Ellerston Capital

Ellerston Australian Market Neutral Fund

Performance Report | September 19

PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	3 Year (p.a.)	5 Year (p.a.)	Since Inception (p.a.)
Net^	3.48%	6.24%	16.49%	2.43%	0.65%	3.26%	6.78%
Benchmark*	0.08%	0.26%	0.61%	1.36%	1.45%	1.69%	1.86%
Alpha	3.40%	5.98%	15.88%	1.07%	-0.80%	1.57%	4.92%

Source: Ellerston Capital

^Net return figure is calculated after fees & expenses. Past performance is not a reliable indication of future performance
*RBA Cash Rate

PORTFOLIO CHARACTERISTICS

KEY PORTFOLIO METRICS

Positive months	66%	**Net Equity Exposure**	25.0%
No. Relative Value positions	93	**Gross Equity Exposure**	193.3%
No. Special Situations	36	**Correlation Coefficient (vs ASX 200 Accum)**	6.18%
Beta Adjusted	5.9%	**Net Sharpe Ratio (RFR = RBA Cash)**	0.91

SECTOR ALLOCATION

Sector	Long Equity	Short Equity	Net Equity
Financials	39.8%	-41.0%	-1.2%
Industrials	42.9%	-11.2%	31.7%
Resources	22.0%	-21.6%	0.4%
Index	4.5%	-10.3%	-5.9%
Total	**109.2%**	**-84.1%**	**25.0%**

COMMENTARY

The Fund produced a net return of +3.5% in September, outperforming the benchmark return of +0.1%. Both Special Situations (+3.5% gross) and Relative Value (+0.1% gross) added to performance, with the increase in deal flow and corporate activity reflected in the higher contribution from Special Situations in the period. Net Equity Exposure was +25% at the end of September, with a beta-adjusted net of +5.9%. Gross Equity Exposure closed the month at 193%.

We had mixed results within Media, with one pair adding and one pair detracting from performance. QMS Media (+12.4%) had a busy period, with the company completing both the acquisition of Stride Sports Management and the merger of QMS NZ with MediaWorks. The company now has three clearly defined divisions, with investors applauding the increased transparency. A paired position between QMS and Nine Entertainment (+0.8%) added to the value of the Fund. Our other Media position, featuring oOh!media and Nine Entertainment, detracted from performance, with investors continuing to be concerned about oOh!Media's balance sheet.

Our paired position between Village Roadshow (+4.0%) and Event Hospitality (+7.4%) added value, with Village continuing to grind higher following the release of its results in August. Despite the recent rally, Village trades at an FY20 EV/EBITDA of just 5.6x, compared with Event which trades at 9.8x.

The share price of Carindale Property (-3.3%) continues to flounder, despite reporting results in line with guidance and confirming an NTA that is +20% above the current share price. Carindale also announced the introduction of Kmart to replace David Jones on level two of the centre, which is expected to further diversify the rental income. In spite of the positive news, Carindale underperformed the sector, with the positions paired with BWP Trust (+1.3%) and Aventus Retail (+2.7%) detracting value from the Fund.

Investment Objective

The Fund targets Absolute Returns with an annualised return objective of 5% above the RBA Cash Rate over rolling five year periods.

Investment Strategy

The Fund will seek to provide investors with a return profile that has low correlation with traditional asset classes. The Fund aims to generate positive returns in all market environment by reducing the majority of market risk and focusing on capital preservation and alpha generation. The Fund will utilise a Relative Value and a Special Situations strategy.

Key Information

Strategy Inception	3 June 2013
Portfolio Manager	Paul Drzewucki
Application Price	$1.0374
Net Asset Value	$1.0348
Redemption Price	$1.0322
Liquidity	Daily
Management Fee	1.20%
Performance Fee	20% of outperformance
Buy/Sell Spread	0.25%/0.25%

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The spread between the Australian and UK listings of both BHP Group (+4.4%) and Rio Tinto (+5.8%) widened during the period, detracting from the performance of the Fund.

The long-awaited capital raise for Superloop (+11.7%) was announced during the month, with the stock closing higher, adding value to the Fund. The company raised $90m via a non-renounceable Entitlement Offer and Institutional Placement, with the proceeds use to reduce net debt to $7.5m, and also provide a $60m funding runway for future growth capital.

The share price of Infigen Energy (+15.3%) continued to outperform in September, following a takeover bid for electricity retailer ERM Power (+1.0%) in August by Royal Dutch Shell. Despite the share price performance, we continue to maintain our holding in Infigen, with the stock trading at a significant discount to listed-peers. Corporate activity in the sector continued during September, with Federation Asset Management agreeing to purchase an 18.4% stake in Windlab (-10.4%), an ASX-listed wind farm developer, owner and asset manager.

A delay in the CE mark certification process for Imricor Medical Systems (-9.7%), led to a fall in the share price, detracting from the Fund's performance in the month. Imricor develops MRI-compatible products for procedures to treat abnormal heart rhythms, and was previously expecting regulatory approval in Europe for their catheter by the end of the September quarter.

At the end September, Nufarm (+17.0%) announced the sale of its Latin American business to Sumitomo for $1.18b, enabling the company to eliminate the balance sheet risk with net debt/EBITDA falling from approximately 3.0x to 0.7x. With the balance sheet repaired, the implied spread for the Nufarm hybrids (+5.9%) narrowed, adding value to the Fund's long position.

Our holding in Uniti Group (+12.9%) added to the performance of the Fund in the period, following a capital raise and the acquisition of LBNCo in August. Uniti is an Internet Service Provider (ISP) that delivers fixed line and fixed wireless broadband internet to residential, business and enterprise customers. The acquisition of LBNCo provides Uniti with a builder and wholesale operator of private fibre networks, predominately comprised of fibre-to-the-premises connections, including multi-dwelling units and residential estates.

ACTIVITY

Relative Value – Gross Contribution +0.10%

We capitalised on the underperformance of Atlas Arteria (-6.5%) in early September, establishing a long position and hedging it with a short in Sydney Airport (-4.7%). Atlas Arteria is a direct infrastructure fund that has interests in four international toll roads – APRR (France), Dulles Greenway (USA), ADELAC (France) and Warnow Tunnel (Germany). Only the APRR and Dulles Greenway interests have any value of significance and Atlas is currently pursuing a restructure of APRR-related agreements that may result in a change of control in the asset. We believe that Sydney Airport is overvalued and in a separate pair, held a long in Transurban (-1.7%) that was also hedged with Sydney Airport. The share price of Sydney Airport fell away by the end of the month and both infrastructure pairs were unwound.

Centuria Capital (+2.3%) raised $100m in equity during the month, with the proceeds used to support an increased co-investment in Centuria Metropolitan REIT (+3.6%) and to retire the 2021 fixed rate corporate bonds. We participated in the equity placement, hedging the exposure with Charter Hall Long WALE REIT (-1.7%).

A block trade in Aventus (+2.7%) facilitated the unwinding of paired positions that featured Aventus as a hedge in pairs including Abacus Property (-1.3%), Centuria Capital (+2.3%) and Ingenia Communities (+3.3%).

We were active in the energy sector during September, establishing longs in Carnarvon Petroleum (+6.8%) and Senex (-10.4%) and hedging the exposure with the outperforming Santos (+7.2%). The share prices of both Carnarvon and Senex has lagged in recent times, following an equity raise by Carnavon and a block sale by the majority shareholder in Senex.

Special Situations – Gross Contribution +3.50%

We initiated a position in Ridley Corporation (-7.9%) during September, capitalising on an increase in liquidity due to the stock's deletion from the S&P/ASX300 index. Ridley is Australia's largest processor of stockfeed products, with production mills and distribution facilities across eastern and southern Australia. The company is largely ignored by institutional investors, with only two sell-side analysts covering the stock. As a result, the company trades at an FY20 PER of 14.9x with mid-teen EPS growth forecast for FY21 and FY22. A new CEO was appointed in August, following the resignation of the long-term CEO and Managing Director earlier in the year.

A block trade in payments company Sezzle (-5.6%) provided an opportunity to re-establish a long position, with the share price underperforming peers since listing in July. The "buy-now-pay-later" sector has been incredibly strong in recent times, with Afterpay Touch (+15.8%), Zip Co (+36.4%) and Flexigroup (+40.3%) all rallying during in September.

We sold our remaining holding in Paradigm Biopharmaceuticals (+79.4%) following a period of outperformance. Our position in Ruralco Holdings (+0.2%) was removed from the portfolio with the conclusion of the takeover by Agrium Australia.

MARKET COMMENTRY

Market Overview

Equity markets were up strongly in September, with Developed Markets up 2.2% in US dollar terms and Emerging Markets up 1.9%. Globally, September marked the 2nd largest monthly outperformance of global value vs. growth in the past decade. Investors positioned themselves in extreme "risk off" positions, which combined with a sustained period of value underperforming, saw a sharp rotation back towards value as global bond yields rose. Not surprisingly, the US Federal Reserve cut rates for the second time this year, and the European Central Bank announced a comprehensive stimulus package. Financials and Energy stocks were among the strongest performers. Markets rallied despite central banks' concerns over a global growth slowdown, as evidenced by announcements of further monetary and fiscal stimulus.

USA

The S&P 500 Index and the Dow Jones Industrial Average Index were in the black in September, returning +1.9% and +2.1% respectively. The NASDAQ was also in positive territory, but with a more modest return of +0.5%.

US economic data was mixed: manufacturing ISM missed, falling to 49.1 (consensus: 51.3, previous: 51.2) but composite non-manufacturing bounced to 56.4 (consensus: 54, previous: 53.7). Also, non-farm payrolls missed, rising to 130,000, which was below consensus of 160,000. The Federal Reserve cut rates by 25 basis points, taking the benchmark rate to 1.75% - 2.00%, however, President Trump tweeted that he wanted a more aggressive move down. Trade tensions simmered in the background but were off the front pages for now.

Europe

European equities were much stronger across the board, with the Euro Stoxx returning +4.3%. In a dovish surprise, the index was pushed higher after the ECB announced a fresh 5 point comprehensive stimulus package. The deposit rate was cut further into negative territory after the ECB re-launched a QE program of Euro 20bn of asset purchases per month.

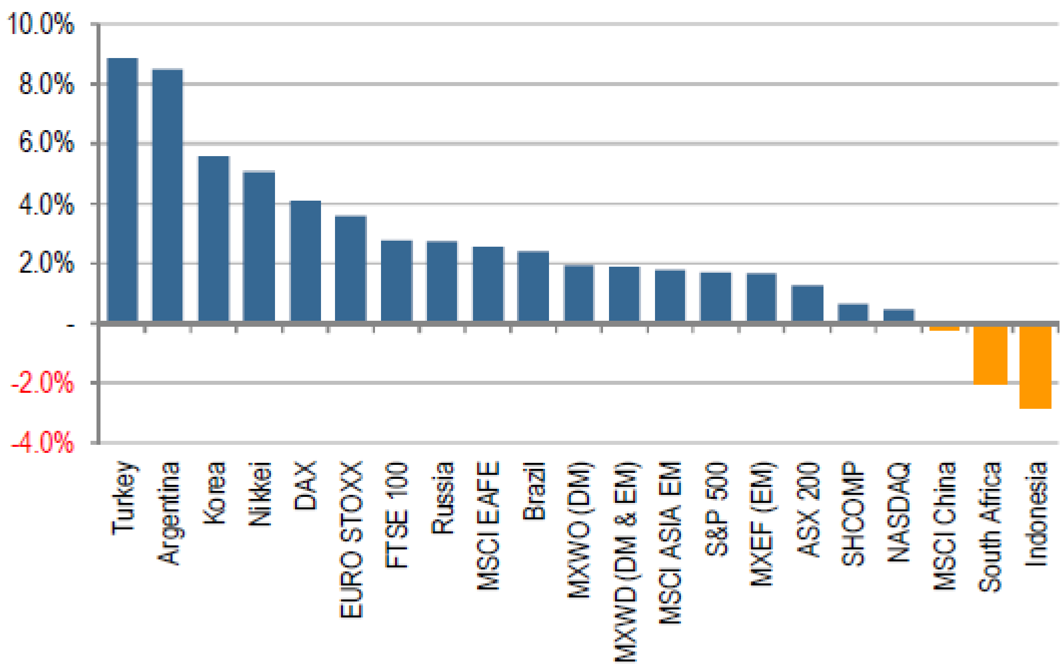
Among the major markets, Germany's DAX was one of the strongest performers with a return of +4.1%, followed by France's CAC 40 which returned +3.7%. In the UK, MPs voted to control the parliamentary agenda backing a bill to stop a "no deal" Brexit by 31 October, whlist towards month end, Britain's Supreme Court ruled Johnson's suspension of Parliament unlawful. The FTSE 100 bounced sharply, up almost 3%, but economic data in Europe continued to moderate: flash Eurozone manufacturing PMI for September missed, falling to 45.6 (consensus: 47.3, previous: 47.0) and the composite PMI moderated to 50.4 (consensus: 52.0, previous: 51.9), justifying further stimulus from the ECB.

Asia

Asian equities were also stronger in the month as talk of global stimulus tempered the extreme bearishness of investors. Despite the protests in Hong Kong intensifying, the Hang Seng Index was up 1.9%. Japan's Nikkei 225 was the best performer of the major markets, up +5.7%, followed by Korea's KOPSI Composite Index which was up 4.8%.

Chinese economic data was broadly weaker. The trade surplus of $34.8 billion was below expectations (consensus: $44.3 billion), and September manufacturing PMI fell to 49.8, again below consensus expectations of 49.6. The Chinese SSE Total Market Index delivered a very modest return of +0.4%.

Global Equity Markets' Performance in the month of September 2019

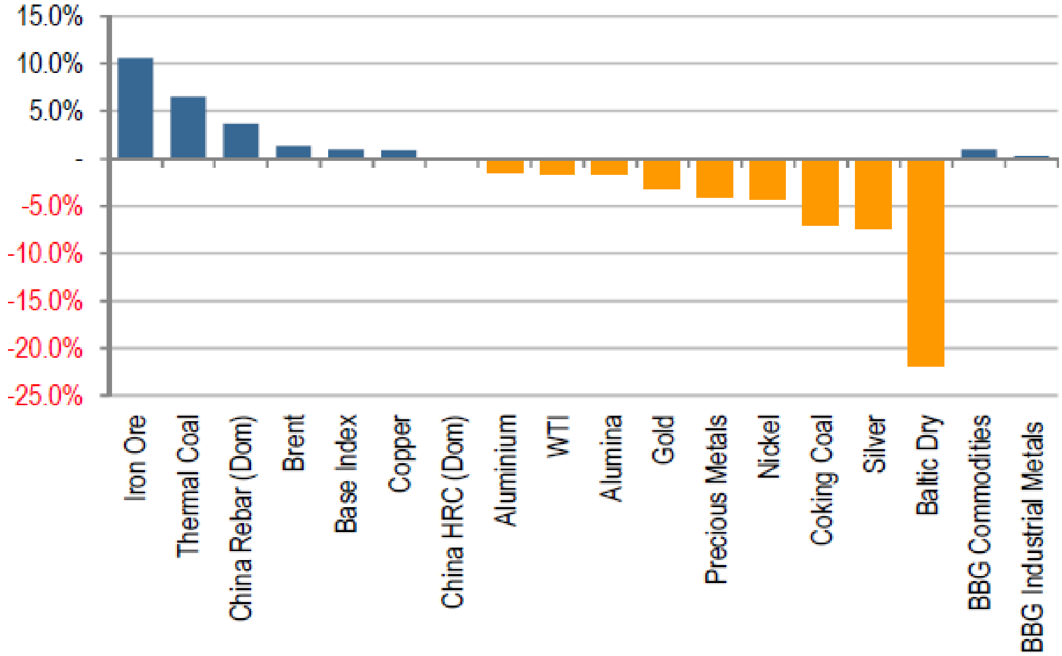


Source: JP Morgan, Bloomberg.

Commodities

The commodities index was up in September. Among the Bulk commodities, Iron Ore rebounded and closed up 10.6% to US$93.8/t, Coking Coal was down 7.1%, but Thermal Coal rose 6.5%. The Base Metals Index was stronger up 1.0%, with Copper up 1%. Nickel was the laggard, down 4.4%. Oil prices were volatile in the month as two Saudi oil processing facilities were attacked by drones. The facilities were shut down for immediate repairs, which resulted in 5.7mb/d or over half of Saudi Arabia's total oil production temporarily being cut (around 5% of global oil supply). Brent Crude oil futures prices initially surged 15%, but as production was brought back on line, the oil price retraced from those highs. Brent soon normalized and ended the month +1.4% or US$59.25/bbl. Precious metals were weaker as a "risk on" mindset took hold: Gold was down 3.2% and silver was down 7.3%.

Commodity Performance in September 2019



Source: JP Morgan, Bloomberg.

Bonds

Despite ongoing weakening global economic data, the relentless compression in bond yields came to a shuddering halt, with global bond yields rising sharply in early September, but then drifted lower. US 10-year bond yields rose 18 basis points to 1.68%. In the US, August retail sales and consumer sentiment were better than expected and this may have contributed to the sell-off in US bonds. The Norwegians bucked the trend and lifted their official rates, causing the Krone to rally. Australian 10-year bonds rose 7 basis points to 0.96% and are now 72 basis points below 10-year US yields.

Australia

The S&P/ASX 200 Accumulation Index ended the month up 1.8%. The index is now up 22.6% for the calendar year to date.

In September, the best three performing sectors in terms of their contribution to the index's performance were Financials (+4.1%, with all the major banks up strongly), Materials (+3.1% driven mainly by BHP Group and Rio Tinto) and Energy (+4.7% with Oil Search up 11.5%). The bottom three sectors were Health Care (-2.5%), Real Estate (-2.3%) and Communication Services (-3.0%). The ASX 200 Resources Accumulation Index was the best performer, with a return of +3.0%. The Small Ordinaries Accumulation Index returned +2.6%, while the ASX 200 Industrial Accumulation Index rose 1.6%.

The top five stocks that detracted from the performance of the S&P/ASX 200 Accumulation Index were CSL (-15 points), Telstra Corporation (-14 points), Newcrest Mining (-10 points), Dexus (-6 points) and a2 Milk Company (-6 points).

The top five stocks that added to the positive index return were dominated by the big banks, including National Australia Bank (+36 points), Australia and New Zealand Banking Group (+29 points), Westpac Banking Corporation (+28 points), BHP Group (+27 points) and Commonwealth Bank of Australia (+18 points).

The RBA September minutes were more dovish than expected and business confidence fell further. In early October, the RBA cut rates by 25 basis points taking official rates to 0.75%. The RBA is widely expected to cut rates by a further 25 basis points in the coming months.

The Australian dollar was up marginally against the US dollar, and ended the month at 0.68 cents.

CONTRIBUTION

Relative Value Gross Contribution +0.10%			
Positive		**Negative**	
NINE ENTERTAINMENT CO HOLDINGS LTD - QMS MEDIA	0.72%	RIO TINTO - RIO TINTO	-0.30%
CENTURIA INDUSTRIAL REIT - CHARTER HALL LONG WALE REIT	0.23%	BWP TRUST - CARINDALE PROPERTY TRUST	-0.25%
EVENT HOSPITALITY AND ENTERTAINMENT LTD - VILLAGE ROADSHOW	0.13%	AVENTUS RETAIL PROPERTY FUND - CARINDALE PROPERTY TRUST	-0.21%
CENTURIA METROPOLITAN REIT - NATIONAL STORAGE REIT	0.12%	BHP BILLITON - BHP BILLITON	-0.19%
SYDNEY AIRPORT - TRANSURBAN GROUP	0.07%	NINE ENTERTAINMENT CO HOLDINGS - OOH!MEDIA	-0.14%

Special Situations Gross Contribution +3.50%			
Positive		**Negative**	
INFIGEN ENERGY	0.82%	POWERWRAP LTD	-0.08%
IMPEDIMED LTD	0.59%	IMRICOR MEDICAL SYSTEMS-CDI	-0.06%
NUFARM FINANCE NZ LTD - NSS	0.54%	KALIUM LAKES LTD	0.00%
SUPERLOOP LTD	0.52%	JOHNS LYNG GROUP LTD	0.00%
UNITI WIRELESS LTD	0.29%	ABANO HEALTHCARE GROUP LTD	0.00%

Top 10 Relative Value Positions	
RIO TINTO - RIO TINTO	EVENT HOSPITALITY AND ENTERTAINMENT LTD - VILLAGE ROADSHOW
BHP BILLITON - BHP BILLITON	NINE ENTERTAINMENT CO HOLDINGS LTD - QMS MEDIA
BWP TRUST - CARINDALE PROPERTY TRUST	ABACUS PROPERTY GROUP - CENTURIA INDUSTRIAL REIT
APN INDUSTRIA REIT - ELANOR RETAIL PROPERTY FUND	CHARTER HALL RETAIL REIT - SHOPPING CENTRES AUSTRALASIA
MIRVAC GROUP - STOCKLAND	GOODMAN GROUP - GOODMAN GROUP

Top 10 Special Situation Positions	
PUT SPREAD ON AS51	APN INDUSTRIA REIT
NUFARM FINANCE NZ LTD - NSS	IMPEDIMED LTD
INFIGEN ENERGY	UNITI WIRELESS LTD
SUPERLOOP LTD	SUNCORP GROUP
KALIUM LAKES LTD	VOLPARA HEALTH TECHNOLOGIESS

All holding enquiries should be directed to our registrar, Link Market Services on 1800 992 149 or ellerston@linkmarketservices.com.au

Should investors have any questions or queries regarding the Fund,

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