ELLERSTON CAPITAL

Ellerston Global Equity Managers Fund (GEMS)

Performance Report | February 19

PERFORMANCE SUMMARY

Net %	1 Month	3 Months	1 Yr p.a.	3 Yr p.a.	5 Yr p.a.	Strategy Since Inception p.a.
GEMS C	-0.90	-1.93	-15.60	4.90	10.32	9.88

Past performance is not a reliable indicator of future performance.

MARKET COMMENTARY

Market Overview

In February, global equity markets continued to rally. Developed Markets, led by Australia, rose 3.4% and outpaced Emerging Markets, up 1.1%. Performance was supported by expectations of a positive outcome from the trade talks between the US and China. In fact, on 24 February, President Trump announced that the US would postpone an increase in tariffs on goods from China due from 1 March because of "substantial progress" in trade talks.

USA

Politics in the US continued to be unpredictable, with President Trump declaring a national emergency on 15 February over border security, in an effort to get more funding for his wall on the US-Mexico border. Markets however shrugged off the political noise from Washington and focused instead on a likely positive outcome from the US-China trade talks and encouraging January activity indicators suggesting continued strength in the US economy.

The S&P 500 Index and the Dow Jones Industrial Average Index delivered solid returns in February following on from a very strong January, ending the month up 3.2% and 4.0% respectively. The NASDAQ also returned a very credible +3.6%.

In January, the Fed signalled that it would pause raising interest rates. Data will need to be monitored closely as minutes released in February suggested that the Fed is still modestly biased towards tightening, despite the statement having conveyed a neutral bias. US activity indicators remain sound. Manufacturing ISM rose more than expected to 56.6 (previous: 54.9; consensus: 54.0) and non-farm payrolls beat expectations, rising 304K in January (previous: +222K; consensus: +165K).

Europe

European equity markets also continued to deliver positive returns, with the Euro STOXX 50 Index up 4.4%. This was despite economic data continuing to moderate. The flash Eurozone manufacturing PMI for February disappointed with a reading of 49.2 (previous: 50.5; consensus: 50.3), but the composite PMI rose modestly to 51.4 (previous: 51.0). The major European indices were much stronger, catching the wave of optimism that a resolution between the US and China over trade would be positive for global growth: France's CAC was up an impressive 5.0%, Germany's DAX was up 3.1% and the FTSE 100 was up 2.3%.

Asia

Asian equities were mixed. The standout was the Chinese market, represented by the SSE Total Market Index, up a staggering 14.3%, as optimism on US-China trade talks firmed. The Hang Seng Index posted a more modest 2.7%, but Korea's KOPSI Composite Index delivered a disappointing -0.4%.

Questions still remain over the health of the Chinese economy. The February manufacturing PMI softened to 49.2 (previous: 49.5; consensus: 49.6) and the composite PMI also fell to 52.4 (previous: 53.2). Resolution and clarity on trade talks should provide some relief to a softening Chinese economy, which remains an area of concern and focus for markets, especially given the very strong rally in Chinese equity markets in February.

Investment Objective

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

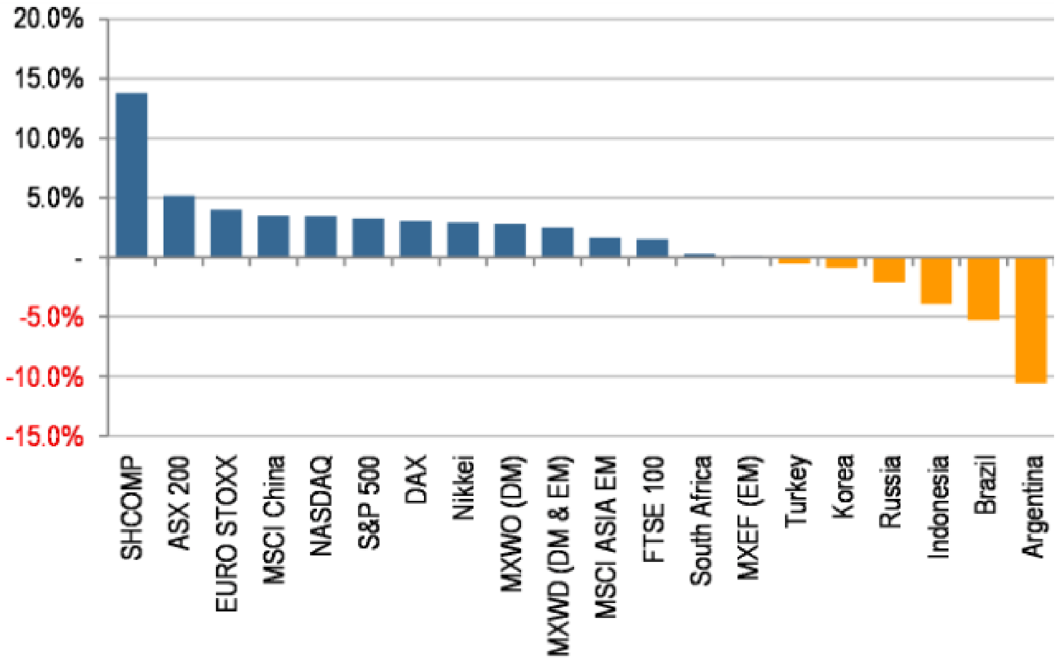
Investment Strategy

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

Key Information

Strategy Inception Date	1 December 2009
Fund Net Asset Value	A$160.4M
Liquidity	Monthly
Application Price	A$ 1.4240
Redemption Price	A$ 1.4169
No. Stocks	68
Gross Exposure	90%
Net Exposure	62%
Management Fee	1.50% p.a.
Buy/Sell Spread	0.25%
Performance Fee	16.50%
Firm AUM	Over A$5b

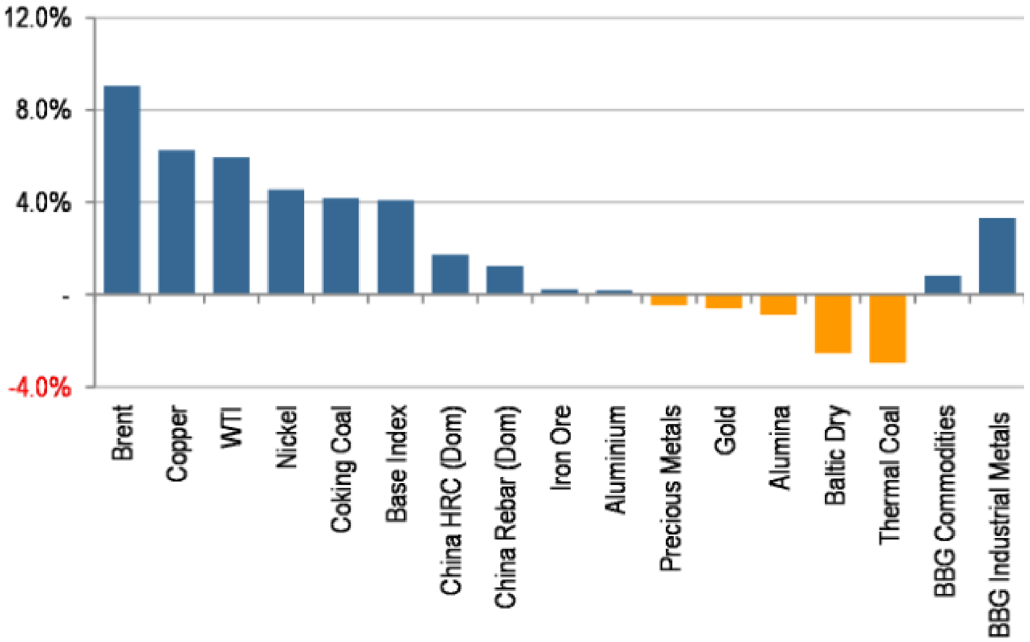
Global Equity Markets' Performance in February 2019



Source: JP Morgan, Bloomberg.

Commodities

The BBG commodities Index rose 0.8% in February. The best performer was Brent, which gained 9.1% to US$66.03 a barrel on falling US inventories, while the worst performer was Thermal Coal, which fell 3.0%. Gold prices fell on the back of a stronger US dollar.



Source: JP Morgan, Bloomberg.

Bonds

Global bonds sold off modestly in February on expectations of a rise in inflation from higher oil prices. US 10-year bond yields rose 8 basis points to close the month at 2.71%. The Australian 10-year bond yield fell again to close the month at 2.10% from 2.24% the previous month.

Australia

Australian shares performed best in the Developed Market. The **S&P/ASX 200 Accumulation Index ended the month up 6.0%**. With the exception of the Consumer Staples sector, all sectors delivered positive returns. The best three performing sectors were Financials (+9.1%), Energy (+7.9%) and Information Technology (+7.6%). The bottom three sectors were Consumer Staples (-1.5%, featuring for the second month in a row in the bottom three), Health Care (+1.0%) and Real Estate (+2.1%).

In February, the **ASX 200 Resources Accumulation Index was once again the best performer**, up 6.9% with BHP Group (+6.9%) and Rio Tinto (+10.5%) building on their strong performances in January as the market rewarded announced capital management initiatives. Woodside Petroleum (+9.4%) was also a significant contributor as investors cheered a better dividend and priced in a strong oil price. The Small Ordinaries Accumulation Index was only slightly behind with a strong return of +6.8% and the ASX 200 Industrial Accumulation Index was also impressive with a +5.8% return.

The top five stocks that detracted from the performance of the S&P/ASX 200 Accumulation Index were Coles (-8 points), Cochlear (-8 points), Stockland (-4 points), CSL (-4 points) and Saracen Mineral Holdings (-4 points).

The top five stocks that added to the index return were Commonwealth Bank of Australia (+68 points), Australia and New Zealand Banking Group (+55 points), Westpac Banking Corporation (+54 points), BHP (+46 points) and Macquarie Group (+25 points).

The pressure on house prices in Australia did not abate. National Corelogic dwelling prices fell 0.7% month-on-month in February, putting the year-on-year decline at -6.3% (the worst since March 2009). December residential building approvals fell, -8.4% which took the year-on-year decline to -22.5%.

Activity data was mixed: December retail sales fell more than expected at -0.4% (previous: +0.5%; consensus: +0.0%) but employment in January rose a greater than expected 39K (previous: +17K), with unemployment levels held steady at 5.0%. NAB's business conditions bounced to +7 in January from +3 previously and business confidence rose too.

In a surprise move, the RBA moved to a neutral bias and downgraded its GDP growth forecast modestly. The Australian dollar depreciated 2.4% against the US dollar to close the month at $0.7094. In trade-weighted terms, the AUD depreciated 1.5%.

Outlook and Portfolio Commentary

We continue to anticipate a very volatile investment environment for the remainder of 2019. On the positive side, in Australia, we expect more capital management initiatives as surplus franking credits are cleared and the prospect of more M&A activity if the AUD weakens further. Whilst on the negative, we are expecting lower earnings, lower growth prospects and uncertainty stemming from the resurgence of high valuations in Industrials ex-financials. Overseas, whilst a number of global geopolitical issues are expecting to come to a head in the next few months, we do not underestimate the potential for some of these being slow to resolve, nor do we believe any of them will be a smooth ride.

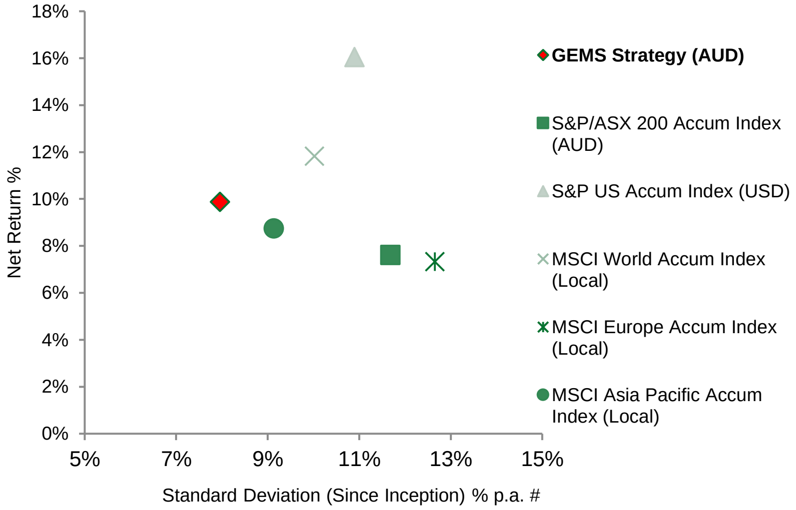
Globally, following the Fed turning dovish with its rate guidance in January, it remains unclear if it will maintain its neutral stance in the case that inflation and wage data in the US are stronger than anticipated. In fact, the Fed minutes (released in February) suggested that committee members were still modestly biased towards an increase in rates. On the heels of recent optimism, markets have been pricing in a positive outcome from trade talks to end the US-China trade war. However, these positives could be somewhat counteracted by worries surrounding weaker macroeconomic data, despite some pockets of strength in the US. Increasingly, the prospects for an earnings recession in the US is also being hotly debated by investors. EPS growth in the S&P 500 has also recently declined substantially due to tax changes, changing energy prices and a turn in the semi-conductor cycle. We believe that the underlying dynamics may be more benign, but more data points are required to support that conclusion definitively. We'd like to reiterate the risks to investment markets we've previously identified. These include the negative effects of a trade war, slowing global growth (especially in China, where there are increasing concerns that the slowdown in their economy might be worse than initially feared) and the uncertainty and incoherence emanating from Trump's White House.

Domestically, our concerns around the sustainability of earnings appear to be playing out. Following the latest Australian reporting season, only 12% of reporting companies upgraded earnings expectations against 36% guiding to lower earnings. This "negative skew" has resulted in earnings growth forecasts of just 3.3% in FY19. This is mostly driven by Resources, as the Industrials ex-Financials are now expecting earnings to contract. Dividends and capital management provided the key upside surprise during the reporting season and cost pressures were the key downside surprise (particularly among the financial stocks). The key risks to the Australian market remain the second-order effects of the macro drivers above, along with sharply slowing credit growth, an indebted consumer, fear of a harder economic landing and a pending Federal election this year.

During February, we have brought down the portfolio's gross long exposure to 76% (from 87%) through decreases primarily in Australia and New Zealand. Similarly, we have decreased its gross short exposure again this month to 14% (from 22%) through adjustments to Australia and New Zealand exposures, as well as North America. In terms of sectors, we rebalancing across a range of sectors, with long exposure trimmed primarily from Healthcare, Energy, Information Technology and Financials, and short exposures trimmed mainly from Materials, Consumer Discretionary and Consumer Staples. Our hedging at the portfolio level remained fairly stable. The aggregate result continues the trend of recent months towards reduction in total gross exposure of the portfolio (this month, from 110% to 90%) and a slight decrease in the portfolio's total net exposure (from 65% to 62%).

Market Exposure as a % of NAV

GEMS Strategy Performance & Volatility ^



Top Holdings (Alphabetical, Long only)

- ALPHABET
- BP
- CATAPULT GROUP
- CLOVER CORP
- GENERATION DEVELOPEMENT
- GRAINCORP
- NEWCREST MINING
- NUFARM
- PSC INSURANCE
- REECE

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

Source: Ellerston Capital

Material Matters

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

ABOUT THE ELLERSTON GLOBAL EQUITY MANAGERS FUND

The Fund aims to achieve its performance objectives by adopting a fundamental "bottom-up" investment approach to stock selection which is focused on identifying and then constructing a portfolio of the highest conviction ideas.

Investment opportunities for the Fund are identified by analysing and understanding the factors affecting (amongst other things): business model, industry structure, management team and overall valuation. Ellerston Capital typically favours businesses that can sustain high returns or improve their return on capital and looks to invest in businesses with a market value below the value we attribute to them.

Benchmark weightings do not drive our stock decisions, our approach is totally benchmark independent.

Due to the high conviction nature of the portfolio and the resulting deviation in portfolio composition relative to benchmark weighting, it is expected that the returns from the Fund will differ significantly from the broader market indices.

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DISCLAIMER

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.