Ellerston Global Equity Managers Fund

PERFORMANCE REPORT June 2018

Investment Objective

The investment objective is to generate superior returns for Unitholders with a focus on risk and capital preservation.

Investment Strategy

- Global long/short equity
- Overlays fundamental stock selection with macroeconomic outlook
- Bias toward Australia

Key Information

Strategy Inception Date	1 January 2002
Fund Net Asset Value	A$192.0M
Liquidity	Quarterly
Class A Redemption Price	A$ 1.7455
Class B Redemption Price	A$1.7016
No. Stocks	144
Gross Exposure	159%
Net Exposure	98%
Management Fee	1.50% p.a
Buy/Sell Spread	0.25%
Performance Fee	16.50%
Firm AUM	Over A$5b

Fund performance

	1 Month	3 Months	1 Yr	3 Yr p.a	5 Yr p.a	Strategy Since Inception p.a
GEMS A Net	-0.45%	0.78%	22.04%	14.40%	16.53%	13.49%
GEMS B Net	-0.45%	0.78%	22.04%	14.39%	16.39%	13.31%

Market Commentary

Market Overview

June was a torrid month for global equities, but the Australian share market bucked the trend and was the star performer, outperforming the major US, European and Asian equity markets. Overall, developed markets significantly outperformed emerging markets (for the third consecutive month), with emerging markets' weakness driven by a further sell-off in the Chinese market, a stronger US dollar and heightened fears of a damaging trade war. As widely expected, the Fed raised interest rates by another 25 basis points in June (the second time this year), given its view on US inflation and a robust labour market, coupled with solid economic growth. The US labour market has staged one of history's most astonishing recoveries over the past decade, a turnaround that has surprised all observers. The unemployment rate has dropped from a peak of 10% in October 2009 (the second highest in the post-war period), to just 3.8% in May 2018 (the lowest seen since 1969). This remarkable fall is the largest experienced during a single cycle in the modern era. That said, wages growth remains below its pre-GFC average, prompting much commentary.

Trade tensions did not abate during June, with the US and China failing to reach a resolution. US, Canadian and European officials also continued to ratchet up their rhetoric on tit-for-tat tariffs. Markets weren't given much direction from the G7 summit either, ending with the leaders squabbling over the contents of their final communique, and President Trump refusing to sign the final release. The much anticipated meeting between President Trump and North Korea's Kim Jong-Un finally took place and resulted in a vague statement on nuclear disarmament. Australia saw the RBA leave rates on hold and the Royal Commission continued its investigative work, but financials, especially the major banks, staged a relief rally from oversold levels, bouncing off their mid-June lows.

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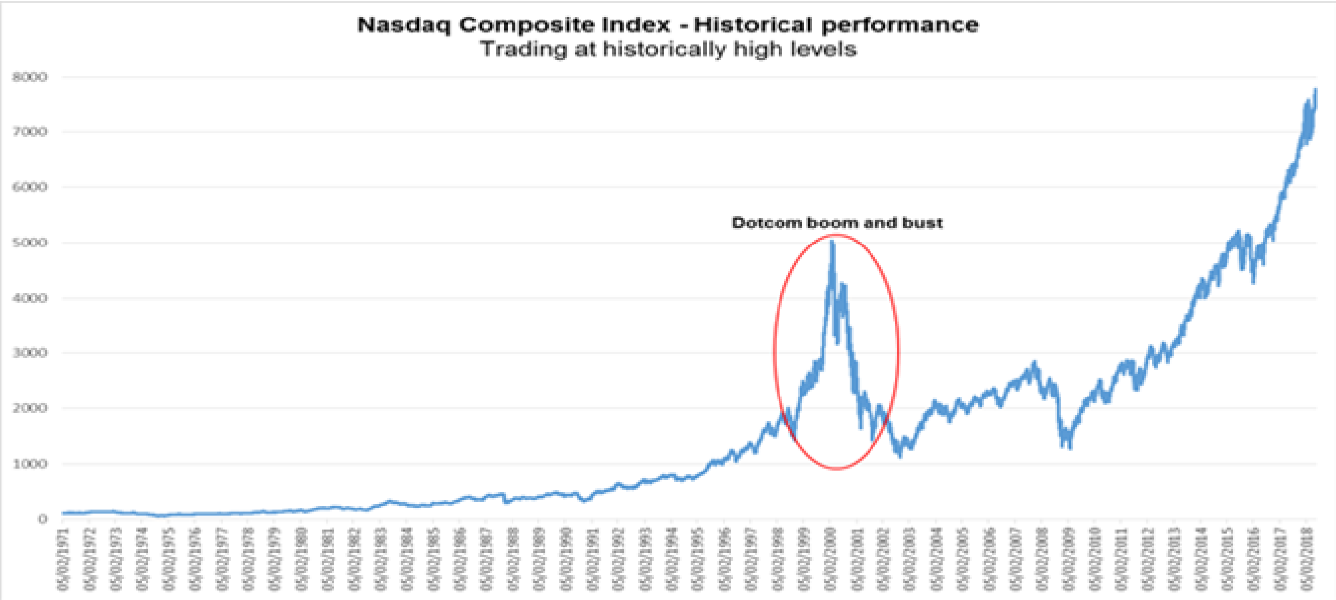
USA

The S&P 500 Index and the Dow Jones Industrial Average Index ended June up 0.6% and down 0.5% respectively, with the NASDAQ continuing its stellar run, up 1.0% after having delivered an impressive +5.5% the previous month. The ill-tempered rhetoric on trade continued with seemingly no resolution with the DJIA trading down 5.3% intra-month. The EU also promised to impose retaliatory measures on $300 billion of US goods in response to Mr Trump's threat to impose punitive tariffs on the importation of European cars and parts, having already stoked tensions over steel and aluminium imports.

The Fed meanwhile hiked rates by another 25 basis points, with policy makers making it clear that market volatility would not divert them from their previously flagged intentions. The US 10-year bond yields closed at 2.86%, broadly unchanged versus their level from the previous month. With the yield curve flattening (the spread between the 2-year and 10-year treasuries compressing), debate rages on what this is actually telling investors. Opinion is divided, with one view holding that the long-end of the yield curve might be suggesting a looming recession. What is clear, is that the NASDAQ and technology-led stocks have had an epic run. See below, the long-term performance of the NASDAQ.



Source: Ellerston Capital Limited, Bloomberg

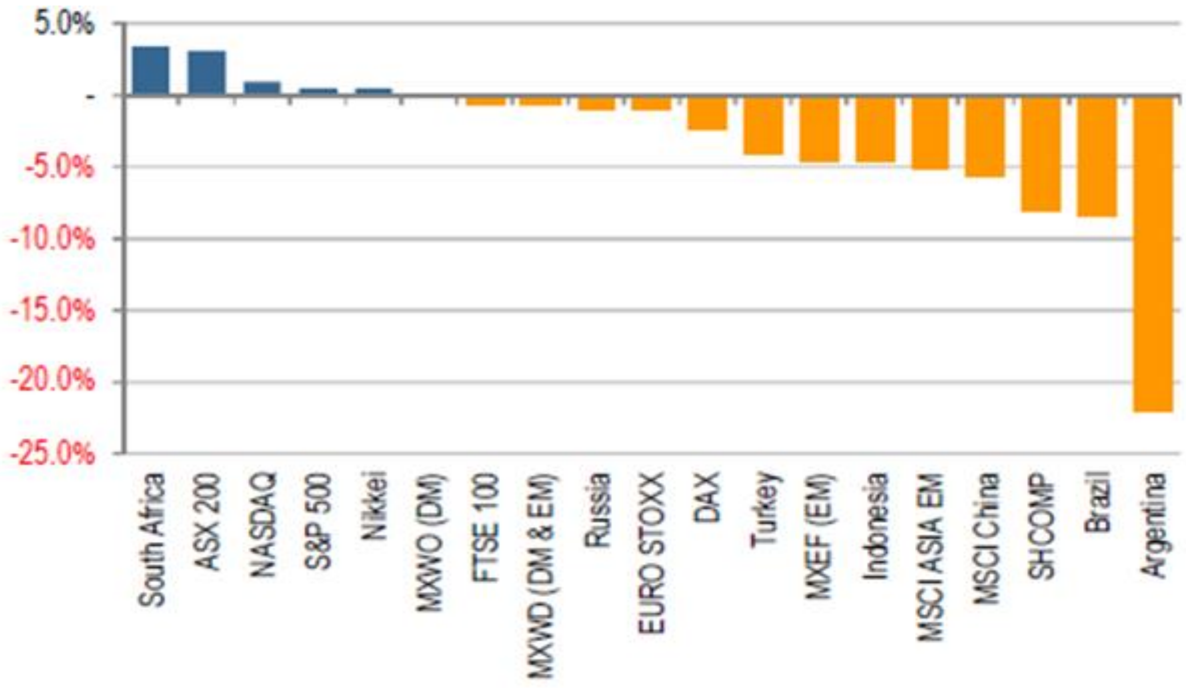
Europe

European stocks were again weaker in June, with the Euro STOXX 50 Index declining 0.2%. France's CAC 40 returned - 1.1% while Germany's DAX was down 2.4%, impacted by Trump's call for tariffs on German cars and parts and compounded by political uncertainty in Germany. The UK's FTSE 100 Index was also modestly in negative territory, down 0.2% and continued to be dogged by the lack of real progress on a post-Brexit deal. The ECB confirmed its tapering of quantitative easing, with QE expected to be completed by this December.

Asia

As witnessed last month, fears of an all-out trade war had a dampening effect on Asian equities, with Korean and Chinese stocks hit particularly hard. As these markets have a relatively high concentration of technology stocks, the threats of tariffs battered their tech-heavy indices. The Shanghai Stock Exchange Composite Index was down almost 7%, the Hang Seng Index was down 4.5% and Korean equities were down 4.0%. Markets were also hit by a strengthening US dollar. Japan's Nikkei 225 Index had a volatile month: it initially sold off after the Trump-Kim summit, before closing the month in positive territory, up 0.6%. The Peoples Bank of China cut its reserve requirement ratio, currently at 16% for big banks by 50 basis points, injecting liquidity into its system in order to cushion the negative impact of a likely trade war. It was the third cut this year.

Global Markets' Performance in June 2018



Source: JP Morgan, Bloomberg.

Commodities

Bulk commodity prices, including iron ore, thermal coal and hard coking coal all continued to firm. Oil was the stand out feature in commodity markets, with WTI crude prices rising 10.6% to US$74.15/bbl , despite the higher dollar, on concerns about tightening global oil supply. Crude prices were helped by OPEC's vague statements post the Vienna meeting where it left its overall quota unchanged, but alluded to production increases from those members with spare capacity. Gold prices dropped 3.5% to US$1,253/oz in June and despite fears of a pending trade war, there hasn't been the flight to the obvious safe haven store of value.

Bonds

The US yield curve continued to flatten as the spread between the short-term rates and long-term rates narrowed. The US 10-year bond yield rose 15 basis points to close the month at 2.86%. In Australia too, the spread narrowed slightly.

Australia

The Australian equity market produced strong returns in the month of June, with the S&P/ASX 200 Accumulation Index closing up 3.3%. Both the ASX 200 Resources and Industrial Accumulation Indices returned +3.3% in the period. The Small Ordinaries Accumulation Index lagged the broader market and delivered a more modest return of +1.1%. Blue Sky Alternative (BLA, -34.4%) was the worst performing small cap stock over the month, and continued its horror run after it released news that it was facing losses for FY18 of $59.4m, a sum greater than all of its previously reported profits since listing in 2012.

Outlook and Portfolio Commentary

We expect markets to remain volatile and unpredictable as we go into FY19, with a number of pertinent economic and political issues likely to impact the direction of markets.

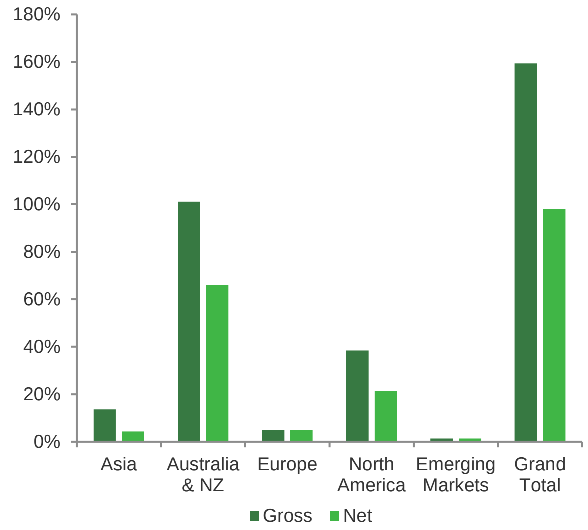
The most significant of these issues remains the potential for a trade war, between the US and China. The rhetoric over the past year has been largely verbal with only minor tariffs imposed. However, this all changed on 6 July 2018 when President Trump's tariffs on US$34 billion of Chinese imports came into effect. Comments from Chinese President Xi Jinping that "in the West you have the notion that if somebody hits you on the left cheek, you turn the other cheek. In our culture we punch back." do not instil confidence that this trade war will be resolved in the near term. How this potential trade war plays out will no doubt have a significant impact on how markets and broader economies perform through Fiscal Year 2019 and beyond.

We note that in the June 2018 US inflation report the index for laundry equipment rose 13.1 percent from a year earlier. This is interesting because washing machines were the subject of initial 'token' imports tariffs announced by President Trump in January 2018. It serves to illustrate that there will be many scenarios where the US consumer is likely to suffer if a trade war were to eventuate. Chairman of the US Federal Reserve, Jerome Powell, has cautioned in regards to the trade war threat – "there could be an effect on inflation… you can imagine situations which would be very challenging, where inflation is going up and the economy is weakening." The trade war headlines, however, have done little to disturb the US Federal Reserve from their rate hiking path thus far. The latest dot plot implies a further two hikes in calendar year 2018 and three in 2019.

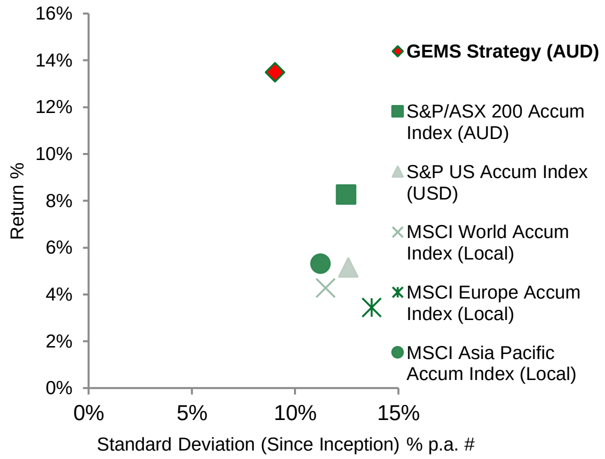
Across the Atlantic, Brexit continues to attract a significant amount attention in the UK and Europe. Theresa May has had a difficult time agreeing on the structure of a deal not only with the EU but with her own internal party. This instability has seen an increased probability that Jeremy Corbyn may be the next UK Prime Minister which may worry markets. In Europe, the ECB has communicated its intention to end QE in December 2018, but not to raise rates until at least this time next year.

Consistent with recent months, the Portfolio's largest exposure remains in Australia. A number of core positions with significant upside are positioned to take advantage of company-specific catalysts. Core exposures include Clover Corporation, Central Petroleum, Catapult Group, Healthscope and Tasfoods. The U.S., whose economy remains resilient, once again comprises the fund's next largest exposure. We will continue to watch situations and opportunities closely as the trade backdrop and the Fed actions play out. The fund's largest North American holdings include CES Energy Solutions, The Stars Group and Nutrien. Albeit at a modest overall level of portfolio exposure, the fund continues to hold a number of strategic investments in Asia, particularly in India, with a view to capitalising on attractive valuations and growth through domestic demand there.

Market Exposure as a % of NAV



GEMS Strategy Performance & Volatility ^



The GEMS strategy since inception has achieved higher returns than all of the major indexes highlighted in this table since inception with lower risk over the same time period.

Top Holdings (Alphabetical, Long only)

- ALPHABET INC
- CATAPULT GROUP INTERNATIONAL
- CLOVER CORP LTD
- EZCORP INC
- GRAINCORP LTD
- HEALTHSCOPE LTD
- LINK ADMINISTRATION HOLDINGS
- PSC INSURANCE CORP LTD
- STARS GROUP INC
- TREASURY WINE ESTATES LTD

Key Service Providers

- **Registry**: Link Market Services Limited
- **Auditor**: Ernst & Young
- **Prime Broker**: Morgan Stanley Intl & Co PLC & Goldman Sachs International
- **Administrator**: Citco Fund Services (Australia) Pty Ltd
- **Custodian**: State Street Australia Limited

Material Matters

During the month there were no material changes to the Fund in terms of its risk profile, investment strategy or changes to investment staff which would impact this strategy. There have been no changes to the key service providers described above.

Disclaimer

^ Actual performance for your account may vary from that set out in this newsletter and will vary for investments made in different classes, or at different times throughout the year. Some performance data is estimated and preliminary and subject to change.

^^For the period 1 January 2002 to 30 April 2006, the CPH Group GEMS Portfolio was not operated within a separate fund structure. The underlying investment assets of the CPH Group GEMS Portfolio were owned during that time within corporate entities of the CPH Group for which audited accounts were prepared on an annual basis. Accordingly, in order to provide relevant historical performance information for the period 1 January 2002 to 30 April 2006 (Historical Returns) net returns were calculated on the basis of the actual dollar returns of the CPH Group GEMS Portfolio adjusted to reflect a fund structure similar to the Fund and including all fees. For GEMS B, GEMS A returns have been used between 1 May 2006 and 2 November 2009.
The returns of the Fund and the relevant Indices are net of fees, expenses and taxes and assuming distributions are reinvested.

The performance figures presented are for the Ellerston Global Equity Managers Fund GEMS A and B Units. The one month return figure may be an estimate and not the final return. This estimate also impacts other performance information provided. Estimated performance figures are preliminary and subject to change. Returns for other classes may differ slightly. Past performance is not indicative of future performance. Ellerston Capital Limited ABN 34 110 397 674 AFSL 283 000 is the responsible entity of the Ellerston Global Equity Managers Fund ARSN 118 887 095 (Fund). This newsletter has been prepared by Ellerston Capital Limited without taking account of the objectives, financial situation or needs of investors. Before making an investment decision you should consider your own individual circumstances and obtain a copy of the Product Disclosure Statement for the Fund dated 31 January 2014 which is available by contacting Ellerston Capital. 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. To the full extent permitted by law, none of Ellerston Capital Limited, 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 newsletter and disclaims all liability that may arise due to any information contained in this newsletter being inaccurate, unreliable or incomplete.

The standard deviation is often used by investors to measure the risk of an asset. The standard deviation is a measure of volatility: the more an asset's returns vary from the average return, the more volatile the asset. A higher standard deviation means a greater potential for deviation of return from the average return of the asset.