

PENGANA HIGH CONVICTION PROPERTY SECURITIES FUND

ENGAGEMENT REPORT

12 Months to 31 December 2024

Voting Summary

	Number	Percentage
Number of votable meetings	14	
Number of meetings voted	14	100%
Number of meetings with at least 1 vote Against, Withhold or Abstain	3	21%

	Number	Percentage
Number of votable items	94	
Number of items voted	94	100%
Number of votes FOR	90	96%
Number of votes AGAINST	4	4%
Number of votes ABSTAIN	0	0%
Number of votes on MSOP	12	13%
Number of votes on Shareholder Proposals	0	0%

Company Engagement Summary

92 company meetings in the last 12 months to 31 December 2024

60 Small group company meetings

27 1-1 Company management meetings

5 Property tours

Engagement Examples

Case Study – Reputational Damage

Objective of Engagement

Company A withdrew earnings guidance after experiencing negative media coverage around its land lease business model. The objective of engagement was to understand the ESG risks and extent this would impact the earnings and valuation for Company A and other companies operating in the sector.

Summary of Issue and Engagement

The media coverage reported that some residents of the Company's land lease communities were challenging its exit fee or deferred management fee (DMF) structure in the Victorian Civil and Administrative Tribunal (VCAT).

The Company argued that the DMF model was favourable as it lowers the upfront entry cost for customers buying into its communities and that they have been transparent in the sales process to ensure customers understood that the fees were in the agreements.

Given the damaging reputational effects of the media coverage and uncertainties around future sales, the company withdrew its earnings guidance. It subsequently announced retirement of the company's co-founder and Managing Director.

After attending meetings with company management, and further investigations and enquiries with our network of market participants, we assessed that the ESG risks and associated negative impact on the company's earnings will take time to resolve. Thus, there is still material risk to earnings in the near term.

We also engaged with other companies operating in the sector to confirm their business models and ensure they would not be subject to similar scrutiny and risks. We were comfortable that there were no significant risks relating to this matter for the companies the Fund had holdings in.

Outcome

Following the above engagement activities and our assessment of ESG risks, we marked down the Social rating of the ESG score for the Company in our valuation model. We continue to monitor any further concerns from customers, the outcome of the VCAT review, any changes to management and how the company will address this.

Case Study – Climate Change Risk

Objective of Engagement

The engagement aimed to assess the risk to development earnings related to floods and fires and understand management's approach to addressing climate risk.

Summary of Issue and Engagement

Background and Earlier Engagement:

Climate risk can lead to labour shortages, making developments more challenging and impacting land values. Insurance coverage for properties in high-risk areas affected by fire or flood may be difficult to obtain, affecting property values and the value proposition for customers.

Concerns around wet weather and growing news of builders under pressure led us to contact management of A-REITs in the residential sector for further information to assist us in assessing risk to development projects and earnings.

We conducted research to map out flood and fire risk zones in Australia and overlay these with locations of projects of residential developers. This enabled us to identify projects that are located in high-risk zones.

Through our proprietary financial models, we assessed the proportion of earnings over the next two years that were derived from development projects located in these high-risk zones. Our analysis identified the company as one of the companies with higher risk to earnings, with over 10% of forecasted earnings over the next two years exposed to flood/fire risk.

We met with the company's management to discuss their management of climate related risk to development projects. Given the high incidents of fires and wet weather experienced at the time in locations where the company operated, we marked down the ESG score and sold down our position.

The company subsequently announced a series of earnings downgrades due to supply chain challenges, labour shortages and adverse weather impacts.

Monitoring and Recent Engagement:

Following the series of downgrades, the company experienced a significant share price decline. We continued to monitor the company to assess value and ongoing ESG risks. Through our ESG questionnaire and engagement we learnt that the company introduced ESG assessments into the acquisition process.

Over 2024, the company appointed a new CEO as well as changes to the Board and management team. We know the new CEO from his previous roles and after meeting with him we became confident in the new management team's ability to better control ESG and operational risks, extract cost synergies across development projects and drive earnings. The company reinstated guidance during 2024 and upgraded guidance in early 2025, as a result of improved operational efficiencies.

Outcome

Outcome from earlier engagement:

Engagement with management and our internal analysis led us to take the following actions:

- Marked down the ESG score in our valuation model;
- Sold down the Fund's holding; and
- We added an additional question to our ESG questionnaire that is sent out to all companies in our investable universe, requesting details on the processes of how the company is managing bushfire and flooding risk within the property portfolio.

Outcome of recent engagement:

- We maintained the lower ESG score given some climate risk remains based on where some of the company's development projects were located
- However, there has been less incidents of fires and floods and we are more confident in the new management team's ability to manage risks.
- We have bought back a position in the company and benefited from the upgrade in earnings.

Case Study – Governance

Objective of Engagement

There were concerns raised about the independence of a Non-Executive Director due to their involvement in investment ventures. The director's company and a fund in which the director held a 50% ownership stake received investments from the company. The board determined that these matters did not affect the director's independence.

Summary of issue and engagement

Research Findings & Considerations:

An analysis was conducted to assess if these matters violated the company's Conflicts of Interest policy. The policy did not specify any prohibited activities, and the director's investments were disclosed in the company's annual report. The investment amount was deemed immaterial from the company's perspective. From the director's perspective, the investments represented a smaller contribution to their overall activities. The director had other investments and ventures unrelated to the company.

One-Off or Recurring Matter:

There were no similar investments or transactions with other directors and executives in previous annual reports. Therefore, it does not appear to be a recurring matter, but ongoing monitoring will be conducted.

Tenure of the Director:

The director had been on the company's board for over four years and held positions in committees. While tenure was considered, it alone did not significantly impact the director's independence.

Outcome

While the company's Governance rating was reduced, it was based on a separate issue with the Remuneration Report. Regarding this particular matter, the team decided to maintain the company's rating and continue monitoring the situation. Further review will occur if additional investments are made in ventures connected to the director.

Dated 31 December 2024