

Ellerston Australian Small Companies Fund (SCF)

Performance Report | March 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.
SCF	-2.43	7.94	1.94	10.28	8.89	8.92
Benchmark	-0.12	12.59	5.78	11.40	7.97	7.81

Source: Ellerston Capital Limited

MARKET COMMENTARY

The Ellerston Small Companies Fund fell 2.43% in March, underperforming the ASX Small Ordinaries Accumulation Index which fell 0.12%. During the month, the Small Industrials Accumulation Index rose 0.42% whilst the Small Resources Accumulation Index fell 2.02%.

The largest contributors to positive attribution were St Barbara (SBM), West African Resources (WAF) and New Hope Corp (NHC). St Barbara, which is not owned by the fund, suffered a 24% fall in the share price as they downgraded production guidance at one of their operations during the month. West African Resources rose 18% despite the fall in the gold price. There was no specific news to drive the share price higher. The company is advancing the development of its Sanbrado gold project in Burkina Faso, which as it is developed and brought into production should see the discount to valuation close over the next 2 years. New Hope Corp, which is not owned by the fund, suffered a sharp fall in the share price during the month as the benchmark price for Thermal Coal fell to an 18 month low.

The largest detractors from relative returns were Eclipx Group (ECX), Ardent Leisure Group (ALG), and Syrah Resources (SYR). Eclipx fell over 60% during the month following a substantial profit warning and the cessation of the agreed merger with McMillian Shakespeare. The profit downgrade was driven by the poor performance of Right to Drive and Grays Auctions, two businesses acquired in the last couple of years. The profit of the core novated and fleet businesses remains steady. Right to Drive and Grays are now up for sale, which if their losses are removed means that the core business remains very attractively price. Ardent Leisure Group fell 30% for the month on no new news. After rallying post the half year result the share price fell away quickly. This is most likely due to a large shareholder/fund manager liquidating their position due to the closure of the business. This will likely clear over the near future and we expect the stock to rally thereafter. Syrah Resources fell 22% during the month on concerns about their ability to get through to cash flow breakeven without another capital raising. The June quarter this year should see the low point for cash as they move into being cash flow positive. We think that the company will make it through this period without a capital raising and have subsequently increased our shareholding during this period of weakness.

OUTLOOK

As discussed last month, we continue to believe the market is stuck in a wide trading range for the foreseeable future, with the upside capped by valuation concerns and downside by supportive Central Banks. Within the small cap space we still remain attracted to resource companies and continue to retain an overweight position in this sector. Industrials are throwing up more opportunities with an increasing bifurcation of valuations driven by the slowing domestic and global economies. Although the outlook for the next year for many of these domestic demand companies looks uncertain, valuations have become increasingly more attractive, warranting further analysis.

Investment Objective

The Investment objective for the Ellerston Australian Small Companies Fund is to outperform the S&P/ASX Small Ordinaries Accumulation Index (Benchmark).

Investment Strategy

The Fund's active, research-driven approach seeks to identify a concentrated portfolio of smaller companies with sound businesses, attractive earnings profiles and supportive industries, which are trading at a discount.

Key Information

Strategy Inception Date	10 October 2013
Fund Net Asset Value	\$0.9915
Liquidity	Daily
Application Price	\$0.9940
Redemption Price	\$0.9890
No Stocks	56
Management Fee	1.25% p.a.
Buy/Sell Spread	0.25%
Performance Fee	20.5% p.a.
Firm AUM	Over \$5 Billion

Returns FYTD for the fund have been particularly disappointing, considering we typically deliver significant “alpha” in a down or sideways markets. This has necessarily resulted in some analysis in determining “what is different” and do we need to change our investment approach. From an industry perspective, the greater level of capital in the small cap space has probably diminished the “small cap effect” and reduced excess returns. An industry generating above average returns will attract capital resulting in a lowering of returns over time. This appears to have happened in the small cap space over the past few years. Looking internally, we are not ready to retreat from a process that has delivered excess returns over the last 15 years on the basis of a couple of years of inadequate returns. “One sparrow doesn’t make a summer”. Like all managers, we need to ensure less “own goals” and ensure portfolio management is improved and this is the focus internally within the process and philosophy developed over a number of years.

You and I both are looking forward to better returns in the near future.

ELLERSTON AUSTRALIAN SMALL COMPANIES FUND PERFORMANCE

Returns (%)	Net [^]	Gross	Benchmark	Net alpha	Gross alpha
1 Month	-2.43	-2.37	-0.12	-2.31	-2.25
3 Months	7.94	8.13	12.59	-4.65	-4.46
Rolling 12 Months	1.94	2.69	5.78	-3.84	-3.09
2 Years p.a.	7.59	8.66	10.29	-2.70	-1.63
3 Years p.a.	10.28	11.23	11.40	-1.12	-0.17
5 Years p.a.	8.89	10.22	7.97	0.92	2.25
Since Inception p.a.	8.92	10.25	7.81	1.11	2.44

Source: Ellerston Capital Limited

ELLERSTON AUSTRALIAN SMALL COMPANIES FUND TOP HOLDINGS

Top 5 holdings as at 31 March 2019	Sector	%
Cleanaway Waste Management Limited	Industrials	4.37
Cooper Energy Limited	Energy	3.90
Ausdrill Limited	Materials	3.88
Viva Energy Group Limited	Energy	3.41
Tassal Group Limited	Consumer Staples	3.39

Source: Ellerston Capital Limited

[^] 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. Past performance is not a reliable indicator of future performance.

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	Over \$700 Million
FUNDS UNDER MANAGEMENT – SCF UNIT TRUST	\$10 Million
APPLICATION PRICE	\$0.9940
REDEMPTION PRICE	\$0.9890
NUMBER OF STOCKS	*56
INCEPTION DATE	10 October 2013

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DISCLAIMER

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