

Ellerston Australian Small Companies Fund

PERFORMANCE REPORT September 2017

The Ellerston Australian Small Companies Fund employs an active research driven investment approach to identify a portfolio of 30 - 60* small company securities which aims to deliver returns superior to the S&P/ASX Small Ordinaries Accumulation Index over time.

Ellerston Australian Small Companies Fund Performance

| Return % | Net [^] | Benchmark | Net Alpha | Gross Alpha |
|----------------------|------------------|-----------|-----------|-------------|
| 1 Month | 1.87% | 1.31% | 0.56% | 0.63% |
| 3 Months | 2.20% | 4.41% | -2.21% | -2.01% |
| Rolling 12 Months | 2.68% | 2.97% | -0.29% | 0.83% |
| 2 Years p.a. | 12.59% | 15.33% | -2.74% | -2.09% |
| 3 Years p.a. | 10.10% | 8.15% | 1.95% | 3.35% |
| Since Inception p.a. | 9.74% | 6.73% | 3.01% | 4.58% |

Ellerston Australian Small Companies Fund Top Holdings

| Top 5 Stock holdings as at 30 September 2017 | Sector | % |
|--|------------------------|-------|
| Tassal Group LTD | Consumer Staples | 3.52% |
| Cleanaway Waste Management LTD | Industrials | 3.50% |
| Austral LTD | Industrials | 3.27% |
| Synlait Milk LTD | Consumer Staples | 3.04% |
| Southern Cross Media Group LTD | Consumer Discretionary | 2.93% |

[^] The net return figure is calculated after fees & expenses. The gross return is calculated before fees & expenses. Past performance is not a reliable indication of future performance

The benchmark is the ASX Small Ordinaries Accumulation Index. The Fund commenced on 10 October 2013.

*This is the typical number of stocks in the portfolio. The Information Memorandum does allow for 20 - 60 stocks.

Commentary

The Ellerston Australian Small Companies Fund rose 1.87% in September, outperforming the ASX Small Ordinaries Accumulation Index which rose 1.31%. During the month, the Small Industrials Accumulation Index rose 1.06% whilst the Small Resources Accumulation Index rose 2.43%.

The largest contributors to positive attribution were Synlait Milk Ltd (SM1), Macmahon Holdings (MAH), and Toxfree (TOX). Synlait reported a solid FY17 result modestly ahead of expectations. Management also lifted FY18 canned infant formula production guidance on the back of strong A2 Milk momentum. Importantly, Synlait has now attained Chinese regulator's CFDA registration ahead of expectations for A2, following submission of the application in May-17. This not only secures direct import volumes into China for Synlait's largest customer, but also increases the chances of registration for other key customers. Macmahon rose during the month as the market gained confidence in the strength of the turnaround and commenced the re-rating to where it's peers trade. After a chequered history over the last 10 years, the new management team have put in place actions to reduce contract losses and with the Batu Hijau contract in Indonesia, significantly grow the long term order book. This should result in a significant earnings recovery over the next 3 years. Toxfree moved higher during the month as they signaled that the company would return to organic earnings growth in FY19 on the back of awarded contracts. After a number of years of negative organic growth, this should end in FY18 as the last of the legacy resources contracts are completed. The acquisition of Daniels has improved the structural growth of the business, which should result in earnings growth and a re-rating over the next few years.

The largest detractors from relative returns were A2 Milk (A2M), Austal (ASB) and Pilbara Minerals (PLS). A2 Milk's rally on the back of Synlait's CFDA registration and increased comfort of A2's import potential into China has seen A2 share price rally further. Both A2 and Synlait has also confirmed production of A2's Stage-4 formula, and the market has capitalised substantial net growth of the product portfolio into the share price. A2M's valuation looks full given the potential volatility of sales channels into China and risk of slower end-demand growth, particularly as A2's market share becomes more saturated in the premium niche end of the Chinese infant formula market. Austal drifted lower over the month on no new news. The company is very well placed to benefit from the early signs of an uptick in the commercial ferry market which has been in a state of hibernation for the last 10 years. Naval contracts margins have improved over the last year which should result in a further uplift in earnings in FY18 and FY19. Market concerns center around Federal Government commitment to local production which has been raised as an issue the last couple of months. However, the Offshore Patrol Vessel will be produced locally and Austal has a reasonable chance of winning this project. Any work from the RAN Frigate program would be a bonus. Pilbara Minerals was not held in the portfolio and hence made a negative alpha contribution as it rallied 79% during the month.

Outlook

Global markets continued to track higher during the month as the "goldilocks" environment continues of just enough growth, low interest rates and easy financial conditions. It is difficult to predict when and what will upset this relatively benign environment, but undoubtedly something will. Consequently, we continue to try and rotate the portfolio out of higher valued stocks and into companies where the risk-return trade-off is more skewed in our favour. With valuations relatively full, this is not an easy task, often resulting in us taking small position sizes in lower market capitalisation companies. Consequently, in the foreseeable future, stock numbers will continue to remain at the higher end of the range.

About the Ellerston Australian Small Companies Fund

The Fund employs an active, research-driven investment approach which seeks to identify a portfolio of smaller company securities with the aim of delivering superior returns to the Benchmark over time.

The Fund will invest in companies that are believed to have the potential to deliver significant upside over the medium term and where there is a reasonable margin of safety to mitigate the downside risk. We will actively manage the positions of the Fund.

Investments will generally be made in companies that have a sound business franchise with an attractive earnings profile, that operate in growth industries and trade at a discount to valuation.

Fund Facts

| | |
|---------------------------------|-----------------|
| Strategy Funds Under Management | \$814 Million |
| Total number of Stocks | 55 |
| Application Price | \$1.0782 |
| Redemption Price | \$1.0728 |
| Inception Date | 10 October 2013 |

Disclaimer

Returns are unaudited estimates and before fees and expenses and assume distributions have been reinvested. Past performance is not indicative of future performance. This letter does not constitute an offer of any Units in the Fund. This letter does not take into account your investment objectives, financial situation or particular needs. Before making an investment decision about the Fund, persons should read the information memorandum which can be obtained from Ellerston Capital and obtain advice from an appropriate financial adviser. This material has been prepared based on information believed to be accurate at the time of publication. Assumptions and estimates may have been made which may prove not to be accurate. Ellerston Capital undertakes no responsibility to correct any such inaccuracy. Subsequent changes in circumstances may occur at any time and may impact the accuracy of the information. Stock opinions and views expressed in this document are Ellerston Capital's and are not necessarily the views or opinions of the market. To the full extent permitted by law, none of Ellerston Capital, or any member of the Ellerston Capital Limited Group of companies makes any warranty as to the accuracy or completeness of the information in this document and disclaims all liability that may arise due to any information contained in this document being inaccurate, unreliable or incomplete.