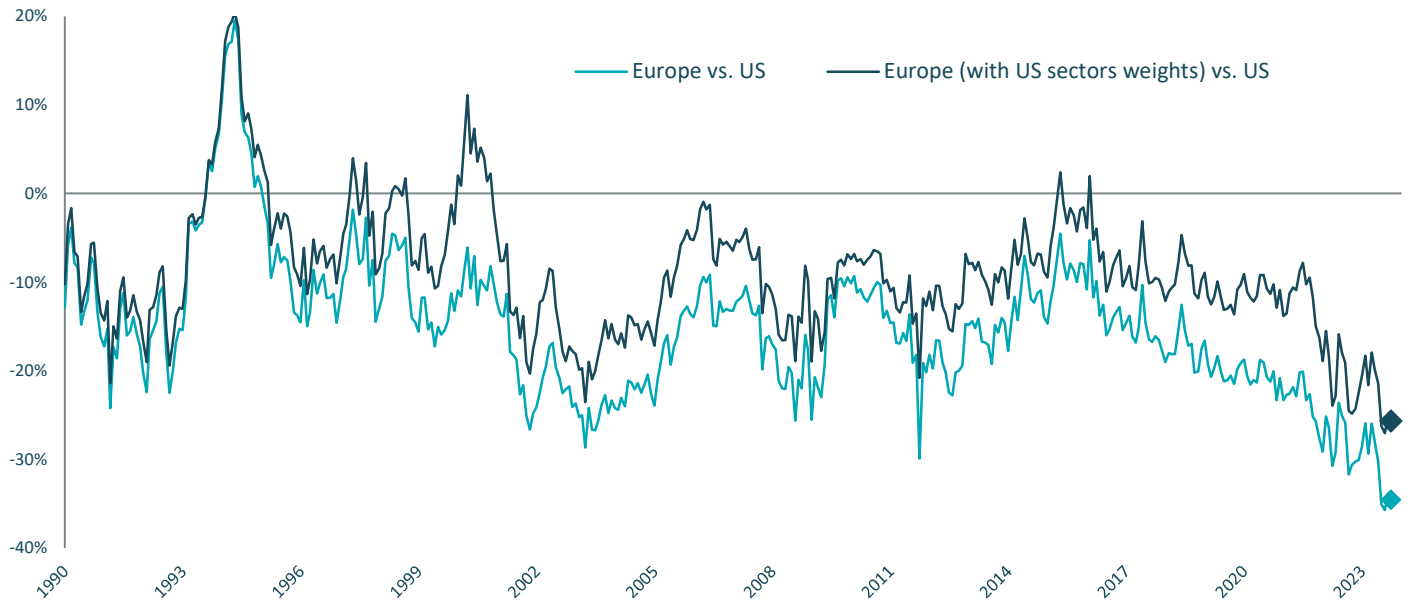


Source: Bloomberg

Historically the US stock market has a -65% correlation with the 10-year yield, but so far this year it has been a positive correlation of +56% which has created the move seen in the charts above. Only in the past few days of the quarter did the market seem to be starting to price in the higher cost of capital.

When looking at valuations Europe trades at a record discount to the US.

Exhibit 4: European PE discount to the US, headline and sector weight adjusted

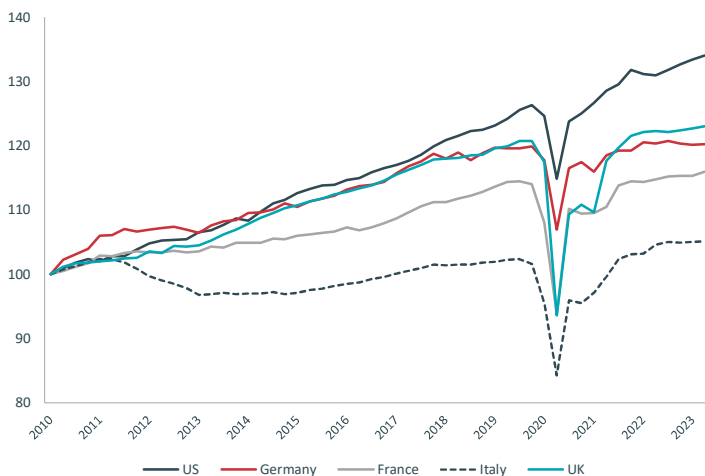


Source: Goldman Sachs

The UK had a good quarter from a macro perspective. Inflation crucially has fallen faster than expectations. This was important as there was a bear chorus saying that due to Brexit UK inflation would surprise to the upside this year. The UK also saw some major GDP revisions from the ONS which marked up post-COVID growth by c.2% and this is meaningful as it shows that the UK growth has in fact been ahead of the European average since the beginning of COVID. Exhibit 6 below is also a surprising reminder for some of how UK growth compares to other major western economies since 2010.

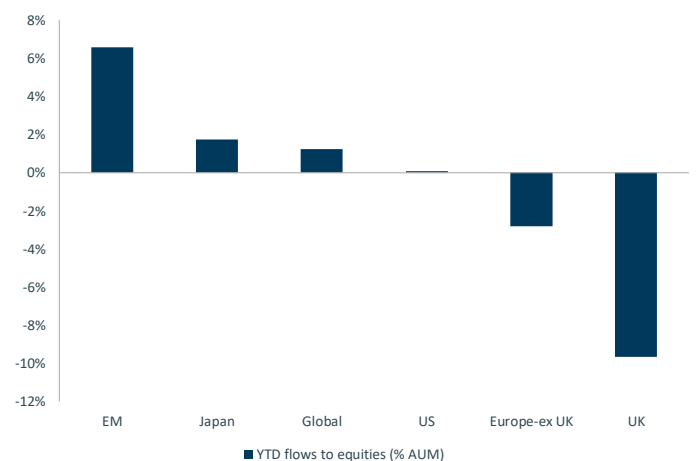
In the last quarter of this year UK real disposable income turns positive and is forecast to be c.2% for next year. Given the fundamentals and the valuations we continue to have a large overweight to Pan Europe and an underweight to the US. Exhibit 7 below shows how Europe continues to be unpopular with investors, with the UK being at the bottom of the pile, this clearly highlights the opportunity with a high wall of worry to climb.

Exhibit 5: selected countries real GDP growth 2010–23 (2010 Q1 = 100)



Source: Lazarus Economics

Exhibit 6: UK has seen the biggest outflows among the major regions ytd



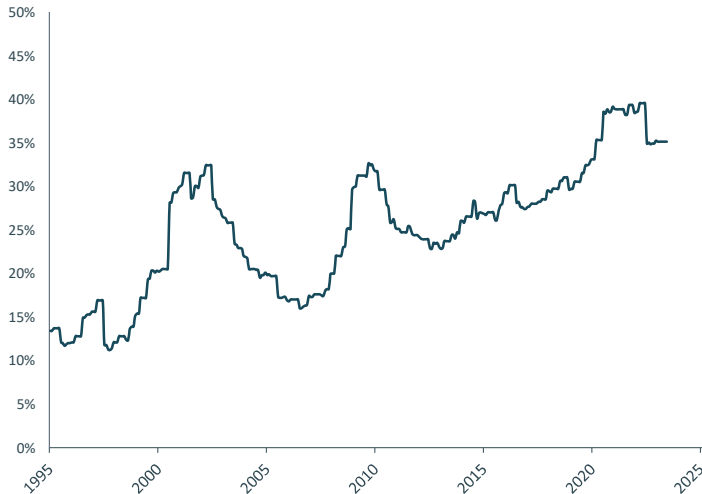
Source: Barclays, EPFR

We have always used index futures as a minority percentage of our short book, and the choice of future has added value. During this year we have shifted most of our exposure towards the Russell 2000, whereas it was the Nasdaq in 2022. This is partly as we are relatively less confident on US domestic growth but also the index trades on a 21x forward PE multiple with 40% of the companies in the index being loss-making. On top of that nearly half of the

loss-making companies have net debt. Whilst the refinancing profile of the Russell 2000 looks fine in isolation, the concerns are more around covenants particularly with 31% of the debt being floating. This is consistent with a June 2023 research paper written by the Federal Reserve economists which stated that 37% of non-financial companies in America are in 'financial distress', which is defined as close to default. Not a great set up for a QT world.

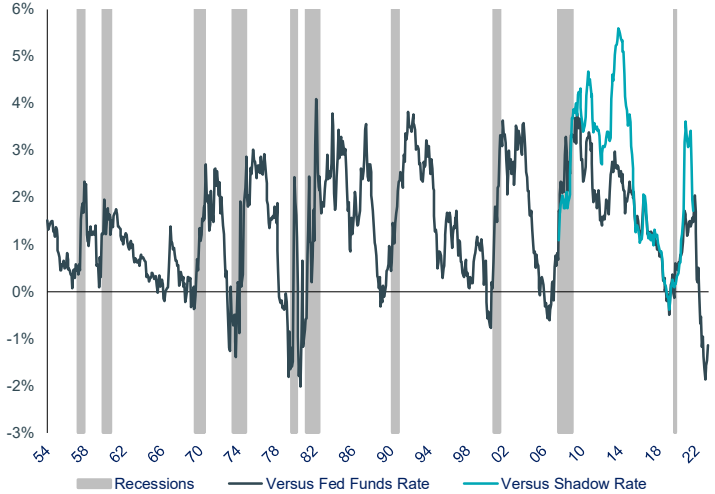
Whilst the market has become more relaxed about a hard landing in the US we feel that the higher yield curve increases the probability of meaningful stresses developing in the economy. There are very few indicators that have a decent track record of predicting recession, the inverted yield curve is one of the few so a smooth glide path from here would defy history.

Exhibit 7: % of companies that are loss making in the Russell 2000



Source: Goldman Sachs

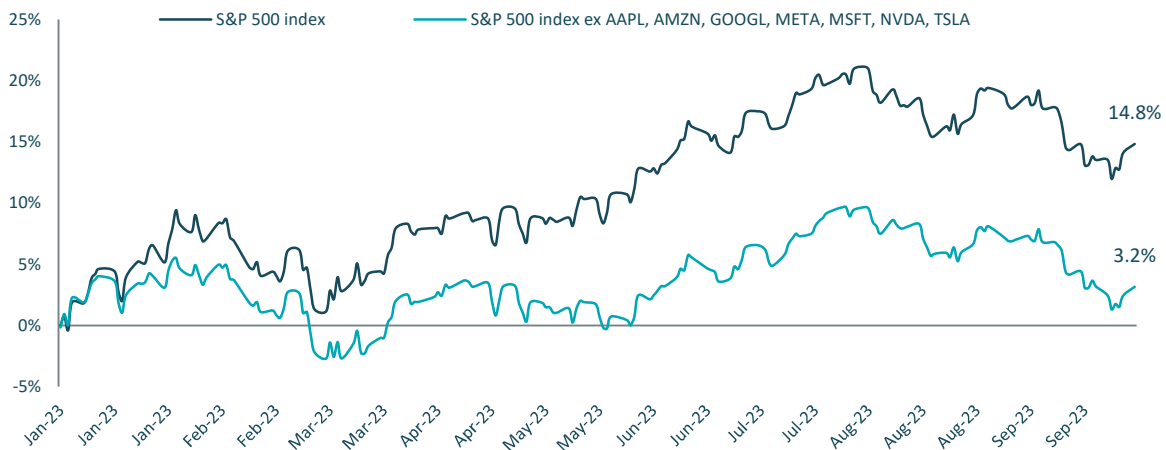
Exhibit 8: 10Yr Bond Yields vs. Federal Funds & Shadow Rates 1954-2023



Source: Federal Reserve Board, Federal Reserve Bank of Atlanta, Bureau of Economic Research.

It has clearly been a large headwind for the fund this year but we continue to believe that European stock markets are providing much better opportunities than those in America. It is astonishing how the 'Magnificent 7' have provided all of the positive performance in the S&P500, we do not currently own any of them and find their multiples (average forward P/E 38x vs. consensus EPS growth 27%) hard to justify.

Exhibit 9: S&P500 cumulative YTD 2023 return with and without the Tech Titans contribution



Source: Bloomberg

Every rising rate cycle there are particular sectors of the economy that face a crisis with varying degrees of significance. We continue to believe that the broader private equity space is among the most vulnerable this cycle; and we see an increasing probability that private equity's problems cause considerable collateral damage to the rest of the economy. In our view the market continues to underprice this risk.

The scale of the private equity industry is systemic with greater than \$21trn exposure across equity and debt in private equity, private debt, infrastructure, and real estate funds. Growth has been exuberant with a CAGR of 15% over the past ten years, accelerating to 17% over the last five years and to 22% over the last three years. Against this backdrop of unprecedented scale and late-cycle growth, we note that all the major factors driving a 30-year secular

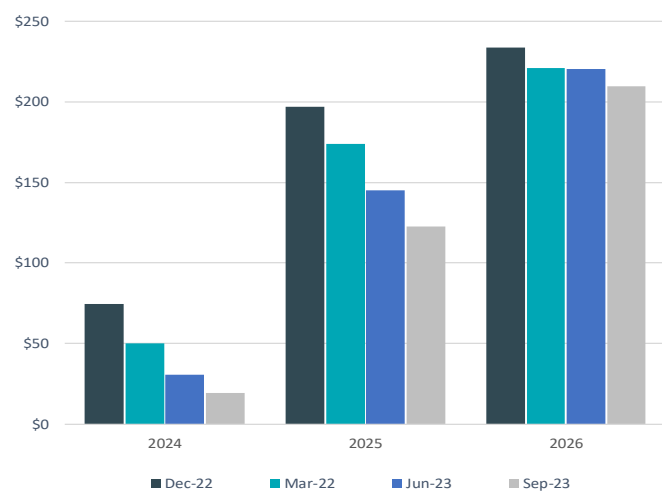
bull market across the economy have now reversed: falling rates, increased access to credit on ever more favourable terms, and increasingly generous valuations.

Straightforwardly, the current situation of rising rates and widening credit spreads challenges the private equity business model. It is now materially more expensive for these businesses to finance or refinance their deals; and as valuations and cash flows come under pressure from higher cost of debt, the equity valuation in leveraged companies gets squeezed. Generally, over the past cycle the private equity industry has made investments where valuations are most exposed to rising rates; technology, biotech, real estate, infrastructure and renewable energy. Meanwhile, we estimate floating rate debt accounts for over 70% of borrowings from private equity-linked companies.

The industry did well to exploit low rates and refinance much debt around COVID; but in our view it is poorly understood that this was only a temporary and partial fix, and that over the next 12 months from here, the industry will start to face a wall of refinancing requirements that will last for the next several years. Also, commentators often seem to overlook the fact that in order to be signed off as a going concern, a borrowing corporate must refinance its debt 12 months in advance of maturity.

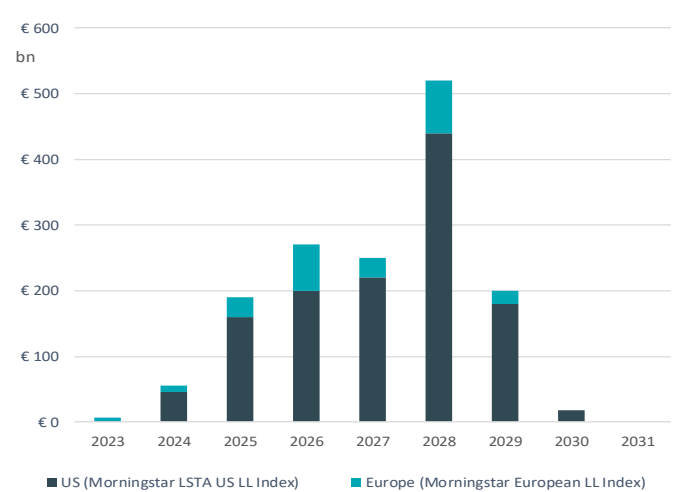
Accordingly, we take little reassurance from the successful deferrals of maturities in 2023-24, and instead focus with concern on those in 2025. These are the important ones that will set the trajectory for the private markets industry from here and threaten the economy more broadly. We note for example that outstanding leveraged loans due to mature 2025 today are c.67% higher than were 2024 maturities four quarters ago.

Exhibit 10: US leveraged loan maturity wall (2024-2026)



Source: Morningstar LSTA US Leveraged Loan index; Pitchbook LCD as at 22-Sep-23

Exhibit 11: Leveraged loan outstanding maturity profile



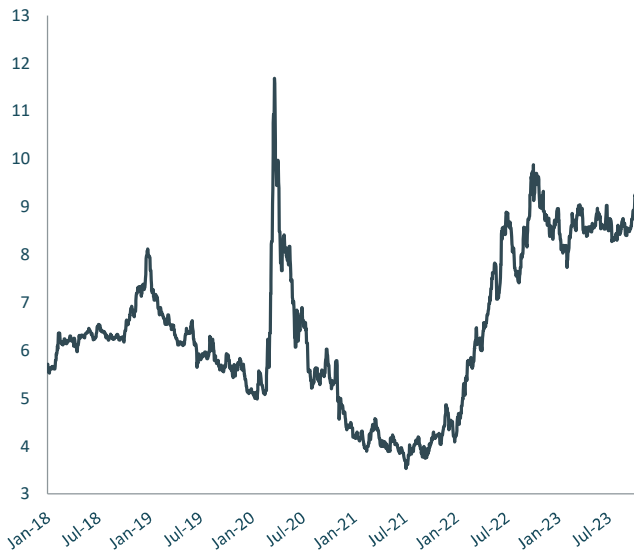
Source: LCD as of end Mar-23

It is also worth pointing out that the debt which matures in 2024 and still needs to be refinanced has probably not been addressed so far for good reason. Regional banks in the US, which have become more cautious since their funding crisis earlier this year, were over-represented in supplying the leveraged loan market. High yield spreads have started to widen in the past few weeks, and when stacked on-top of the risk-free rate, the increase in the cost of refinancing over the past 2 years is very meaningful. It is no surprise therefore that we are seeing increasing signs of stress in the refinancing behaviours of private equity managers. Whereas previously, debt was isolated against each individual company in the portfolio, we are now seeing that in order to complete their refinancings, private equity firms are needing to offer lenders the entire portfolio as collateral in so-called NAV loans. To our mind this is a breach of trust with the LP as to how the model was meant to work: damage from poorly performing companies was meant to be isolated.

It is impossible to quantify the potential impact of a private equity crisis. However, we believe it is inconceivable that with exposure representing c.21% of global GDP (ranking between China and the US in terms of global importance), the contagion risk would not be meaningful. There are several private equity shorts in the fund and we touch on the micro elements in the stock section of this report. Meanwhile we are doing more work on the potential wider ramifications of a private equity crisis. If press reports are accurate then CVC is due to launch its IPO imminently. It is always interesting to see when industry insiders want to sell.

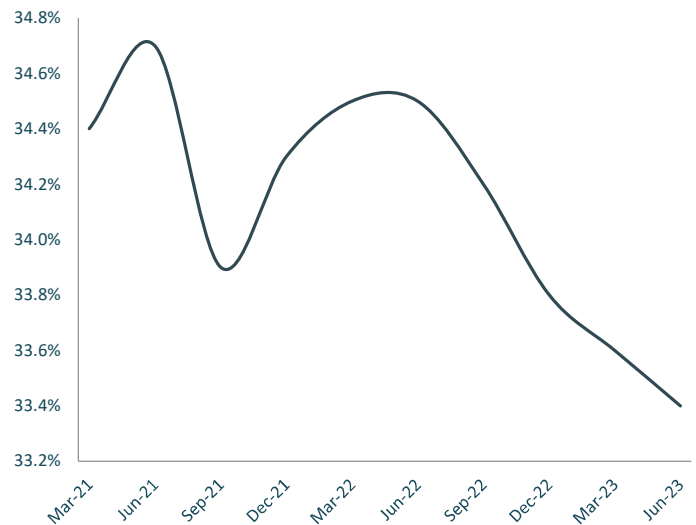
China has fallen out of sync with the western economies. Consensus, including us, expected it to bounce back much stronger from COVID this year when actually COVID rebound waves were more impactful than expectations. China has also suffered from western economies shifting their spending marginally away from goods and back into services. This phenomenon has also been helpful at supporting western labour markets given that the service sector is more labour intensive.

Exhibit 12: US Corporate High Yield Yield to Worst (%), Jan-18 to Oct-23



Source: Bloomberg

Exhibit 13: US goods as a share of PCE

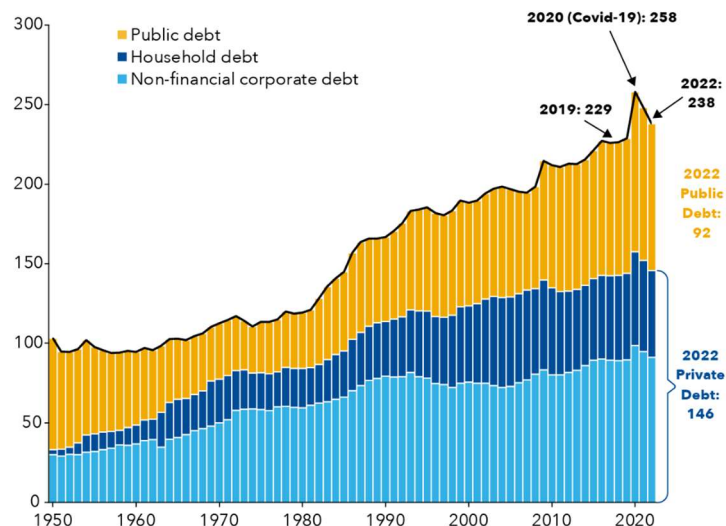


Source: Goldman Sachs

In terms of forecasting the China macro we put it into the 'too hard' bucket and we are well aware it has the ability to surprise meaningfully both ways. Given the depressed activity in Chinese real estate we actually find it quite bullish for copper given how well it has held up. The Chinese economy is regaining some momentum after policy support and if this does gain real traction it will clearly be an inflationary force globally.

We are finding the inflationary debate more complicated. It is easy to draw parallels to the 70's and we do have some sympathy with this. That said the stock of debt in the system is materially higher than what we saw in the 70's and so interest rate rises have the potential to cause much more stress in the financial system (private equity, LDI, regional banks...). One argument is that this simply means that central banks are forced to keep rates lower than expected to avoid potential crisis. The counter argument is that is central banks could be slow to recognise a crisis emerging and damage becomes too embedded unleashing deflationary forces for a period of time. Another good reminder of why we are pleased to have our primary edge coming from stock picking.

Exhibit 14: Global debt as a percentage of GDP



Source: IMF Global Debt Database

As a summary we prefer the macro and valuation set up in Europe compared to the US and we also feel incrementally more nervous about systemic issues surfacing after this extraordinary period of rising rates. Both of these views are represented in our positioning.

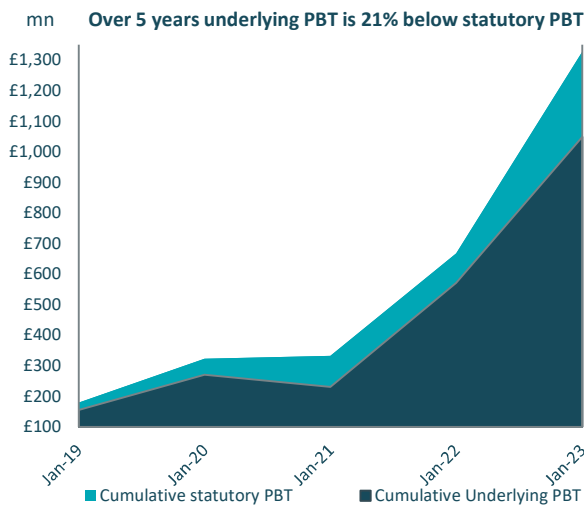
Fund performance and positioning

Both the long and short book generated positive returns for the fund in Q3-23 linked to strong alpha generation on both sides of the book.

Long book

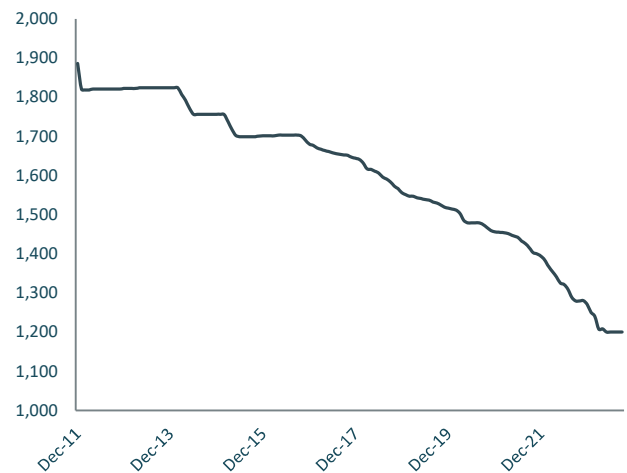
Frasers Group was our top contributor for the quarter after strong results and outlook at its full year update. Frasers Group find themselves in rarified company among larger western retailers by guiding for 10% PBT growth for their next financial year. Whilst for many companies that we look at we take 'adjusted earnings' with a pinch of salt, Frasers Group has some of the most conservative accounting that we have come across, the output of which is shown below. The group is a beneficiary of QT also as the higher cost of capital and tougher retailing environment allows it to stand out from the pack and win share. We can see a long runway of growth ahead of Frasers Group and yet it trades on a forward p.e. 7x ex its investments and cash flow is often stronger than P&L earnings.

Exhibit 15: Frasers' accounting is conservative



Source: Frasers Group, Lancaster IM

Exhibit 16: Man Group, shares outstanding (m)



Source: Bloomberg

A new position we took in the quarter was **Man Group**. We know the business well and have been shareholders several times over the past decade. We have been impressed by its use of technology throughout the business and we admire the high barriers, stickiness and growth trajectory this brings. We also admire the company's excellent track record in capital allocation over many years. We believe that the fund management industry will increasingly polarise between the larger houses which can invest in and engage with technology, and more focused fundamental firms who are benchmark agnostic. There should be a virtuous circle for Man Group as it leverages its central investments, and its rare diversity and sophistication, to be able to offer bespoke solutions to some of the largest clients globally. This should result in Man winning a larger slice of the pie going forward. Meanwhile higher interest rates create a better environment for hedge funds given their absolute benchmark is zero; and positive absolute returns may not be so easy through passive solutions, easing a major source of competition in recent years. We were able to invest into Man Group on a forward p.e. ratio (2024) of 7x on our numbers, which we believe prices in very little for growth and performance fees we forecast. That is a very important point for Man's shareholder returns: the market has consistently put the performance fee on a multiple of 1 or 2 times and management has continuously arbitrated this by using it to de-equitise.

Exhibit 17: MAN Group (Long) vs. Private Equity shorts, relative valuations

	MAN Group	EQT	Partners Group
AUM (June '23, Fee Earning)	\$151.7bn	\$137.6bn	\$141.7bn
Enterprise value	\$2.7bn	\$24.1bn	\$30.3bn
Enterprise value / AUM	1.8%	17.5%	21.4%
Consensus AUM CAGR, 2022-26	12%	10%	9%
Consensus Revenue CAGR, 2022-26	2%	25%	14%
Consensus Perf Fees vs AUM (Avg), 2023-26	20bps	49bps	47bps
EV / Earnings 2024	6.8x	14.9x	21.6x

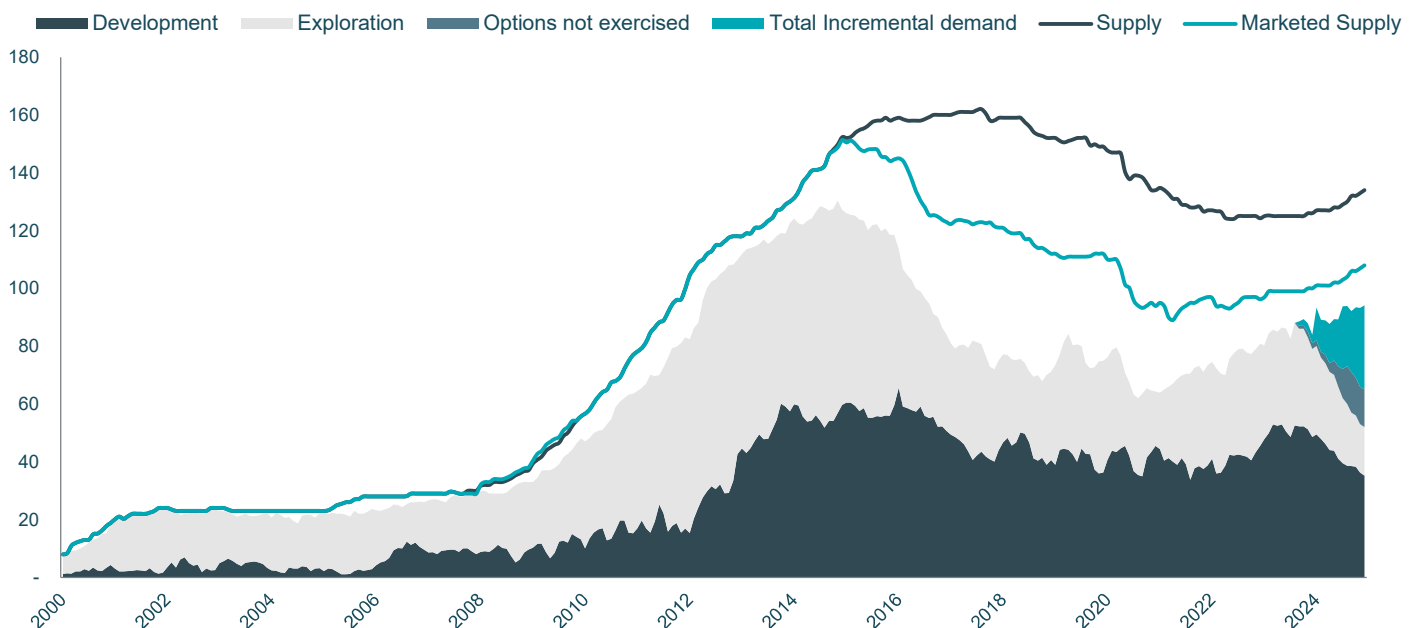
Source: Bloomberg, as at 29-Sep-23.

Although the performance fee is volatile, it is a consistent cash generator over the cycle for such a large and diversified firm. Over the last 10 years performance fees have represented c.30% of revenues and c.50% PBT for Man Group. Whilst we expect Man Group to move into a more favourable world with QT taking place, we believe the opposite is true for private equity houses (as discussed above). The market shows no reflection of our view though - as seen in the relative metrics in exhibit 17 above.

Ubisoft performed well in Q3-23 with the market potentially starting to view more positively its new game pipeline and its strategic alliance with Tencent. Regarding the pipeline, we were encouraged earlier this year by the feedback from and levels of gamer interest in the large-scale public testing of Ubisoft's upcoming free-to-play title XDefiant. More recently, on the paid game side, with The Crew Motorfest and Assassin's Creed Mirage, Ubisoft has begun once again to deliver consistently at high quality. There was also, what we regard as, a windfall for Ubisoft in the quarter as Microsoft signed a long-term deal to licence to it the cloud streaming distribution rights for Activision Blizzard's portfolio, most likely in order to get that acquisition over the line with the UK CMA. Finally, we feel that the market may finally be viewing more positively Ubisoft's long-standing strategic alliance with Tencent. We have long been encouraged by Tencent's willingness to build its stake in Ubisoft at levels above the prevailing share price (e.g. at c.Eur 80 per share in September 2022 vs a current share price of c.Eur 30). On top of this, however, in June Tencent was also identified as the licence partner investing significantly to take Ubisoft's key Assassin's Creed intellectual property into the mobile gaming arena.

Our oil exposed names had a good quarter helped by the oil price being up c.27%. **BP, Shell, Total** all performed well and **Valaris** additionally benefited from increasing its buyback target. It is a sign of the times when oil drillers are increasing capital returns rather than signing up newbuilds. Meanwhile, the supply/demand of deep-water drill ships looks as good as it has for a long period of time due to the lack of new capacity.

Exhibit 18: Ultra Deep Water rig supply/demand (number of rigs)



Source: DNB Markets, S&P Global

Vistry, our only UK housebuilder, updated the market with regards to its business model in September. It will focus on its capital light partnership model and will not continue with traditional housebuilding. The market is undecided on this strategic move but what is clear is how well Vistry is outperforming sector peers. Vistry earnings so far this year have been upgraded by 15% whilst the sector average has been downgraded by 12%. The shares trade on a 25% premium to Tangible Book Value, which looks inconsistent with target medium term KPI's (4 to 5 years out) of 5-8% revenue growth and a 40% ROCE and £800m of operating profit. In fact, factoring a capital return broadly in line with guidance, the shares would trade on a PE of sub 4X if management hit their targets. Meanwhile political parties seem keen to highlight that they would build more houses as a key election pledge. Vistry's bias to affordable housing certainly puts them in a good position if Labour were the next UK government.

Plus500 has had a tough year so far with the shares being down c. 25%. There have been a few drivers of this underperformance which do not concern us. Volatility in financial markets during the second and third quarters was low, and this is a key driver of activity and customer recruitment. We see low volatility as cyclical not structural, but it will clearly have an impact on those quarters' earnings. There was also a regulatory change in Spain with advertising prohibited for CFD trading, and we feel there is a reasonable chance that this gets rolled out across Europe in some form. As we saw in 2018 with ESME

regulatory changes it tends to favour the better positioned and larger providers. The strongest brands benefit in a world where there is less advertising. Plus500 as a multi-portal financial provider will also be able to continue advertising for its investing or futures division unlike its competitors. By having advertising restrictions, it increases the barriers to entry and reduces the 'Google tax'. Meanwhile Plus500 has launched its Japanese offering in September and the Middle East and US divisions should begin to generate material revenue growth in the next few quarters. As has been the case for many periods in the fund, we are long Plus500 and short IG Group. Given Plus500 has just passed its 10-year anniversary as a listed entity it is worth comparing the two companies.

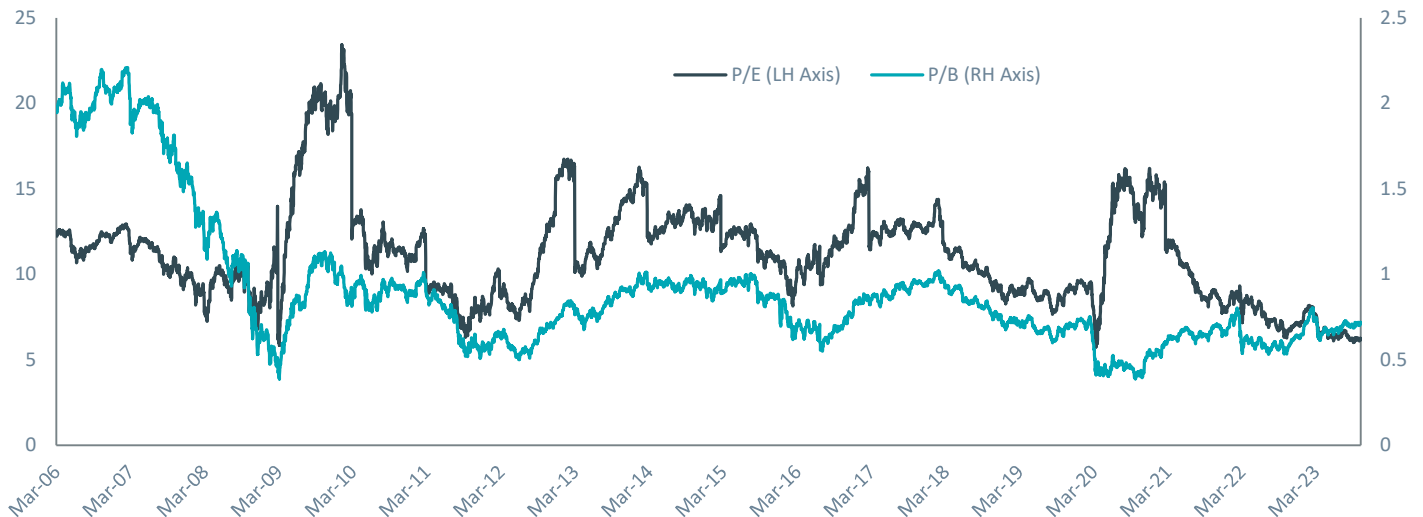
Exhibit 19: Plus500 vs. IG Group, relative valuations

	Plus500	IG Group
10-year stats:		
Marketing Spend Average % Revenue	25%	10%
Revenue CAGR, levered organic	23%	7%
Customer CAGR, levered organic	13%	3%
ARPU CAGR, levered organic	9%	4%
Average Operating Margin	57%	48%
Average ROE	95%	26%
% Share Count Change	-30%	13%
M&A Consideration	\$33m	\$1,000m
Current Stats:		
Surplus Cash % Market Cap	25%	20%
EV / EBIT (FY1)	2.6x	6.3x

Source: Bloomberg, as at 29-Sep-23.

We continue to have exposure to the European banking sector through **Commerzbank**, **Deutsche Bank**, **Barclays** and **Natwest Group**. As ever there are macro risks with banks but unlike our financial shorts we feel these are more than discounted and the opportunity for meaningful capital returns is very real. In fact, the European banking sector has never been so cheap.

Exhibit 20: Euro Stoxx banks index forward P/E (LH axis) and P/B (RH axis)



Source: Bloomberg

IWG has been a poor performer for the fund this year. However, for us the story has got more compelling, and we see three clear areas where the market is underappreciating the opportunity and value of the business.

- Wework is close to going into Chapter 11. Catalysed by a negative cost of capital, Wework has been extremely disruptive to pricing in the serviced office industry over the past six years; we estimate it may have reduced industry gross margins by c.300bps, along with other QE driven start-ups in the space. Wework now has a market cap of only \$151m versus net debt of \$2.7bn. It looks inevitable that either the

company goes into Chapter 11 and comes out as a much smaller business; or logically that IWG should be part of the solution, possibly by running the Wework sites for a fee and allowing Wework to reduce costs dramatically.

- The IWG capital light model is gaining traction. IWG is now signing up around 100 new centres a month for the capital light (franchising) division. Given there has been significant investment into this division, there is a hockey stick in forecast profitability with losses this year. We model that in 2025 and 2026 this capital light division should be generating EBIT of c. £70m and £115m respectively. Putting these figures on multiples of comparable franchise businesses would almost account for the entire IWG EV.
- Worka is a valuable business. Having acquired 85% of The Instant Group for £270m in March 2022 IWG merged it with some of its own assets to create a leading brokerage business that also offers technology and turnkey solutions for the serviced office industry. Both Instant and the IWG assets are high growth: Instant was growing revenues at a 20% CAGR and EBITDA at a 30% CAGR in the three years prior to acquisition. We believe this division could be worth the entire EV of IWG.

Yes, IWG is cyclical, but higher rates are starting to drive creative destruction among their lower quality competitors, and we have plenty of cyclical shorts which price in a much rosier outlook. If we are right on the evaluation of the IWG business as per the points above, then there are multiples of upside to the shares.

Vivendi has been another disappointing performer so far this year. Vivendi is currently finalising its takeover of Lagardere, whose key strategic asset is the book publisher Hachette. We have long felt that the book publishing industry has so far failed to capitalise on the full potential of mass-scale digital distribution, with the result that as many as one third of consumers in a market like the UK don't engage with books as a regular form of entertainment. We were therefore encouraged by Spotify's recent announcement that it has now reached agreement with all the largest global book publishers to begin offering its >200m subscribers 15 hours per month of audiobook content (with the cost seemingly borne at launch by Spotify itself). This announcement has the potential to both significantly grow the audiobook market and to improve the book publishers' negotiating leverage vs the current dominant audiobook distributor Amazon.

Our biggest detractor in the quarter was our long position in **Jet2** despite the company upgrading guidance during the quarter. The market is concerned about the climbing oil price and capacity coming back too strongly in 2024. Our two positions in the airline and package holiday sector are **Ryanair** and **Jet2** and in both instances they are material contributors to this growing capacity. On top of that we believe demand for package holidays and low-cost travel is structurally higher than pre-COVID. A JP Morgan survey showed that UK consumers are now 45% "more likely to choose a low-cost airline than before the pandemic". Jet2 is less exposed to the oil price with a 10% rise in the cost of fuel equating to a 1% rise in the cost of a package holiday. Ryanair meanwhile as the lowest on the cost curve has the greatest ability to ride out the increase. Jet2 trades on an EV/EBIT multiple of 3x for 2024 when we include only half of the customer cash and Ryanair trades on a p/e of 8.4x for 2024. Low multiples for structural market share winners.

'Everything has beauty, but not everyone sees it' (Confucius). Our job is to find companies that have better risk-adjusted prospects than the market is pricing in. The push back to our overweight in Europe and 'value' (and many of our names) is that we are backing lower quality companies. The empirical evidence would suggest otherwise. When comparing key consensus metrics of our long book to that of the market it would imply that we are paying a materially lower price for higher quality companies taking on less balance sheet risk. It is worth saying that all our metrics for the fund long book would be higher than what consensus is expecting in the table below.

Exhibit 21: KPI comparison – WS Lancaster Absolute Return Fund Long Book vs. MSCI World

	Forecast 12m revenue growth	Return on capital*	Net Debt / EBITDA	Forward P/E	Forward EV/EBIT	Forward EV/Sales
WS Lancaster AR Long Book*	4%	7.0%	0.4	9.7	7.7	0.7
MSCI World Index	4%	5.8%	1.4	17.5	16.7	2.2

*consensus data. ¹Lancaster Absolute Return long book median ROCE increases to 9% when banks are removed. Source: MSCI, Bloomberg, Lancaster IM, as at 29-Sep-23.

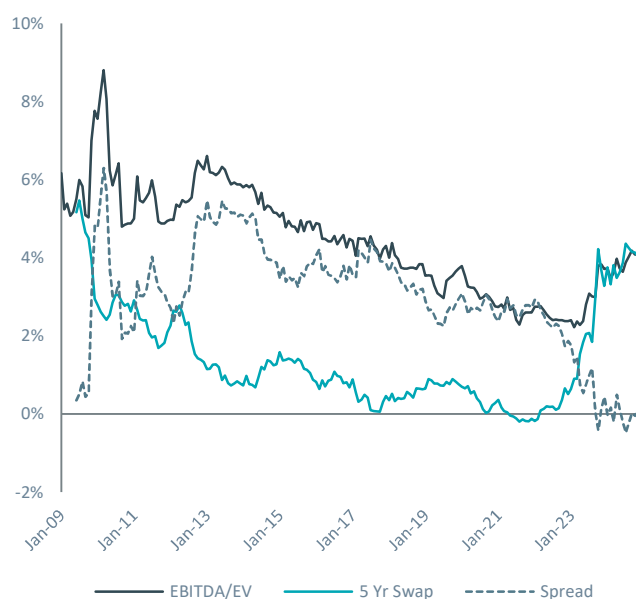
Short book

The short book made a positive contribution in Q2-23 with strong alpha.

Our index future short position in the Russell 2000 was our largest contributor as all other shorts were reduced in position size over the quarter while we migrated the fund to Lancaster and re-established relationships with our prime brokers.

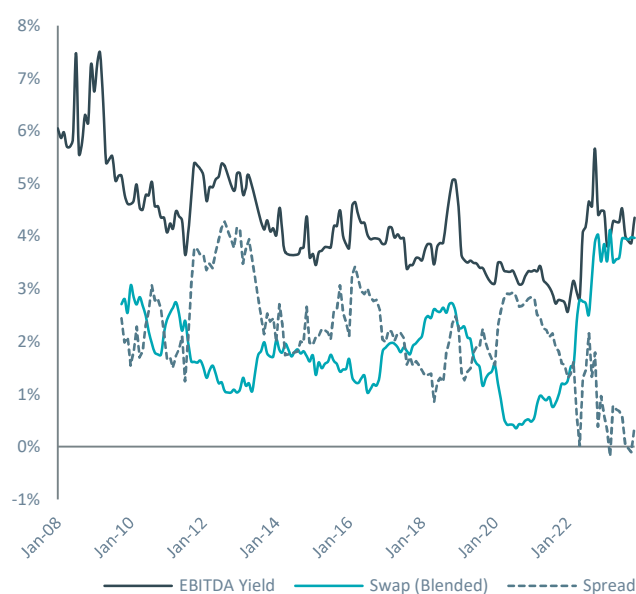
Our logistics property shorts performed well during the quarter but the market is still struggling to digest the change in facts. Despite falling over the past 2 years they have actually got more expensive compared to the move in the risk-free rate. The market is implicitly saying the risk-free rate is wrong (which can be hedged out) or these companies have become less cyclical with more pricing power over the past two years, which we don't believe to be the case. The sector remains a core short for the fund with **Segro** and **Prologis** as our largest sector positions.

Exhibit 22: Segro relative value



Source: Bloomberg & Lancaster

Exhibit 23: Prologis relative value



Source: Bloomberg & Lancaster

The Fund recently initiated short positions in **Deckers Corporation** and **On Holding**. The former is home to a small portfolio of footwear brands but its key growth engine is the Hoka running shoe brand that generates c.40% of its group revenue. The latter owns the On Running shoe brand. In our view, both of these brands have over the last few years benefitted from multiple significant exogenous demand tailwinds. Among these have been the running boom sparked by COVID-related lockdown orders, a potentially cyclical increase in runner interest in the very cushioned running shoe styles that particularly characterise these two brands and an apparent strategic de-prioritisation of the wholesale distribution channel by larger diversified competitors like Nike and Adidas. The confluence of these factors has contributed to drive the two brands' aggregate revenue from a base of c.\$600m (growing at c.\$250m p.a.) in calendar 2019 to a level of c.\$2.7bn (growing at c.\$1bn p.a.) in calendar 2022. We are however concerned about the sustainability of the exogenous tailwinds listed above and feel that some have the potential even to reverse into headwinds. Were that to happen, it would come at a time too when long-term investments into areas like store footprint expansion may make the cost bases rather sticky. Given the premium near-term valuation multiples, recent sales by insiders and near blanket sell-side analyst Buy ratings that currently characterise both companies, we feel that the real opportunity with them lies on the short side at this point.

We also started a new short position in **Rivian** during Q3-23 after a meaningful bounce in the shares. This is a successful short we have previously held where we feel medium term profit and market share targets are unrealistic. We covered **Diageo** as a short as the market started to price in our previously discussed more bearish thesis, particularly focused on the American market. In mirror image to our longs our short positions tend to have higher multiples and higher net debt ratios than the market.

Exhibit 24: WS Lancaster Absolute Return (LAR) Fund median consensus valuation multiples

	Forward P/E	Forward EV/EBIT	Forward EV/Sales
LAR Long Book	9.7	7.7	0.7
LAR Short Book	17.5	16.7	2.2

Source: MSCI, Bloomberg, Lancaster IM, as at 29-Sep-23.

Conclusion

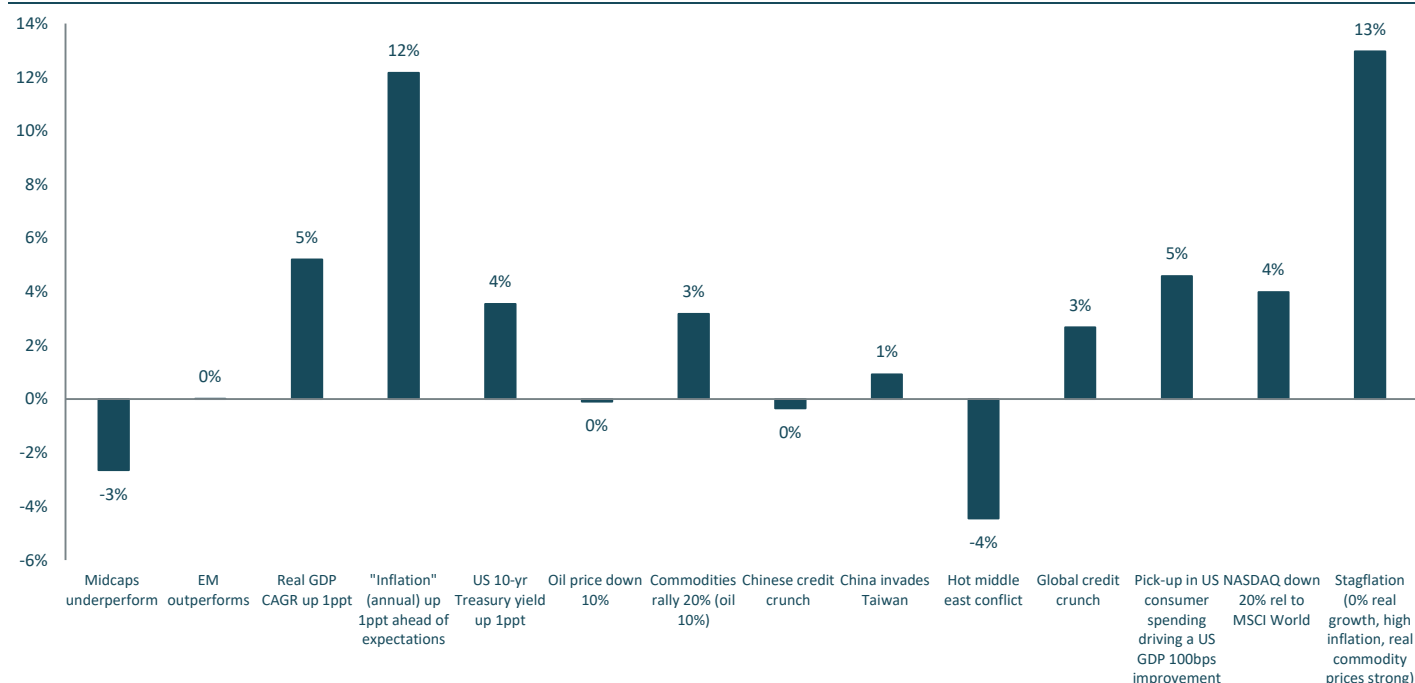
The Fund is currently broadly market neutral with a strong pan European overweight for our longs. When you combine the starting point for market multiples and the degree to which discount rates have risen we do not feel it is time when we want to be taking on much market risk. That said there are areas of the market offering what we consider to be extremely attractive entry points for high quality companies. We believe that during quantitative tightening stock picking should be able to add great value and strong brands and companies will stand out from the crowd. Our short book is more skewed towards the US and contains many unproven business models that are trading on high multiples.

The systematic risk in the fund is 62% and we are unhedged on our non-sterling positions except for our dollar holdings.

Whilst it is frustrating to have had returns impacted by reduced leverage due to exogenous events we are pleased that the Fund is now trading normally with position sizes where we want them. The investment team has hit the ground running at Lancaster with productivity and further improving the investment process being a renewed area of focus. We are very excited by the set up in the market and the opportunity set in front of us. Generally, markets are poor at pricing in unusual and extreme macro scenarios, and this creates inefficiencies in how companies are valued.

Lastly, and most importantly, we would like to thank you for your continued backing. We have been humbled by the support we have received over the last few months, we hope you can join our upcoming investor call and we look forward to updating you at the end of the year.

Exhibit 25: WS Lancaster Absolute Return (LAR) | Estimate factor return (relative) as at 13-Oct-23



Source: Lancaster IM unaudited internal data & Bloomberg, as at 29-Sep-23. Note: Assumes current currency hedging; The information above is an estimation of the expected factor return; Lancaster may make investment decisions that are inconsistent with these views expressed in this communication. The chart above presents projections of future performance. These projections are based on a number of assumptions that may or may not prove to be accurate. Future performance is subject to a wide range of significant risks. As a result, there can be no assurance that the projections in the chart above will prove to be accurate.

James Hanbury & Jamie Grimston

WS Lancaster Absolute Return Fund

Net Performance (GBP)

	1-month	3-month	1-year	3-year	5-year	YTD	Inception	Inception CAGR
Fund	4.0	6.6	15.9	54.2	59.2	-4.7	387	11.6
MSCI Daily TR Net World	-0.7	0.7	11.8	35.6	55.8	10.6	436	12.4
Relative	4.7	5.9	4.1	18.6	3.4	-15.3	-49.1	-0.7

Yearly Trailing Performance (net)

1-year to	29 Sep 19	31 Sep 20	31 Sep 21	31 Sep 22	31 Sep 23
Fund	-9.3	13.8	53.3	-13.2	15.9
MSCI Daily TR Net World	8.7	5.7	24.1	-2.3	11.8
Relative	-7.7	-8.3	37.5	-22.3	28.2

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2023	6.2	-0.3	-1.3	-0.1	-7.7	-7.1	-0.4	2.9	4.0				-4.7
2022	9.6	-10.9	-7.0	10.3	8.1	-11.1	-0.8	1.6	-6.3	8.1	11.7	0.7	10.7
2021	-12.5	21.3	1.1	2.8	4.2	-9.0	-0.8	2.1	8.9	-7.6	-8.6	12.9	9.9
2020	-5.4	-6.9	-10.6	10.1	6.9	3.0	-6.1	13.2	-4.4	6.6	22.8	1.6	29.1
2019	6.8	-4.9	0.3	-1.7	3.1	-5.3	-4.1	0.7	0.3	4.2	2.2	10.1	11.1
2018	-0.3	0.7	0.9	4.8	3.2	0.3	2.6	-5.6	1.8	0.4	2.8	-7.3	3.8
2017	1.2	-3.4	0.0	1.6	2.9	0.6	-1.3	7.1	0.9	1.4	-1.6	-6.0	2.9
2016	-3.8	5.3	-5.2	-3.6	4.4	2.1	-2.0	-1.2	0.4	-8.9	-1.1	-4.8	-17.8
2015	-2.6	-2.3	1.1	5.6	-5.4	5.0	1.4	1.0	-1.2	4.5	-0.6	1.4	7.6
2014	0.4	3.0	-1.7	-4.7	1.4	-3.0	-0.5	0.3	3.6	2.4	3.2	1.5	5.5
2013	6.7	3.0	1.2	2.0	7.9	1.2	3.5	1.1	4.9	1.8	2.0	3.0	45.6
2012	6.9	8.9	2.3	-1.2	-3.2	3.7	0.9	3.6	3.0	4.1	1.4	2.3	37.2
2011	7.5	2.8	1.7	1.0	2.4	-1.1	-1.1	-10.9	1.0	3.8	-2.9	0.3	3.5
2010	-0.5	-0.5	0.8	2.9	-2.5	-4.7	3.4	-4.8	9.2	2.4	2.8	7.2	15.7
2009					3.9	2.0	2.3	6.3	8.8	-1.4	-1.0	0.5	22.9

Fund details¹

£ I Class	486.8
£ R Class	455.5
\$ I Class	2.71
€ I Class	2.65
Fund Size	£385 million
Strategy AUM	\$1,146 million
Fund Inception	11 May 2009
Class Inception	11 May 2009
Fund Type	UK Long Short UCITS
Comparators	Primary: Cash Secondary: MSCI Daily TR Net World GBP
Base Currency	£

Team & contact details

Portfolio Managers

James Hanbury
Jamie Grimston

Enquiries

T: +44 (0)20 7842 1030
E: reporting@LancasterIM.co.uk
W: LancasterIM.co.uk

Lancaster Investment Management, Yalding House, 152-156 Great Portland St., London, W1W 6AJ

Top 10 Long Equities

Frasers Group	9.7%
IWG	7.8%
Jet2	6.6%
Plus500	4.4%
Ubisoft Entertainment	4.3%
Shell	4.2%
BP	4.2%
Vivendi	3.7%
AO World	3.4%
Natwest Group	3.3%

Portfolio Characteristics

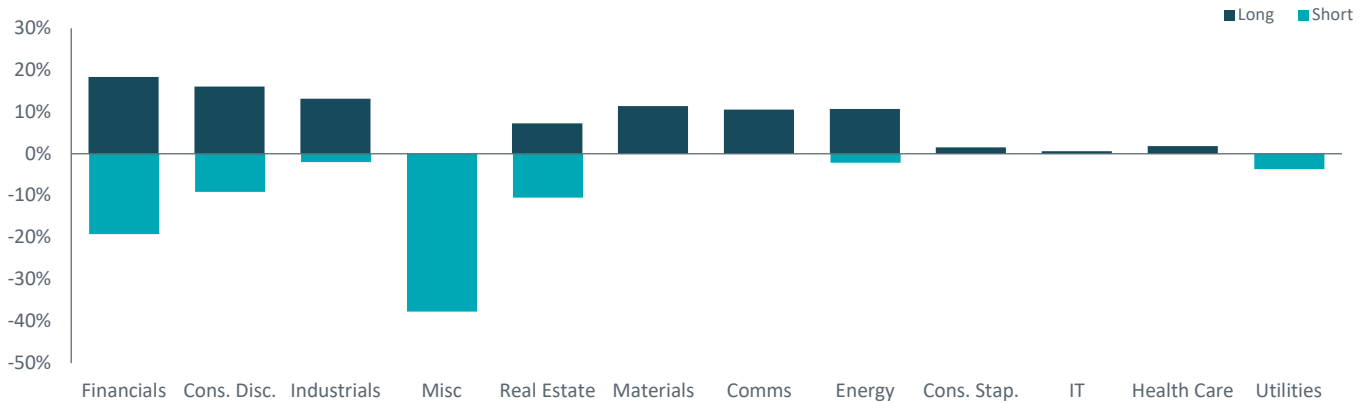
Long position count	60
Short position count	25
Gross long exposure	95%
Gross short exposure	85%
Total gross exposure	179%
Net exposure	10%
Beta adj. net (av. of accounting, 60d & 180d)	30%

Important information

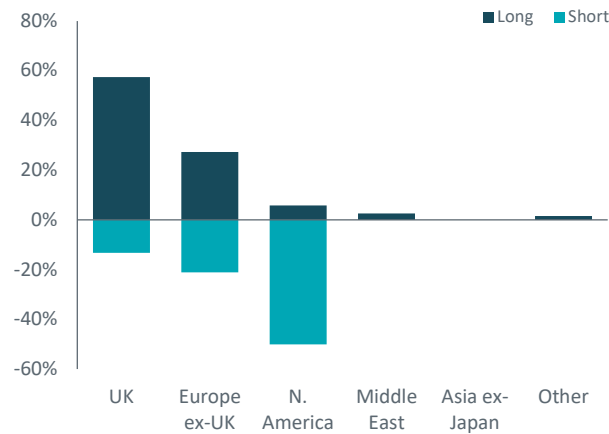
These figures refer to the past. Past performance is not a reliable indicator of future results.

This document is a marketing communication. Before subscribing please read the prospectus and the KIID, available upon request from Lancaster IM. The performance calculation shown is based on the GBP I share class. If the past performance is shown in a currency which differs from the currency of the country in which you reside, then you should be aware that your performance may increase or decrease as a result of currency fluctuations.

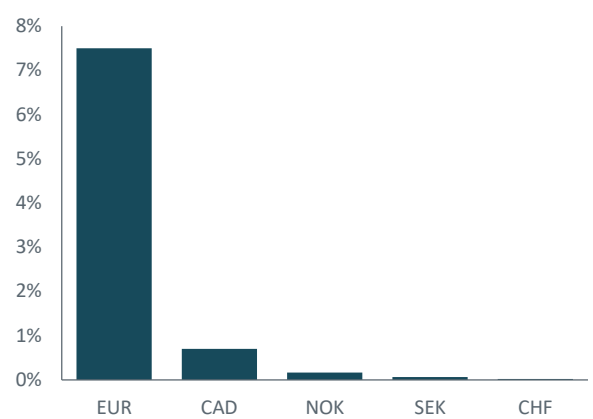
Equity exposure by sector



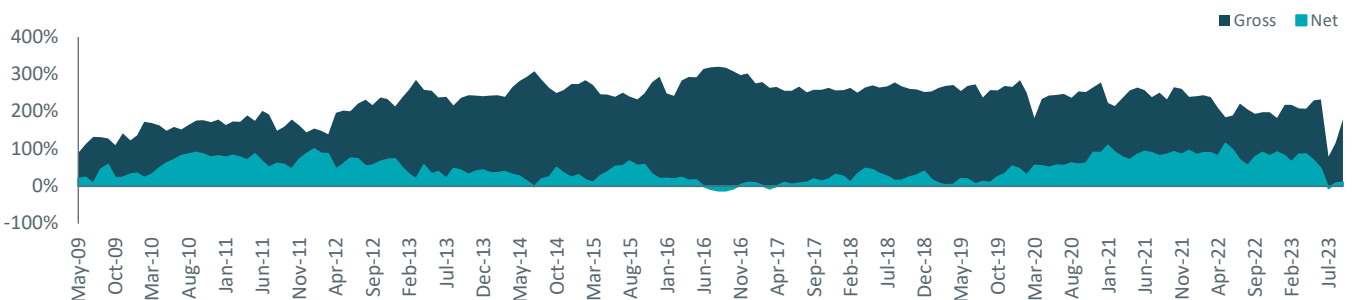
Equity exposure by geography



Non-base currency exposure



Equity exposure



Allocation figures are taken at close of business whereas Fund performance is taken at 10am. Equity exposure includes all equity related instruments. Government Bond exposure can be provided on a ten-year adjusted basis. Currency exposure shows non-base currency through forward currency contracts and portfolio holdings. Commentary is provided on a quarterly basis. Equity exposure as classified by GICS. The fund was renamed from LF Brook Absolute Return Fund to WS Lancaster Absolute Return in Q3-23 on the back of the Investment Management Agreement transferring to Lancaster Investment Management LLP and also Waystone acquiring Link Financial Services. All performance in GBP.

Source: All sources, unless otherwise stated, are Lancaster internal unaudited data and refer to the £ I share class. All data shown as at 29 Sept 2023. ¹Waystone and Bloomberg, calculation on a NAV basis with net income reinvested – the share class prices refer to NAV per share.

Investment objective and policy

The WS Lancaster Absolute Return Fund ('The Fund') aims to achieve a positive absolute return on a 12 month rolling basis independent of market conditions. Capital is at risk and there is no guarantee that a positive return will be delivered over any one or a number of 12 month periods. The Investment Manager seeks to achieve this objective through managing a portfolio of securities, bonds and currencies and related financial instruments.

Approach

The strategy is fundamentally driven global equity long short and built around three core principles; investing in fundamentally sound companies, disciplined short selling, and diversification, which is an essential tool in risk management. On the long side, the approach is valuation driven with a particular focus on sustainable free cash flow generation. On the short side the portfolio is stock-specific. The strategy harnesses the experience and judgement of James Hanbury, his investment team and the wider equity research resource at Lancaster Investment Management. While the team invest for the medium to long term, they continuously resize positions to ensure the portfolio remains focused on their highest conviction ideas. The Fund is built without formal reference to an index and typically contains 30-40 positions both long and short with a higher concentration in the top 10 positions.

Risk Considerations

The Fund has considerable latitude over its allocation both long and short equities and it may employ leverage and own sophisticated instruments such as futures and options. The Fund may hold a large weighting in a small number of investments and may therefore be subject to larger than normal swings in its value. The performance stream is likely to be volatile and the Fund is suitable only for investors who have a long time horizon (>5 years) and can tolerate high risk. Investors may not get back all the money invested and an investment in this Fund should only form part of an investor's total portfolio. Investors should discuss the suitability of this Fund with their professional adviser.

Investor information

Share classes	R (£), I (£, €, \$) Acc.	Anti-dilution fee	May apply up to 0.75% to NAV on subs/reds if large deals (typically >5%) occur
Share class hedging	Non-base currency share classes are hedged	Minimum investment	R £5,000; I £1,000,000
Trade date	Daily	Dividends	Accumulation shares only
Dealing	Forward to 10am	Authorised Corporate Director (ACD)	Waystone
Valuation	10am	Auditor	Ernst and Young LLP
Front end fee	Up to 4%	Custodian	BNY
Annual management fee	R 1.25%, I 0.75%	Price reporting	Prices published daily on lancasterim.co.uk, Bloomberg and by other third party data providers.
Ongoing charge	R 1.55%, I 1.06%	ISIN	R: GB00B55NGR79, £I: GB00B55NGS86, €I: GB00B3SX1S66, \$:GB00B3Z00X80
Performance fee basis	20% of the increase in the value per share of the fund between the beginning and the end of the year. Fees crystallise annually. Losses carried forward.	SEDOL	R: B55NGR7, £I: B55NGS8, €I: B3SX1S6, \$:B3Z00X8

Important Legal Information and Disclaimer

This is a marketing communication and it is not intended to be viewed as a piece of independent investment research. This document and the information contained in it relates to the WS Lancaster Absolute Return Fund (the "Fund") and is being communicated by Lancaster Investment Management LLP ("LIM"). LIM is authorised and regulated by the Financial Conduct Authority (the "FCA") of the United Kingdom and is registered as an investment adviser with the United States Securities and Exchange Commission. LIM and its affiliates together will be referred to as "Lancaster" in this document.

LIM has approved this communication which is for private circulation only, and in the UK is directed to persons who are professional clients or eligible counterparties for the purposes of the Conduct of Business Sourcebook of the Financial Conduct Authority of the United Kingdom (the "FCA") and it is not intended for and must not be distributed to retail clients. It does not constitute an offer to sell or an invitation to buy or invest in any of the securities or funds mentioned herein and it does not constitute any personal recommendation or investment taxation or any other advice. The tax treatment of an investment in any of the securities or funds mentioned herein depends on the individual circumstances of each investor and may be subject to change in the future. The information and any opinions have been obtained from or are based on sources believed to be reliable, but accuracy cannot be guaranteed. The capital you invest is at risk and you may lose some or all the money you invest. Past performance does not guarantee future results and the value of all investments and the income derived from them can decrease as well as increase.

Investments that have an exposure to currencies other than the base currency of the Fund may be subject to exchange rate fluctuations. This communication and the information contained therein is a financial promotion for the purposes of the Financial Services and Markets Act 2000 of the United Kingdom and the rules of the FCA. The distribution of this communication may, in some countries, be restricted by law or regulation. Accordingly, anyone who comes into possession of this communication should inform themselves of and observe these restrictions. Lancaster is not liable for a breach of such restrictions or for any losses relating to the accuracy, completeness or use of information in this communication, including any consequential loss.

Please always refer where appropriate to the relevant Fund prospectus and relevant key investor information document(s) before you invest. The Fund's prospectus and key investor information documents are available in English and may be obtained from reporting@lancasterim.co.uk.