ELLERSTON CAPITAL

Ellerston Global Equity Managers Fund (GEMS)

Performance Report | June 2020

PERFORMANCE SUMMARY

Performance*	CYTD	FYTD	3 Year (p.a.)	10 Yr (p.a.)	Since Inception (p.a.)^^
GEMS A	6.99%	19.76%	7.58%	11.21%	12.07%
GEMS B	6.97%	19.76%	7.58%	10.96%	11.91%

Source: Ellerston Capital

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

MARKET OUTLOOK & PORTFOLIO COMMENTARY

STRATEGY GLOBAL: LONG SHORT

Portfolio:

Fiscal Year to June 30, 2020, the Australian ASX 200 was down -7.68%, and the US S&P500 was up +7.51%. **The Fund was up net +19.76%. Net after fees.**

Calendar Year to Date from January 1 to June 30, the Australian ASX 200 was down -10.42%, and the US S&P500 was down -3.08%. **The Fund is up net +6.99%**

For the Month of **June 2020**, **the Fund was up net +0.88%**

As of July 24, the portfolio has a net exposure of circa 48% plus an exposure to gold and silver of circa 16% and has minimal foreign currency exposure.

The Fund has had a strong performance for the month to date in July. We have taken advantage of this and a buoyant month in markets to very materially increase our portfolio hedging, incorporating put options, equity shorts and index shorts.

Performance:

Although the Fund has performed extremely well against all possible benchmarks, we believe that there is an extraordinary opportunity set in front of us from the perspective of a Global Long Short Fund. The ability to pivot quickly and change our net exposures radically, gave us flexibility in a very uncertain world. Flexibility in portfolio structuring allows us to not only move quickly to protect capital but also capitalise on emerging opportunities in stocks and more obscure asset classes.

Investors should rest assured that despite a good performance for the financial year ending June 30 we remain committed first and foremost to preserving capital. Absolute risk adjusted positive returns remain our driver. If we had carried a bit more beta (risk) as we did from March to June 30 our returns could have been substantially better.

Market Commentary:

The first six months of 2020 have been truly extraordinary. Health, economic, financial and social crises manifested themselves all over the world. Lockdowns, trade wars, job losses, record central bank balance sheet expansions, record fiscal stimuli. The list goes on. Volatility ruled, with fear and uncertainty ultimately giving way to unprecedented injections of liquidity and vaccine hopes. The health crisis remains, along with the economic uncertainty, and the desperate need for ongoing stimuli, while the accelerated shift to digital has been breathtaking. Equity markets have rallied extremely hard off their March lows with the S&P 500 trading less than 5% off its all time high and the Nasdaq hitting an all time high in July.

While the rally has been incredible, markets now look somewhat tired. Growth and technology have been the star outsized performers. The Nasdaq is narrowing the breath of its advance. FANG + Apple + Microsoft, which has been at the forefront of the advancing market, appears to be peaking. These companies look bulletproof with their fortress like balance sheets, relentless double-digit revenue growth and in most instances, commensurate earnings growth. However, the new marginal buyers are not apparent, and these stocks, as amazing as they may be, have the potential to underperform and turn down in certain circumstances.

Investment Objective

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

Investment Strategy

The Fund provides investors with exposure to global markets through a long short equity strategy. The strategy overlays fundamental bottom-up stock selection with global macroeconomic and market outlook.

Key Information

Inception Date	1 January 2002
Portfolio Manager	Ashok Jacob
Class A Redemption Price	$1.5694
Class B Redemption Price	$1.5319
Liquidity	Quarterly
No Stocks	77
Gross Exposure	145.03%
Net Exposure	60.94%
Management Fee	1.50%
Performance Fee	16.50%
Buy/Sell Spread	0.25%/0.25%

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The GAAP (Growth At Any Price) Stocks, most of which are leaders in their space, have experienced parabolic moves and are now exhibiting parallels to the Nifty 50 stocks of the 1960's and early 1970's.

*"The **Nifty Fifty stocks** captivated investors for the significant part of a decade prior to its demise in 1973.*

*The 50 stocks identified by Morgan Guaranty Trust represented some of the fastest-growing high quality large sized companies in existence in the latter half of the 1960s. Their popularity among institutional and individual investors sparked a **radical shift from "value" investing to a "growth at any price" style of investing.***

While most of the reasons were sound and logical, the Nifty Fifty school of investors departed from the tenets of sound investing in one aspect — Valuation."

Source: Medium - Nifty Fifty Stock Bubble of the Seventies — Is There a Similarity with Today's Market

"The delusion was that these companies were so good, it didn't matter what you paid for them; their inexorable growth would bail you out.

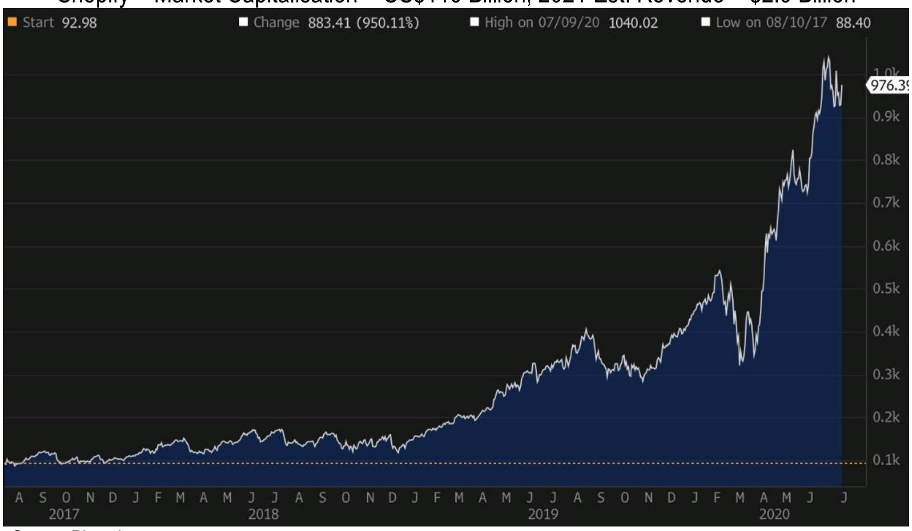
Obviously, the problem was not with the companies but with the temporary insanity of money managers — proving again that stupidity well-packaged can sound like wisdom. It was so easy to forget that no sizable company could possibly be worth over 50 times normal earnings"

Source: Forbes Magazine

Nifty Fifty companies included Pfizer, Coca-Cola, Revlon, Johnson & Johnson, Walt Disney, McDonald's and American Express. Great companies. Some of these companies traded at PE's of greater than 80 times at their peak in 1972. Then reality or common sense kicked in and valuations cratered. For instance, Coca-Cola was as great a company in 1974 as it was in 1972, but the stock was down 50% from its high. The pendulum swung extremely hard the other way. It wasn't until the early 1980s before Nifty Fifty stockholders who bought at the top broke even.

Today's GAAP companies including Shopify, Docusign, Peleton, Coupa, and many others don't trade at non-existent PE multiples, they **trade at extreme Revenue multiples**. They are great franchises where management teams have executed superbly. Much like the Nifty Fifty, the question is not about the companies it's about the valuations. We provide some illustrative examples below.

Shopify – Market Capitalisation = US$116 Billion, 2021 Est. Revenue = $2.9 Billion



Source: Bloomberg

Docusign – Market Capitalisation = US$36 Billion, 2021 Est. Revenue = $1.3 Billion

Source: Bloomberg

Coupa – Market Capitalisation = US$19.6 Billion, 2021 Est. Revenue = $490 Million

Source: Bloomberg

"History doesn't repeat itself, but it often rhymes." said Mark Twain. **Will GAAP rhyme with Nifty Fifty?**

The Gold and Silver opportunity

The performance of Gold is now apparent to everyone. However, what we want to point out is that the outlook for Gold is even stronger at USD $1900 than it was at USD $1550.

While we were beating the drum earlier, the broad-brush theory about relentless expansion of the Fed balance sheet to finance the ballooning US deficit and provide liquidity directly to the market is now well known. “All roads lead to the Fed and the USD” is a truism until it isn’t. The new dynamic that is emerging is the intention of the Fed to supress interest rates to a level that is below the underlying GDP growth rate. This is very promising for asset values and designed to restart the US Economy. The change comes from the direct flow of money from the Government to the average citizen. After the GFC, the heavy lifting by the Fed through the various QE mechanisms, saved and recapitalized the banks.

It got very little money into the hands of the people. Asset prices exploded. We got zero inflation but robust asset price inflation. Money directed into the hands of the people is increasing in velocity and potentially inflationary. Governments and Politicians have a direct to market tool that could be incendiary.

With new stimulus coming in the US, direct to the consumer, velocity of money increases and so does inflation. Imagine a scenario where interest rates remained tethered at meaninglessly low levels, modest inflation appears and the economy remains patchy. Regardless of whether this scenario is what you call ‘stagflation’, the bottom line is that it makes policy makers nervous as the risks of raising and lowering rates become risky at both ends and plays into the hands of gold and even more so with silver.

Low rates with a touch of inflation create a scenario of Negative Real Rates which is a certain boon for the Precious Metal Asset Class.

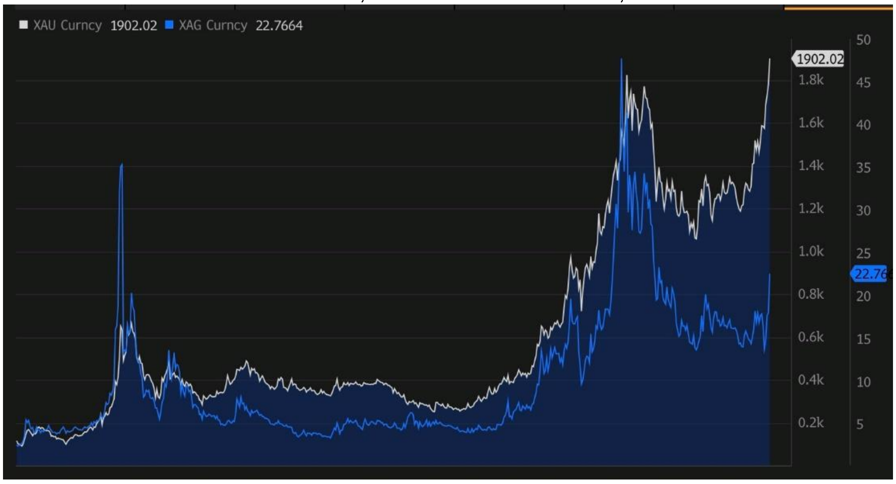
Inflation in any scenario is good for Gold. Inflation without Real Economic Growth is very good for Silver. Inflation has the potential to raise rates and cause the market to rotate from the Growth stocks to the Low Growth Value laggards. We expect extreme market volatility and dislocation in the near future.

We have discussed the portfolio’s material gold exposure and the reasoning behind it numerous times over the past two years. In more recent months we have added exposure to silver.

“As gold is knocking on new all-time highs, I have remembered that historically silver has outperformed gold in bull markets. Some of my previous notes had indicated that from October 2008 to September 2011, gold futures rose 140% while the price of silver jumped 350%, pushing the Gold/Silver ratio to a bottom of 44/1. ***Additional notes had indicated that since 1973 when the U.S. came off the gold standard, it had averaged about 60 to 1, and the all-time low was from a period of 1976-1980 where it had bottomed out at 16/1.”***
Source: Phillip Streible – Kitco Commentaries

The gold/silver ratio, the quantity of **silver** in ounces needed to buy a single ounce of **gold,** has come in to focus. The ratio reached an all time high of 126.5 on March 18, 2020 and currently sits at 78. The chart below is powerful and very telling.

Chart from 1975 to June 25, 2020 – Gold = White Line, Silver = Blue Line



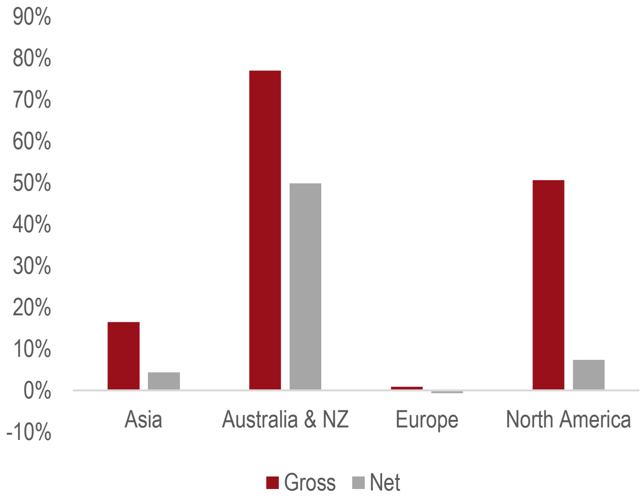
Source: Bloomberg

Market Outlook:

As Fund managers who have been around for a long time, we believe that markets are approaching a turning point again. The "Relentless" outperformance of Growth versus Value has been entirely justifiable. The lack of inflation has made growth the "New Gold". However, the even more stunning performance of hyper growth, large companies trading at 10-50 times revenue has an eerie similarity to many market tops. The pin required to burst that bubble may well be the arrival of inflation. The spectacular return of Gold (Old Gold!) in the past three months could well be a harbinger.

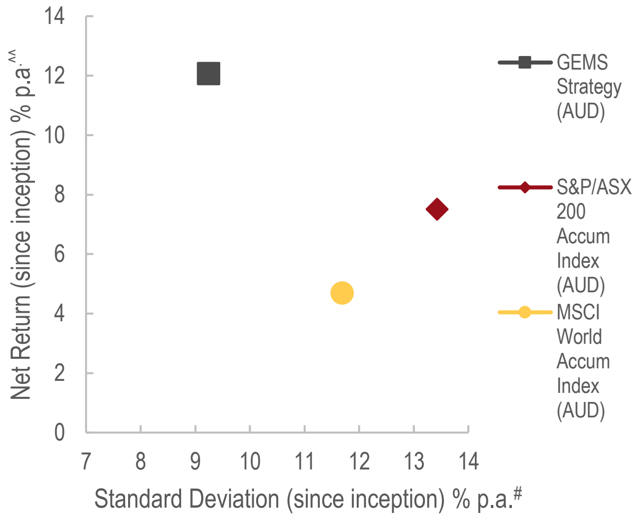
PORTFOLIO CHARACTERISTICS

Market Exposure as a % of NAV



Source: Ellerston Capital

GEMS Strategy Performance & Volatility^



Top 10 Holdings (Alphabetical, Long Only)

- CELSIUS HOLDINGS INC
- FACEBOOK.COM
- GRAINCORP LTD
- GRUBHUB INC
- HEALIUS LTD
- NEXTDC LTD
- RELIANCE INDUSTRIES LIMITED
- SKY CITY ENTERTAINMENT GROUP
- UNITED MALT GROUP LTD
- VANECK GOLD MINERS

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 7701 or info@ellerstoncapital.com

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DISCLAIMER

^ Actual performance for your account may vary from that set out in this newsletter and will vary for investments made in different classes, or at different times throughout the year. Some performance data is estimated and preliminary and subject to change.

^^For the period 1 January 2002 to 30 April 2006, the CPH Group GEMS Portfolio was not operated within a separate fund structure. The underlying investment assets of the CPH Group GEMS Portfolio were owned during that time within corporate entities of the CPH Group for which audited accounts were prepared on an annual basis. Accordingly, in order to provide relevant historical performance information for the period 1 January 2002 to 30 April 2006 (Historical Returns) net returns were calculated on the basis of the actual dollar returns of the CPH Group GEMS Portfolio adjusted to reflect a fund structure similar to the Fund and including all fees. For GEMS B, GEMS A returns have been used between 1 May 2006 and 2 November 2009. The returns of the Fund and the relevant Indices are net of fees, expenses and taxes and assuming distributions are reinvested.

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.

The performance figures presented are for the Ellerston Global Equity Managers Fund GEMS A and B Units. The one month return figure may be an estimate and not the final return. This estimate also impacts other performance information provided. Estimated performance figures are preliminary and subject to change. Returns for other classes may differ slightly. Past performance is not indicative of future performance. Ellerston Capital Limited ABN 34 110 397 674 AFSL 283 000 is the responsible entity of the Ellerston Global Equity Managers Fund ARSN 118 887 095 (Fund). This newsletter has been prepared by Ellerston Capital Limited without taking account of the objectives, financial situation or needs of investors. Before making an investment decision you should consider your own individual circumstances and obtain a copy of the Product Disclosure Statement for the Fund which is available by contacting Ellerston Capital. This material has been prepared based on information believed to be accurate at the time of publication. Assumptions and estimates may have been made which may prove not to be accurate. Ellerston Capital undertakes no responsibility to correct any such inaccuracy. Subsequent changes in circumstances may occur at any time and may impact the accuracy of the information. To the full extent permitted by law, none of Ellerston Capital Limited ABN 34 110 397 674 AFSL 283 000, or any member of the Ellerston Capital Limited Group of companies makes any warranty as to the accuracy or completeness of the information in this newsletter and disclaims all liability that may arise due to any information contained in this newsletter being inaccurate, unreliable or incomplete.