

Ellerston Low-Vol Income Strategy Fund

Performance Report | October 19

PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	2 Year p.a.	Since Inception (p.a.)
Net [^]	0.37%	1.69%	7.24%	-	-	7.24%
Benchmark*	-0.35%	-0.91%	7.59%	-	-	7.59%
Alpha	0.72%	2.60%	-0.35%	-	-	-0.35%

Source: Ellerston Capital

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

*S&P/ASX 200 Accumulation Index

COMMENTARY

Despite global markets broadly rallying in October, the ASX 200 Accumulation Index declined by 35 bps, led down by Energy, Consumer Staples & Utilities. The fund managed to defy this decline, rising 37 bps on a net basis and thereby outperforming the benchmark by 72 bps. Strong sector performance in Financials (underweight major banks) and Materials (underweight BHP & Newcrest Mining) was a key driver while Consumer Discretionary (overweight Flight Centre & Treasury Wines) detracted from performance.

On a relative performance basis, not owning much of the major banks (ANZ, CBA & NAB) contributed 70 bps due to continued concerns over bank profitability, dividend sustainability and regulatory capital requirements whilst key overweights in CSL, Aristocrat Leisure and Macquarie Group added 30 bps collectively. Conversely, Flight Centre detracted 30 bps due to concerns over slowing demand in their leisure business while Treasury Wines detracted 20 bps as concerns over the US – China trade war weighed on the stock.

During the month we exited our GPT Group position on valuation grounds, with the stock trading at a 15% premium to its long term valuation average. We also reduced our position in Resmed Incorporated, who produced a very strong Q1 2020 result which saw the share price jump over 10%. We still maintain an overweight position in the stock given the company's market leading position in global masks and devices for the treatment of sleep apnea and other respiratory conditions. We also purchased a position in Kathmandu Holdings via participation in an equity capital raising as the company entered into an agreement to acquire Rip Curl. The company expects the acquisition to be 10% earnings per share accretive in FY20. The cash dividend yield is around 5.6%, growing at 8% p.a. Finally, we added Spark New Zealand to the portfolio due to the stocks attractive yield, robust valuation metrics, strong balance sheet and medium term growth profile driven by mobile, cloud and cost savings.

In October, Emerging Markets (+4.2%) outperformed Developed Markets (+2.6%) by a reasonable margin. Financial markets took some comfort from easing geopolitical tensions, with signs that the US and Chinese authorities were edging closer to some agreement on their trade dispute and the UK stepping back from its Brexit precipice. The US Fed cut rates for the third time this year and global central banks reiterated their accommodative stance, which helped bolster investor sentiment. Against the backdrop of a positive earnings season, the S&P 500 Index made further gains of +2.2% in October, hitting all-time highs at the end of the month. The Dow Jones Industrial Average Index was up a more modest +0.6%. The NASDAQ was the strongest performer, with a return of +3.7%.

US-China discussions on trade oscillate wildly but appeared to be more constructive in general in October. Financial markets were buoyed by the generally positive sentiment on trade. But US economic data suggested that the economy is fast losing momentum, especially in the trade-dependent manufacturing sector. The manufacturing PMI data indicated that the manufacturing side of the economy is contracting. Consumer confidence was also weaker in October. Not surprisingly, the Fed cut rates by 25bps for the third time this year but signalled its intention to pause in the easing cycle. Markets took their lead from better than expected 3Q earnings on average and squeezed higher.

The commodities index rose 1.9%. Precious metals were stronger in October, as both Gold (+2.8% to US\$ 1,968/oz) and Silver (+6.3%) shone. Among the bulks, Iron Ore had a poor month, down 5.5% with Thermal Coal weaker too, down 4.5%. Brent was up 1.9% to US\$59.62/bbl. Base metals were mixed with Copper up 1.7% but Nickel and Alumina were down 3.1% and 4.1% respectively.

As we saw last month, bond yields appeared to have stemmed their seemingly inexorable decline. The US 10-year bond yield moved up to 1.69% while the Australian 10-year bond yield backed up sharply to 1.14%. The Australian 10-year bond yield is now 55 basis points below the US 10-year bond.

Investment Objective

The investment objective of the Ellerston Low Volatility Income Strategy Fund ("ELVIS" or "the Fund") is to provide investors with returns and income growth greater than the S&P/ASX 200 Accumulation Index over rolling 3-5 year periods.

Investment Strategy

The Fund is a fundamental, bottom up Australian equity strategy with a clear focus on delivering low volatility, sustainable income for investors through actively blending multiple, distinct dividend yield strategies throughout the market cycle.

Key Information

Strategy Inception	1 May 2019
Portfolio Manager	Chris Hall
Application Price	\$1.0742
Net Asset Value	\$1.0715
Redemption Price	\$1.0688
Liquidity	Monthly
No Stocks	36
Management Fee	0.70%
Performance Fee*	10%
Buy/Sell Spread	0.25%/0.25%

*10% of the investment return of the relevant class over the Benchmark return, after recovering any underperformance in past periods.

The portfolio broadly maintained its recent increased positioning into cyclical yield as the continued RBA rate cuts and optimism over trade US – China trade talks should provide good support for the materials and consumer discretionary sector. We have also added more “value” stock names as part of the portfolio’s increased exposure to the cyclical part of the market. The beta of the fund (a measure of volatility) has moved marginally higher as a result of this but still sits comfortably at 0.92 vs a market beta of 1.00. The expected dividend growth rate of investee companies held within the portfolio is comfortably above that of the market, at 9.0% vs -4.8% for the ASX 200 .The expected dividend yield of investee companies held within the portfolio is currently 3.60%.

Regards,
Chris Hall - Portfolio Manager, CIO

PORTFOLIO CHARACTERISTICS

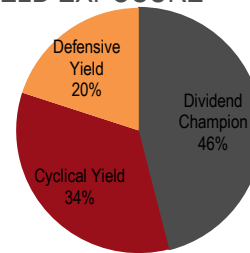
HOLDINGS

Top 10 holdings	Sector	%
CSL Limited	Health Care	7.9%
Macquarie Group Limited	Financials	6.7%
Rio Tinto Limited	Materials	6.0%
James Hardie Industries	Materials	4.9%
Aristocrat Leisure Limited	Consumer Discretionary	4.7%
Goodman Group	Real Estate	4.6%
Sonic Healthcare Limited	Health Care	4.5%
Woodside Petroleum Ltd	Energy	4.0%
Westpac Banking Corporation	Financials	4.0%
Caltex Australia Limited	Energy	3.9%

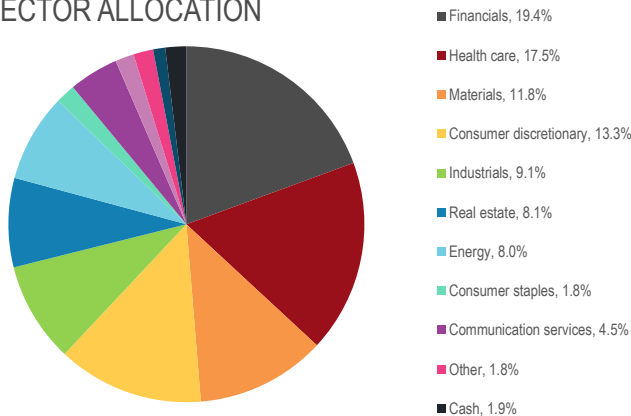
KEY PORTFOLIO METRICS

Fy20(E)	Fund	Benchmark
Price/Earnings (x)	19.9	17.7
Dividend Yield (%)	3.6	4.1
Dividend Growth rate (%)	9.0	-2.2
Beta*	0.92	1.00

PORTFOLIO YIELD EXPOSURE

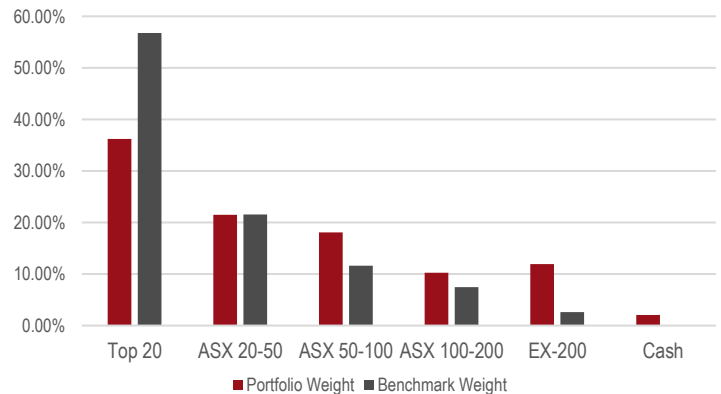


SECTOR ALLOCATION



Source: Ellerston Capital

MARKET CAPITALISATION



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, please contact our Investor Relations team on 02 9021 7797 or info@ellerstoncapital.com or visit us at <https://ellerstoncapital.com/>

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