ELLERSTON CAPITAL

Ellerston Australian Market Neutral Fund

Performance Report | June 20

PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	3 Year (p.a.)	5 Year (p.a.)	Since Inception (p.a.)
Net^	2.28%	17.46%	-6.74%	7.99%	0.91%	2.72%	6.29%
Benchmark*	0.02%	0.06%	0.22%	0.67%	1.21%	1.42%	1.72%
Alpha	2.26%	17.40%	-6.96%	7.32%	-0.30%	1.30%	4.56%

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**	22%
No. Relative Value positions	43	**Gross Portfolio Exposure**	221.1%
No. Special Situations	25	**Correlation Coefficient (vs ASX 200 Accum)**	53.53%
Beta Adjusted	17.6%	**Net Sharpe Ratio (RFR = RBA Cash)**	0.50

SECTOR ALLOCATION

Sector	Long Equity	Short Equity	Net Equity
Financials	31.3%	-19.7%	11.6%
Industrials	43.0%	-10.3%	32.7%
Resources	32.4%	-24.9%	7.5%
Index	10.1%	-40.4%	-30.3%
Total	**116.8%**	**-95.3%**	**21.5%**

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	$1.0520
Net Asset Value	$1.0494
Redemption Price	$1.0468
Liquidity	Daily
Management Fee	1.20%
Performance Fee	20% of outperformance
Buy/Sell Spread	0.25%/0.25%

COMMENTARY

The Fund produced a net return of +2.3% in June, outperforming the benchmark return of +0.0% in the period. For the 2020 Financial Year, the Fund returned +8.0% net, well in excess of both the benchmark and the Australian equity market (-7.7%) over the twelve months. Net exposure was +22.0% at the end of June, with a beta-adjusted net of +17.6%. Gross exposure continued to move higher, closing the period at +221.1%.

Our long-held expectation that Infigen Energy (+56.7%) would one day be the target of corporate action came to fruition in June, with both UAC Energy and Iberdrola launching takeovers in the period. The first bid came from UAC, which is an investment holding company ultimately controlled by the Philippines-listed Ayala Corporation. Following the UAC approach, Spanish-based Iberdrola announced a higher bid, also announcing that it had secured a 20% interest in the company from majority-shareholder The Children's Investment Fund. Our long position in Infigen, hedged with AGL Energy (+1.7%), added to performance in the month.

A long position in Karoon Energy (+6.1%), hedged with Santos (-1.1%), also added value in June, with increasing interest surrounding Karoon's strategic review and their call option over the Bauna oilfield in Brazil. With the stock still trading well below cash-backing and the oil price up over 10% in the period, we added to the paired position. We expect a decision on Bauna in the September quarter, with a capital return announced if the company does not proceed with the acquisition.

An announcement from ARA Asset Management of its intention to make a proportional off-market takeover bid to acquire 29% of Cromwell Property (+14.8%) sent Cromwell's share price higher, detracting value from the Fund. Despite the bid, Cromwell remains in the unenvious position of having sector-high gearing and a portfolio that is overweight Polish retail assets. We have the position hedged with a long in Charter Hall Social Infrastructure (-4.6%), which has a solid balance sheet, strong management and trades at a 23% discount to NTA.

The spread between the Australian and UK listings of both BHP Group (+3.4%) and Rio Tinto (+4.9%) widened during the period, detracting from the performance of the Fund.

The biggest detractor from performance in the month was the cost associated with our index derivative position, which is used to hedge the equity exposure of the Fund.

Our long position in Damstra Holdings (+44.0%) added value in the period, with the company announcing the acquisition of SmartAsset Software, a provider of end-to-end enterprise asset management software. Whilst the acquisition was relatively modest in value (approximately $450k), there is a significant opportunity to cross-sell the integrated solution to existing Damstra clients. The Damstra share price was also helped along by an initiation report from a sell-side analyst that suggested a price target more than 40% higher than the share price at the time the report was published.

The Atomos (-24.8%) share price came under pressure in June, closing the month below the price of last month's equity raise and detracting from the Fund's performance. The company raised $12.6m in May to expand into the streaming market and provided a buffer against any further COVID-19 shocks. Management has also taken the opportunity to reset the cost base and focus resources, to maximise leverage to a recovering market. We participated in the equity placement and remain confident in management's ability to innovate in the video accessory space.

ACTIVITY

Relative Value – Gross Contribution 2.87%

Fast-growing telecommunications company Uniti Group (-7.6%) announced the proposed acquisition of rival telco Opticomm (+6.3%) during the month, with the cash-and-scrip deal receiving the approval of the Opticomm board and major shareholders. To fund the cash component of the bid, Uniti also announced a $270m underwritten entitlement offer, with shares offered at a 9.1% discount to last. The acquisition is expected to be 23% EPS accretive (including $10m in cost synergies) in the first full year. We capitalised on the liquidity even, establishing a long position and hedging it with TPG Telecom (+5.1%).

The rebound in the oil price has buoyed our confidence in the ability of Karoon Energy (+6.1%) to settle the proposed acquisition of the Bauna oil field in Brazil. Despite the delays, we expect an announcement in the September quarter, with revised terms that reduce the requirement for debt and stage the payments over time. We accordingly added to our paired position between Karoon and Santos (-1.1%).

We unwound our paired positions between Insurance Australia (-5.6%) and Suncorp (+0.0%), Charter Hall Retail (+5.5%) and Shopping Centres Australasia (-4.7%), Dexus (+4.8%) and GPT Group (+4.5%), and Scentre (-2.7%) and Vicinity (-11.2%), following a narrowing in their respective spreads. We also unwound the paired position between AGL Energy and Infigen Energy after the first takeover bid for Infigen was announced.

Special Situations – Gross Contribution -0.48%

After an incredibly busy May, activity within Special Situations was more muted in June, with the Fund participating in a select number of equity placements including AFT Pharmaceuticals (-16.6%), Alliance Aviation Services (+14.3%), Challenger (-12.0%), Megaport (-12.1%), Openpay (+62.8%) and Uniti (-7.6%).

We established a position in Retail Food Group (+0.0%) during the month, capitalising on a block sale that was cleared at a modest discount to market. Retail Food Group is a developer and manager of retail franchise systems with brands including Gloria Jeans, Michel's Patisserie, Brumby's Bakery, Crust and Pizza Capers. The company provided a trading update late in the month, upgrading FY20 EBITDA guidance by approximately 6% and providing comfort around FY21 forecasts. The stock trades on an FY21 Price/Earnings ratio of just 7.5x, with upside to earnings if we come out of the COVID-19 environment more quickly.

We sold our remaining holdings in Electro Optic Systems (-17.6%) following a rally in the share price early in the month. We also reduced our exposure to Damstra (+44.0%), Limeade (+5.8%) and Village Roadshow (+4.9%).

MARKET COMMENTRY

Market Overview

As restrictions on mobility were eased around the world, global markets rallied again in June. The Australian Dollar remained firm, mainly due to the resilience in the iron ore price. However, towards the end of June, a spike in COVID-19 cases, particularly in the US, weighed on investor sentiment. But it didn't impact what turned out to be the second-best quarter for global equities since the turn of the century. While price momentum continues to be positive, the risks from the spike in COVID-19 cases and a lack of consensus on the shape and timing of the economic recovery will ensure high market volatility going forward.

USA

In June, despite the rise in the number of COVID-19 cases towards the end of the month (especially in key states like Florida, California and Texas), markets were stronger as the economy was opened up. The S&P 500 was up 2.0%, the Dow Jones was up 2.3% and the NASDAQ Composite was up an impressive 6.1%. As at the end of June, the NASDAQ was up +12.7% for the calendar year-to-date. Investors clearly betting on the ongoing strength of tech-related stocks.

Activity indicators were mixed. The manufacturing ISM improved to 43.1, which was slightly weaker than consensus expectations. While economic data was negative, there were signs of improvement. May retail sales surged +17.7% month-on-month, and May housing starts lifted 4.3%.

Europe

European equities, which had been previously hit very hard, also participated in the rally on hopes of a strengthening global recovery, as economies commenced opening up again in that region. The Euro STOXX 50 closed the month up 6.4%. Among the major exchanges, the UK's FTSE 100 recorded a 1.7% gain, France's CAC 40 was up +5.4%, and Germany's DAX ended the month up +6.3%.

Activity indicators in Europe appear to be improving. Flash Eurozone manufacturing PMI for May was ahead of expectations, coming in at 46.9 (consensus: 45.0; previous: 39.4).

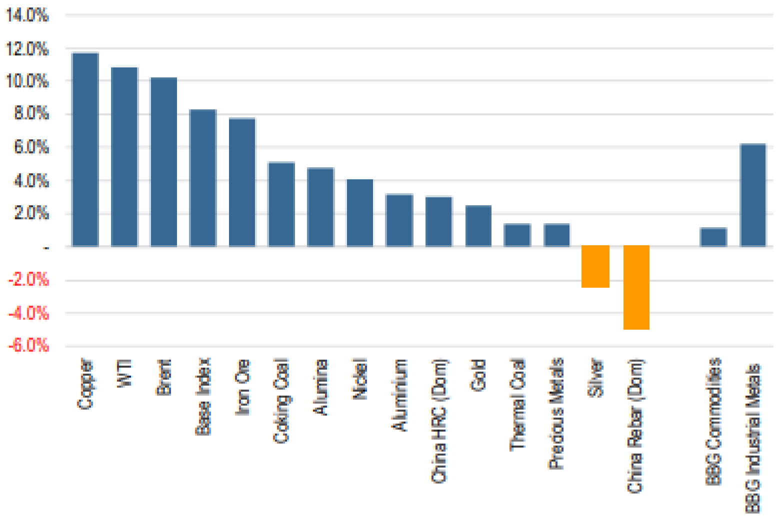
Asia

Asian equities also participated in the rally. The Hang Seng Composite Index rebounded strongly to +8.1% (after last month's negative return), the Chinese SSE Composite Index was up 4.6% and Japan's Nikkei 225 Index was up just shy of 2%. Better Chinese economic data helped sentiment in the region, with China's trade surplus in May ahead of expectations and June manufacturing PMI up, albeit modestly, to 50.9 (consensus: 50.5; previous: 50.6).

Commodities

Global commodity markets continued to rise in June. Gold was stronger again, with rising risk sentiment supporting the price, but the standout performers were Iron Ore (+7.8%) and Brent Crude (+10.2%), driven by the improving China demand outlook for steel, economies coming out of lockdown and the extension of OPEC+ cuts.

Global commodity performance in June 2020



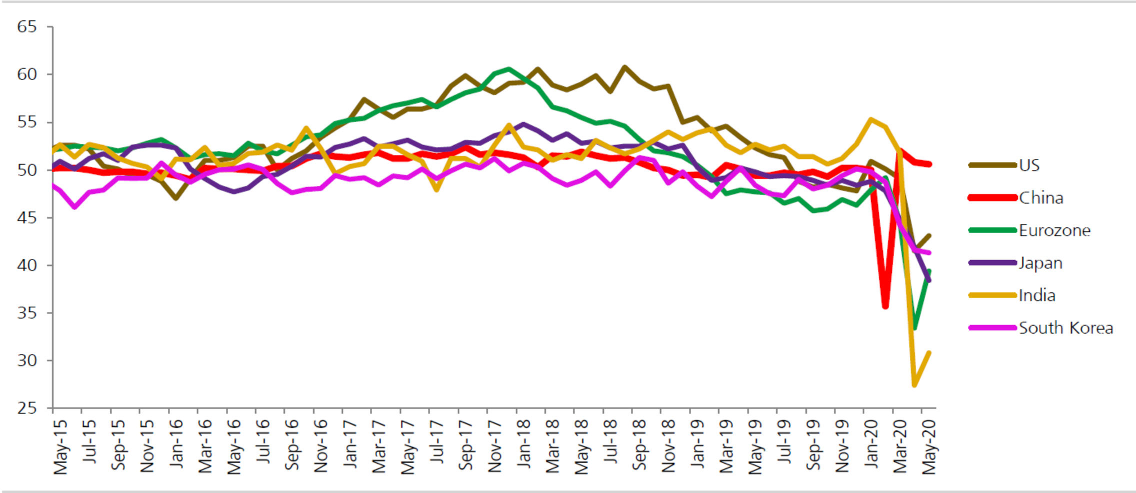
Source: JP Morgan, Bloomberg

The June quarter was better than expected for commodities. Investors expected the June quarter to be challenging, with mobility restrictions driving outcomes and bulk commodities to outperform base metals, given the ongoing supply issues with Vale's Brazilian iron ore operations. While this broadly played out, what surprised was the speed of China's recovery and the resilience of commodity prices in the face of weak demand elsewhere, particularly Europe. What investors overlooked was the greater than expected disruption to commodity supply, especially in emerging markets. This resulted in the Metals & Mining Index rising 28% versus the ASX 200 up 16% in the quarter, with FMG leading the charge, up +38%, BHP +22% and RIO lagging, +14%.

In China a V-shaped recovery appears underway as property and infrastructure investment increase. RoW demand should also bounce back in the 2H and production risks in emerging markets will probably continue to restrict commodity supply, with COVID-19 re-emergence being the greatest risk to this scenario.

Our preferred exposure, particularly to the strength in Chinese commodity demand, as well as RoW recovery, is through S32, given its strong balance sheet, valuation support and key exposures to alumina, as well as the steel making raw materials, manganese and coking coal.

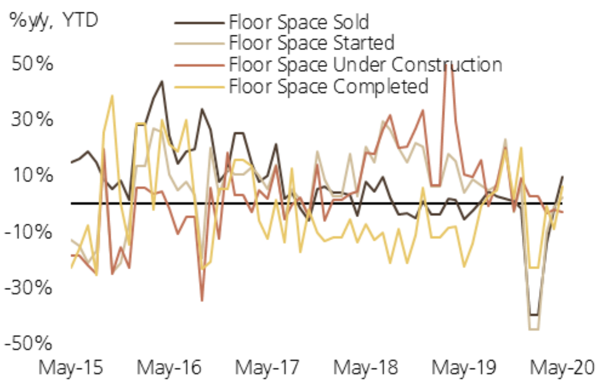
Global PMI: China has rebounded sharply v RoW



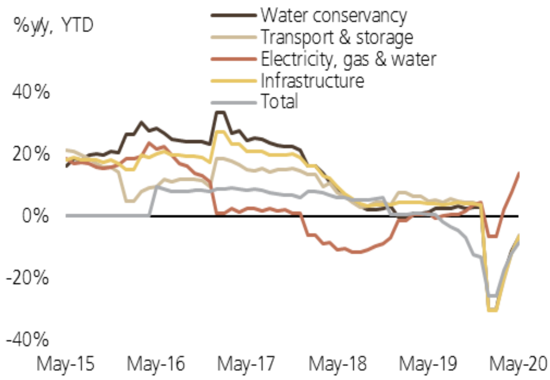
Source: Bloomberg

China was directly impacted first but also strong government stimulus has been responsible.

China Property Activities Continue to Improve



China FAI is Rebounding



Source: UBS Research

Bonds

Global bond yields remained depressed, with 10-year yields in the US flat at 0.65%. Australian 10-year bond yields fell 2 basis points to finish the month at 0.87%.

Australia

The S&P/ASX 200 Accumulation Index was in positive territory again, up another 2.6% in June, despite a surge in COVID-19 cases in Victoria's hotspots causing heightened investor anxiety. The index is now down 10.4% for the calendar year to the end of June 2020. The Australian sharemarket had its best quarter since the turn of the century, with the S&P/ASX 200 Accumulation Index up 16.5% in the June quarter.

As the macro outcome so far has turned out to be better than previously expected, the laggard Financials sector, given its economic sensitivity, was the best performer in terms of contribution to the index's performance, with a contribution of 1.2%. Materials was the second best contributor (+0.5%) followed by Health Care (+0.4%). The bottom three sectors in terms of contribution were Real Estate (-0.10%), Industrials (-0.09%) and Energy (-0.07%).

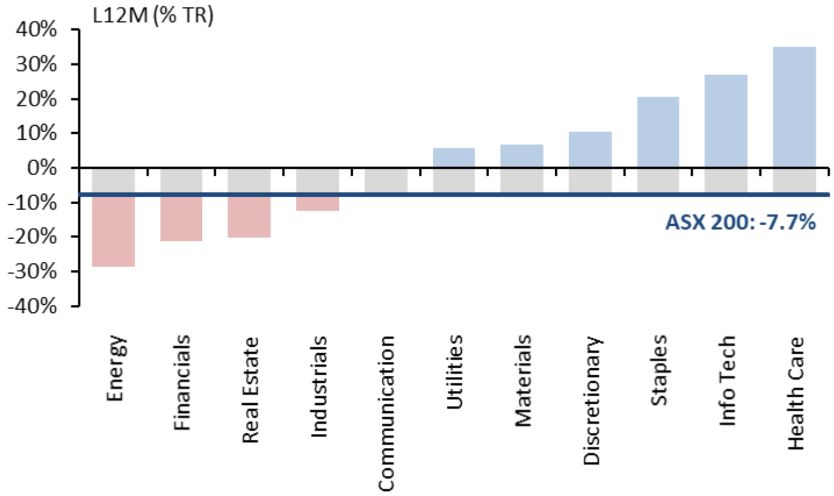
The ASX 200 Industrial Accumulation Index was the best performing sub-index in the month of June, up 2.9%, with the Small Ordinaries Accumulation Index the worst performer, returning -1.9%. The ASX 200 Resources Accumulation Index delivered a credible return of +1.7% and the ASX 200 A-REIT sector gave up some recent gains and ended the month down 1.4%.

The top five stocks that detracted from the performance of the S&P/ASX 200 Accumulation Index were: Telstra Corporation (-8 points), Brambles (-7 points), Northern Star Resources (-7 points), Woodside Petroleum (-6 points) and Vicinity Centres (-5 points).

Conversely, the top five stocks that made a positive contribution to the index's return were Commonwealth Bank of Australia (+62 points), Wesfarmers (+31 points), CSL (+30 points), BHP Group (+22 points) and Afterpay (+18 points).

Not surprisingly, the RBA left rates unchanged in June. The Australian dollar remained strong, closing at 0.69 against the US dollar, given the recovery in key commodity prices.

The ASX delivered -7.7% Total Return in FY2020, the 15th worst Financial year since 1903. Attribution was heavily influenced by Healthcare, whilst Financials were a sizeable laggard, with Technology's share of the Index continuing to grow (now 3.5% of ASX200).



Source: Morgan Stanley Research

CONTRIBUTION

Relative Value Gross Contribution 2.87%			
Positive		**Negative**	
AGL ENERGY LTD - INFIGEN ENERGY	0.86%	CROMWELL PROPERTY GROUP - CHARTER HALL EDUCATION TRUST	-0.31%
APN INDUSTRIA REIT - ELANOR RETAIL PROPERTY FUND	0.52%	TPG CORP LTD - UNITI WIRELESS LTD	-0.27%
KAROON GAS AUSTRALIA LTD - SANTOS	0.48%	RIO TINTO - RIO TINTO	-0.26%
APN INDUSTRIA REIT - GDI PROPERTY GROUP	0.26%	BHP BILLITON - BHP BILLITON	-0.18%
GDI PROPERTY GROUP - GROWTHPOINT PROPERTIES	0.25%	ADELAIDE BRIGHTON - FLETCHER BUILDING	-0.13%

Special Situations Gross Contribution -0.48%			
Positive		**Negative**	
DAMSTRA HOLDINGS LTD	0.72%	PUT SPREAD ON ASX 200	-1.36%
BIGTINCAN HOLDINGS LTD	0.41%	ATOMOS LTD	-0.70%
VILLAGE ROADSHOW LTD	0.32%	IMPEDIMEDD LTD D	-0.60%
SUNCORP GROUP	0.21%	INVEX THERAPEUTICS LLTD	-0.18%
IMRICOR MEDICAL SYSTEMS-CDI	0.20%	PALADIN ENERGY LIMITED	-0.12%

Top 10 Relative Value Positions	
RIO TINTO - RIO TINTO	COLES GROUP LTD - WOOLWORTHS
BHP BILLITON - BHP BILLITON	APN INDUSTRIA REIT - GDI PROPERTY GROUP
KAROON GAS AUSTRALIA LTD - SANTOS	TPG CORP LTD - UNITI WIRELESS LTD
MIRVAC GROUP - STOCKLAND	APN INDUSTRIA REIT - ELANOR RETAIL PROPERTY FUND
CROMWELL PROPERTY GROUP - CHARTER HALL EDUCATION TRUST	CENTURIA INDUSTRIAL REIT - INVESTEC AUSTRALIA PROPERTY

Top 10 Special Situation Positions	
PUT SPREAD ON ASX 200	KALIUM LAKES LTD
NUFARM HYBRID	OPTICOMM LTD
VOLPARA HEALTH TECHNOLOGIESS	ATOMOS LTD
LIMEADE INC-CDI	INVEX THERAPEUTICS LLTD
SUNCORP GROUP	IMPEDIMEDD LTD D

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/

SYDNEY OFFICE

Level 11, 179 Elizabeth Street,
Sydney NSW 2000

MELBOURNE OFFICE

Level 4, 75-77 Flinders Lane,
Melbourne VIC, 3000