Ellerston Asia Growth Fund

Performance Report, February 21

Investment Objective

To outperform the MSCI Asia Ex Japan (non-accumulation) (AUD) benchmark on a net of fees basis, with a focus on capital growth and downside protection.

Investment Strategy

The Fund's investment strategy is to provide access to a high quality portfolio of primarily large cap Asian Companies using the Manager's distinctively high growth, high conviction and benchmark independent investment approach.
The Manager believes that the trade-off between risk and potential returns at the portfolio level is improved by implementing highest conviction ideas from a filtered universe of securities that offer the best risk/reward.

Key Information

Strategy Inception	4 January 2017
Portfolio Manager	Mary Manning
Application Price	$1.2571
Net Asset Value	$1.2540
Redemption Price	$1.2509
Liquidity	Daily
No Stocks	34
Management Fee	1.00%
Performance Fee	15%
Buy/Sell Spread	0.25%/0.25%
Minimum Investment	$10,000
Minimum Additional Investment	$10,000
Distribution Frequency	Half Yearly (June & December)
APIR Code	ECL1411AU

Performance Summary

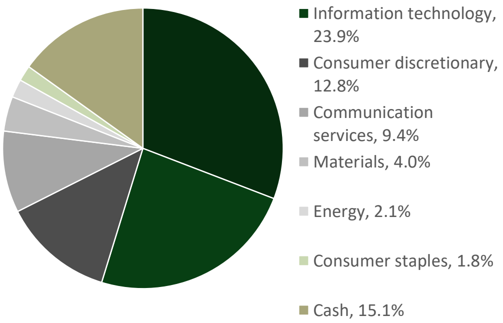
Performance	1 Month	3 Months	6 Months	1 Year	3 Year (p.a.)	Since Inception (p.a.)
Net^	-0.34%	6.08%	14.34%	15.04%	8.11%	11.94%
Benchmark*	0.31%	6.80%	16.95%	15.74%	7.02%	11.93%
Alpha	-0.66%	-0.72%	-2.61%	-0.70%	1.08%	0.00%

^ The net return figure is calculated after fees & expenses. Past performance is not a reliable indication of future performance
* MSCI Asia ex Japan (non-accumulation) (AUD)

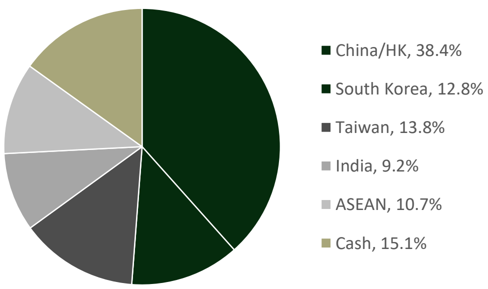
Portfolio Characteristics
Top 10 Holdings

TSMC	Information Technology	9.9%
Tencent Holdings Ltd	Communication Services	7.6%
Samsung Electronics	Information Technology	7.1%
Alibaba Group Holding Ltd	Consumer Discretionary	7.0%
Ping An Insurance	Financials	4.2%
United Overseas Bank	Financials	3.2%
DBS Group Holdings Ltd	Financials	3.2%
OCBC Ltd	Financials	3.2%
Hong Kong Exchanges & Clearing Ltd	Financials	3.1%
China Construction Bank Corp	Financials	2.6%

SECTOR ALLOCATION



GEOGRAPHIC LOCATION



Source: Ellerston Capital

Commentary

The Ellerston Asia Growth Fund was down -0.34% (net) during February versus the benchmark which was up 0.31%. Financial year to date in 2021, the Ellerston Asia Growth Fund is up 20.20%.

Market Outlook

The main driver of global markets in February was the spike in US bond yields and the implications for factor, country and sector allocation. In Asia, China's "two sessions" shed some light on how the leadership is looking at growth going forward. Commodity prices and the global chip shortage are also important to note. These issues are discussed in detail below

TAPER TANTRUM 2.0

In May of 2013, then Fed Chairman Ben Bernanke announced that the Fed would, by the end of the year, reduce the volume of its bond purchases. The market reactions across equities, bonds and FX was violent. Bond yields spiked immediately with the US 10 year rising from less than 2% in mid-May to 2.75% by the end of June and 3% by the end of CY13.

Equities slumped across the world with some notable divergences: the US outperformed almost all other markets, DM outperformed EM (except Japan which was down 20% in less than a month), Asia outperformed EM as a whole, and large caps outperformed small caps in most markets. The sell-off was short lived (~ 1 month) and the rebound was sharp but not uniform across markets. By the end of 2013, US markets were back up well above their pre-Taper Tantrum highs while MSCI World was almost 7% higher. Asia and Emerging Markets were mixed with high current account deficit countries generally under-performing on both the sell off and the rebound.

Late February and early March 2021 have witnessed a minor tantrum but without the Fed saying anything about tapering. Obviously Fed language could change if inflation expectations continue to creep up or if inflation itself becomes an issue. The following factors could combine to generate inflation in the short term:

- Base effects for CPI which kick in at the end of 1Q21 and beginning of 2Q21;
- Vaccine roll out and return to normal business activity, particularly in the services sector;
- Impact of simultaneous fiscal and monetary stimulus in the US;
- Supply chain disruptions and the impact on prices of semiconductors, wood products, pharma products, oil, etc.

Apart from base effects, much of the Fed commentary is around whether the return of inflation is structural or cyclical. Dallas Fed Chairman Kaplan has said he expects the "cyclical elements of inflation to build" in early 2021 but that the drivers of this inflation may not be "persistent". Over the medium term, the structural forces technological disruption combined with demographics may outweigh the upward price pressure caused by cyclical factors.

Our view is that the Fed would be reluctant to taper on base effects alone but would need to see evidence of a recovering labour market to taper. To actually raise rates they would have to see some of "persistent" elements return to CPI. However, the late February mini-tantrum has shown that the market may move ahead of the Fed. Our very high overweight in financials (~11% overweight versus the benchmark) is in place to protect returns in the event of another taper tantrum and a spike in bond yields. Our country allocation, namely zero or underweight current account deficit countries with volatile currencies, is also in preparation for a potential taper.

TWO SESSIONS IN CHINA

In early March, over 5000 members of China political elite met in Beijing for the annual gatherings of the Chinese People's Political Consultative Conference (CPPCC) and the National People's Congress (NPC), also known as the Two Sessions. The main headline to come out of the two sessions thus far is that China has revised its GDP growth target to "above 6%" for 2021. This is lower than consensus which had China growing at over 8%. Chinese leadership emphasized quality growth which focuses on employment and carbon neutrality. Specifically, the government is targeting a 13.5% reduction in energy consumption per unit of GDP and an 18% reduction in CO_2 emissions during the 14th FYP. We continue to research ways to best reflect the China Net Zero theme in the portfolio.

CHIP SHORTAGE

For the past 3-4 months the semiconductor industry has been facing severe supply constraints across a number of different applications, most notably automotive chips. This chip shortage situation has been caused by three main factors: (1) US sanctions against Chinese companies such as Huawei and SMIC; (2) The resilience of consumer tech throughout the COVID pandemic; and (3) The recovery in auto related demand. Overall this is a positive for some of our technology positions, namely TSMC and UMC.

OIL PRICE

The oil price rose approximately 10% in the last month. EAI currently has no direct exposure to the energy sector other than via conglomerate Reliance Industries. However, we still watch the oil price closely as it has implications for country weightings given some countries in Asia are significant oil importers (India) and some are major oil exporters (Malaysia).

The key events impacting the oil price last month were: the Saudi military intercepting drones and missiles launched from neighbouring Yemen that were targeting key Aramco facilities; US Crude production saw its biggest ever decline of about 1mbpd; and the Texas freeze event which shut down 18 US oil refineries. Finally, OPEC+ surprised the markets by choosing not to increase their production output as the market was expecting and instead announced an increase of about 1mbpd of production.

In terms of country impact, India's oil import bill could be US$22b higher than budget estimates if crude continues to remain at current levels. This is a potential negative for the Indian currency and it could prompt the RBI to intervene in the forex markets and could add pressure to India's double deficit problem (current account and fiscal).

PERFORMANCE

In February, India and Singapore were the largest country contributors to alpha while Hong Kong was the largest detractor. Communication Services and Financials were the largest sector contributors to alpha while Materials was the largest detractor. Kuaishou Technology and SK Hynix were the largest single stock contributors to alpha, while our position in LG Chem was the largest detractor.

As always, if you have any questions regarding any aspect of the portfolio, please feel free to contact us at info@ellerstoncapital.com.

Kind regards,
Mary Manning

Contact Us

Sydney

Level 11, 179 Elizabeth Street,
Sydney, NSW 2000
+612 9021 7701
info@ellerstoncapital.com

Melbourne

Level 4, 75-77 Flinders Lane,
Melbourne, VIC 3000
+612 9021 7701
info@ellerstoncapital.com

Find out more

All holding enquiries should be directed to our register, 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** or visit us at **ellerstoncapital.com**

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