ELLERSTON CAPITAL

Ellerston Australian Share Fund (ASF)

Performance Report | December 2020

PERFORMANCE SUMMARY

Net %	1 Month	3 Months	FYTD	Rolling 12 Months	5 Yr p.a.	Strategy Since Inception p.a.
ASF	-1.46	12.88	14.34	-5.66	5.84	7.84
Benchmark	1.21	13.70	13.20	1.40	8.73	9.72

Past performance is not a reliable indicator of future performance.

MARKET COMMENTARY

Market Overview

Investors ended a wild year by piling into everything from bitcoin to emerging markets, with expectations that a material economic recovery, fuelled by massive government and central bank stimulus and the rollout of the vaccine, will push prices even higher. The performance of global equity markets were mixed, but the Eurozone was the clear laggard.

US government bond yields remain near all-time lows, but squeezed higher towards year end. Crude oil prices were back over US$50 a barrel after briefly dropping to minus US$37.00/bbl for the first time ever in April.

The year ended with investors evaluating the likelihood of further fiscal support from Washington and continuing to buy risk assets, with momentum still the powerful force driving equity prices.

USA

US stocks ended their record-setting run, capping a banner year for everything from gold to bitcoin. After plunging into steep bear market territory as worries about the rapidly spreading coronavirus virtually shut down the globe and smashed investor sentiment, stocks soared in 2020, an unthinkable outcome when markets gapped down in February and March.

The Federal Reserve's massive stimulus, central bank action of a magnitude never seen before and subsequently, news of a vaccine, stoked a powerful rally in markets. The S&P 500 climbed 18.4% for the calendar year to 3,756.1, ending the year at a record level, while the tech-heavy Nasdaq Composite gained 44.9% to 12,888.3, its best year since 2009.

The Dow Jones finished up 9.7% in 2020 to 30,606.5, a far cry from its 23rd of March low of 18,213 points. In the month of December, the S&P 500, Nasdaq Composite and Dow Jones were up 3.8%, 5.7% and 3.4% respectively, fuelled by the distribution of the first COVID-19 vaccines across the country and Congress passing President Trump's signed US$900 billion stimulus deal four days before the end of the year.

Investment Objective

The Investment objective for the Ellerston Australian Share Fund is to outperform the S&P/ASX 200 Accumulation Index (Benchmark).

Investment Strategy

The Fund uses a benchmark-independent, high conviction approach that looks beyond investing in the Top 20 stocks in order to capture the neglected opportunities created by under-researched stocks in the broader Australian market.

Key Information

Strategy Inception Date	1 April 2009
Fund Net Asset Value	$0.9392
Liquidity	Daily
Application Price	$0.9415
Redemption Price	$0.9369
No Stocks	22
Management Fee	0.90%
Buy/Sell Spread	0.25%
Performance Fee	15%

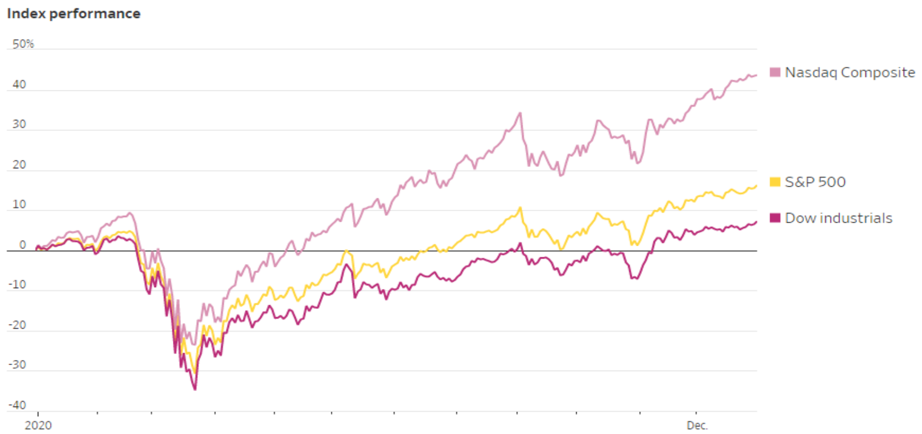
Ellerston Capital Limited
ABN 34 110 397 674
AFSL 283 000

Level 11
179 Elizabeth Street
Sydney NSW 2000

Ph: +61 2 9021 7701
Fax: +61 2 9261 0528

info@ellerstoncapital.com
www.ellerstoncapital.com

APIR Code: ECL0005AU



Source: Factset

Under the surface, many individual securities logged even more astonishing returns. More stocks gained at least 400% at their yearly peaks in 2020 than in any year since 2002. Among the names were Tesla (up almost 700%), Peloton Interactive and several biotechnology firms.

Europe

European markets were the worst performers in 2020. The pandemic didn't seem to be under control for any extended period and economies in Europe were severely impacted, as countries went in and out of lockdown. News of the vaccine brought some temporary relief towards the end of the year.

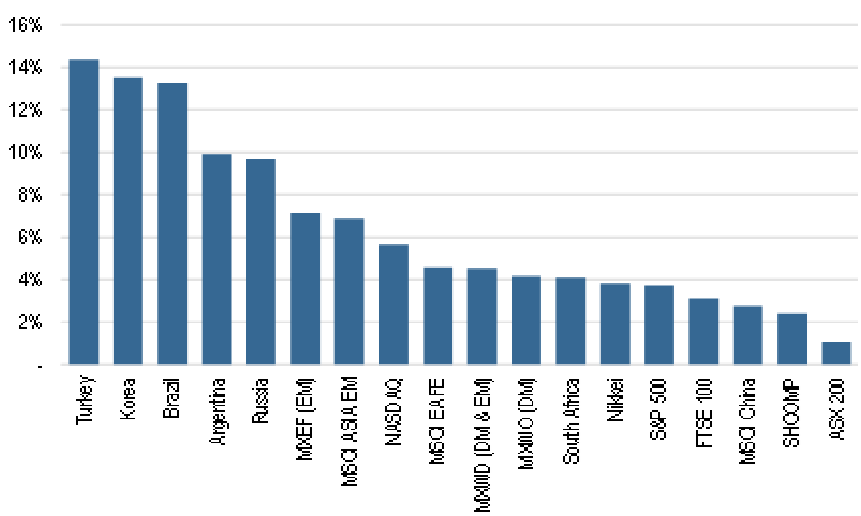
The Euro STOXX 50 Index ended the calendar year down 3.2% (December: +1.8%). Among the major exchanges, the UK's FTSE 100 fared relatively badly, down 11.6% (December: +3.3%), France's CAC 40 returned -5.0% (December: +0.8%) and Germany's DAX's was the only key market which bucked the trend to finish in positive territory for the calendar year with a return of +3.6% (December: +3.2%). Britain became the first Western country to approve the Pfizer vaccine and start mass-vaccinations. At the same time, the European Central Bank boosted its emergency program by 500 billion euros and essentially locked in low interest rates until the pandemic is over. The STOXX50 enjoyed a relief rally in December after the European Union and UK finally reached an agreement on Brexit terms, reaching its highest level since April 2019.

Asia

Despite the economic and humanitarian damage from COVID-19 in 2020, Asian ex-Japan equities ended the year with a gain of 22.5%. The 68% rally from the 23 March bottom (5% gains from this point would match the 2016-18 trough-to-peak rally) which was initially met with extreme scepticism, has increasingly been embraced by investors, especially after the US elections and vaccine progress in November. Unsurprisingly, the strongest performance for the year came from the Healthcare sector (especially in Malaysia and Korea) and other COVID-19 beneficiaries. Strong gains were also seen in the Tech hardware space (5G, laptops and, recently, memory optimism) and the renewables/EV complex (especially after China's carbon neutrality pledge). On the other hand, Property, Energy and Utilities ended the year down. The year also saw record capital raisings and turnover (especially from retail investors) in the region.

The Hang Seng Index was the exception to its major Asian market peers. For the calendar year, it returned a disappointing -0.5% (December: +3.4%), India's BSE SENSEX was up 17.2% (December: +8.2%), Korea's KOPSI rallied 30.8% (December: +10.9%), Japan's Nikkei 225 Index was up 17.8% (December: +3.9%) and the Chinese SSE Composite Index delivered a return of 13.9% (December: +2.4%).

Global equity market performance in December 2020

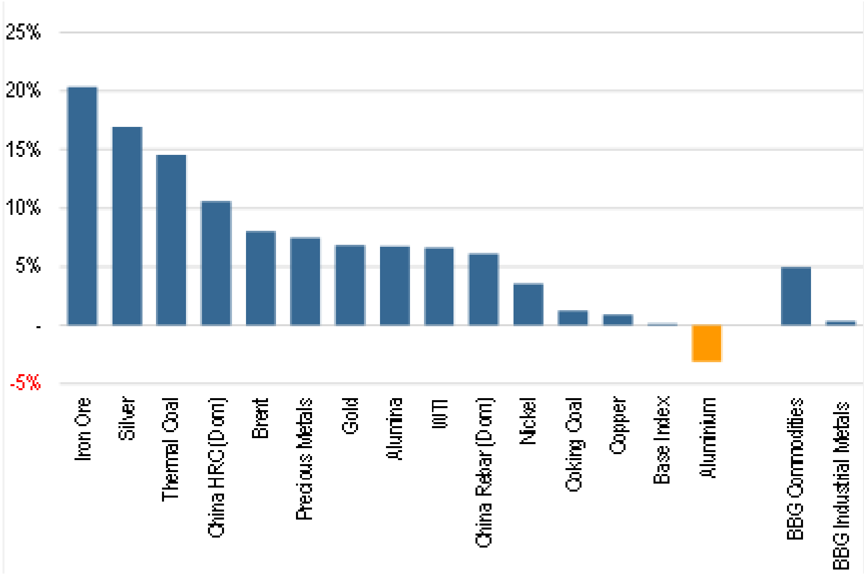


Source: JP Morgan, Bloomberg

Commodities

The CRB commodities index continued its recent strength (up 5% in December). The standout was the 20% rise in the iron ore price, setting all-time highs in Australian dollar terms at over A$200 per tonne following Vale, Brazil's major iron ore producer, again downgrading its production guidance for CY21. Brent oil rose 8% to US$51.72/bbl, driven by the OPEC+ decision to limit their previously announced January 2021 supply increase of 2m bpd to a maximum 0.5m bpd and review further increases on a monthly basis. This was premised on the group's concerns over the prospect of reduced demand from new COVID-19 lockdowns. Gold was 7% higher to US$1898/oz as bond yields rose and the US dollar weakened.

Global commodity performance in December 2020



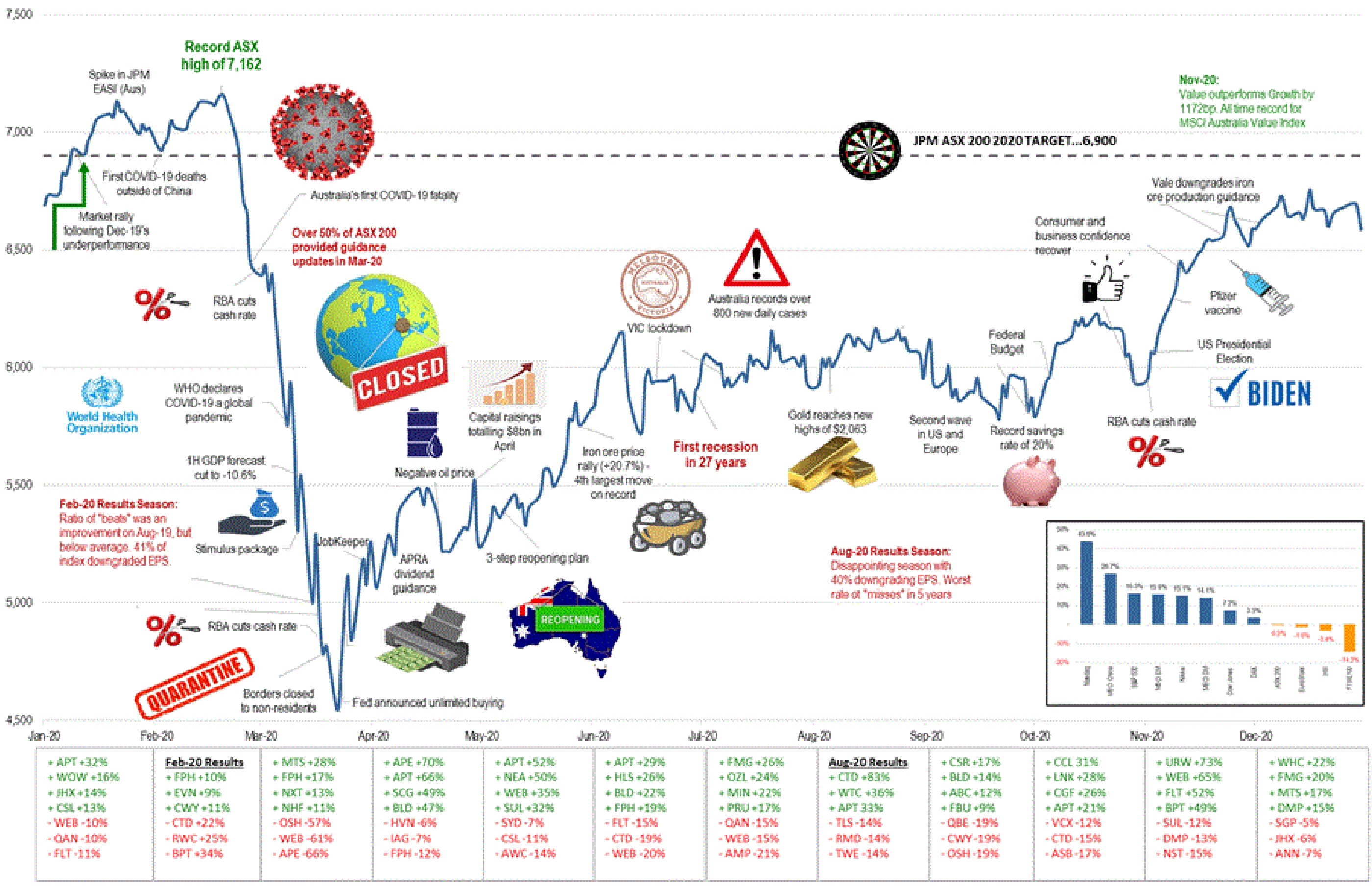
Source: JP Morgan, Bloomberg

Bonds

US 10-year bond yields rose again in December and ended the year at 0.91%, while the Australian 10-year bond yields closed just shy of 1.0%, rising almost 9 basis points. The spread between the US and Australian 10-year has narrowed and expectations of stronger economic growth in the US is likely to push bond yields higher in the US. While official interest rates seemed anchored at historically low levels, it will be interesting to observe just how bond yields fare if the robust forecast global economic recovery eventuates.

Australia

2020 Pictorial Review



Source: JP Morgan

The S&P/ASX 200 Accumulation Index ended the month of December with a return of +1.2% and for the calendar year, up a rather subdued +1.4% to 6,587 points. This is despite key data showing that the economy grew by 3.3% in the September quarter and that it had officially emerged from the recession. The ASX 200 fell 36% peak to trough (and bounced ~50%) as containment measures and social distancing effectively stalled activity. Victoria's second-wave virus experience, marked the inflection of Australia's cycle response and recovery path.

Australia underperformed most global peers in 2020. InfoTech was the clear winner across all major markets.

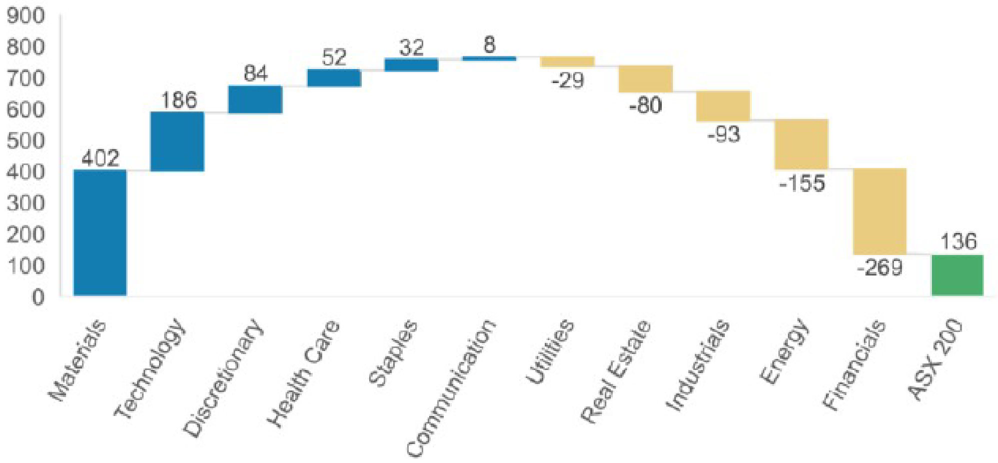
	AUS	ACWI	EM	US	Europe
Index	8.9%	16.8%	18.7%	21.4%	5.9%
Info Tech	67.3%	46.1%	60.9%	46.2%	25.0%
Comms	26.9%	24.1%	27.7%	26.6%	-5.2%
Materials	25.2%	21.5%	25.3%	20.7%	19.9%
Discretionary	19.9%	37.0%	36.8%	50.3%	16.4%
Staples	18.2%	8.8%	11.0%	10.7%	5.7%
Health Care	11.9%	15.4%	52.9%	15.2%	7.6%
Financials	2.8%	-3.2%	-7.8%	-2.0%	-7.5%
Real Estate	2.5%	-5.7%	-16.7%	-2.8%	-3.0%
Industrials	-4.2%	11.8%	5.3%	12.4%	13.5%
Utilities	-12.0%	4.6%	-4.8%	0.2%	22.5%
Energy	-22.7%	-27.7%	-15.0%	-34.0%	-27.4%

Source: MSCI, RIMES, Morgan Stanley Research. Returns showed in US$ terms

ASX 200 CY2020 Performance Attribution

Fortescue, Afterpay and BHP were the largest contributors to the index return for Calendar 2020

Sector Contribution to Performance (TR)



Source: Bloomberg, Morgan Stanley Research. Performance as at 31/12/2020

The S&P/ASX 200 advanced in December, closing at its highest level since February on December 17th at 6756.7. For the month, the Materials sector was the most significant contributor to the index's performance, adding 1.6%, followed by Information Technology, contributing +0.4% and the Consumer Staples sector contributing +0.1%. Health Care was the worst performer, with a total return of -4.9%, detracting -0.5% from the index's performance.

The best performing sub-index was the ASX 200 Resources Accumulation Index, surging 8.5%, followed by the Small Ordinaries Accumulation Index, +2.8% and the ASX 200 Industrial Accumulation Index, -0.6%.

The top five stocks that detracted from the performance of the S&P/ASX 200 Accumulation Index were: CSL (-35 points), Westpac Banking Corporation (-15 points), QBE Insurance Group (-11 points), Cochlear (-11 points) and a2 Milk Company (-9 points).

The top five stocks that made a positive contribution to the index's return were: BHP Group (+69 points), Fortescue Metals Group (+46 points), Commonwealth Bank of Australia (+29 points), Afterpay (+29 points) and Rio Tinto (+25 points).

The AUD was a strong performer in December, rising almost 5% against the USD, and ended the year at 0.77 US cents, helped by the surge in iron ore prices and weakness in the greenback. The AUD, up circa 10% in 2020, recorded its best year in a decade.

Not surprisingly, the RBA left the official cash rate at its historical low level of 0.1% following its meeting in early December.

COMPANY SPECIFIC NEWS

The Market Misses

Mesoblast (MSB -45.9%)

Investors blasted biopharmaceutical company MSB's stock price after reporting that the data from the Phase 3 heart failure trial of its Revascor mesenchymal precursor cells, used to treat chronic heart failure, had not met its primary endpoint or the majority of its secondary endpoints. This raised concerns for investors over the future of MSB's stem cell therapy in inflammatory disease.

Appen (APX -21.7%)

Appen provided a trading update in December, downgrading their underlying FY20 EBITDA expectations from $125m - $130m previously, to $106m - $109m. APX suggested various COVID-19 related disruptions were to blame, with work volumes from their concentrated customer base slower to recover due to reshaped customer priorities and rolling Californian lockdowns.

Service Stream (SSM -20.1%)

SSM was impacted in December by an updating of the company's contract with NBN. The updated Unify Service awards from NBN, which will take effect from March 2021, has effectively reduced SSM's wallet share of NBN related deployment work from ~50% to ~25%. Under the prior contract, SSM earned revenue of $330m in FY20 from NBN and now expect to deliver only around $70m in the first year under the new contract.

IDP Education (IEL -18.9%)

IDP Education underperformed the market in December on no company specific news.

A2 Milk (A2M -17.1%)

A2 Milk delivered a second material downgrade to FY21 expectations, attributing it to a slower than anticipated recovery in their important Diagou distribution channel. A2M downgraded their guidance for first half FY21 revenue to NZ$670m (prior guidance: NZ$725-$775m) and NZ$1.40bn-$1.55bn (prior guidance: NZ$1.8bn-$1.9bn) for FY21 revenue. Full year FY21 EBITDA margin guidance was also downgraded to 26%-29% versus prior guidance of 31%, leaving investors unimpressed.

QBE Insurance (QBE -14.7%)

QBE's share price was hit following a surprise update from the company that downgraded FY20 earnings. Reserve top-ups for prior years and higher catastrophe and crop claims were blamed. While partly one-off in nature, higher claims inflation trends in the US and lower bond yields are likely to persist in the medium-term. The stock offers compelling leverage to firming premium rates (the best in 20 years) and rising bond yields (eventually) and trades at a material discount to valuation. But investor confidence, painstakingly restored these past few years, has once again been damaged.

Cochlear (COH -14.7%)

No particular news caused the fall in the hearing implant maker's share price. COH lost its final chance to appeal the $US268 million of damages it had been ordered to pay two US research institutions due to patent infringement violations, but COH had already previously paid the damages and the patents in question have expired so little impact. Its poor performance in the month is likely to do with the PE premium for COH's defensive quality unwinding and a stronger AUD, along with other similar stocks over the previous two months.

ZIP (Z1P -12.7%)

Having rallied very strongly from the lows in March, the stock hit a high point in August, riding the buy-now-pay-later wave. It has since issued equity to fund an acquisitive growth strategy. In December, the company announced a $120m fully underwritten placement to be used across the US, UK and ANZ. The issue was dilutive and concerns around execution risks and margin pressure saw the shares sell off.

Corporate Travel / Webjet (CTD -12.5%/ WEB -12.1%)

COVID-19 reared again, particularly across international markets during December, impacting sentiment towards all the travel names. Both WEB and CTD, with significant operations in Europe and the US, were sold off on the back of further delays to cross border travel.

The Market Hits

Independence Group (IGO +37.4%)

IGO entered into a binding US$1.4bn agreement with China's Tianqi Lithium Corporation to acquire a 24.99% indirect interest in the Greenbushes spodumene mine and a 49% indirect interest in the Kwinana lithium hydroxide plant (under construction) in Western Australia, which included an equity raising of up to $766m. Investors reacted positively to the strategic purchase which, despite the acquisition price being fair at best, was consistent with IGO's strategy to increase its exposure to clean energy metals through long-life, high quality assets (which Greenbushes ore reserves and low cost position achieves).

Fortescue Metals Group (FMG +28.5%)

FMG benefitted from the 20% increase in iron ore prices which set all-time highs in Australian dollars of over A$200 per tonne. This followed Vale, Brazil's largest iron ore producer, would miss its production targets for CY21 based on COVID-19 constraints to its workforce and other safety issues. The now lower than expected supply further extends the current tight market conditions caused by surprisingly strong Chinese steel mill demand.

Credit Corp (CCP +24.9%)

The company entered into an agreement to acquire Collection House's asset base and arrangement book. The acquisition is expected to be highly value-accretive and lead to broad based earnings upgrades. The company also confirmed that it has been deploying the capital raised at the height of the coronavirus-induced crisis in May, effectively and has a vastly improved its liquidity position.

Afterpay (APT +24.2%)

APT continued its phenomenal share price run post March 2020, up a further 24% in December. APT benefitted in December from a strong trading update and RBA Governor Lowe suggesting the benefits of the broader buy-now-pay-later space outweigh the costs at this point, reducing any near term risk around surcharging regulatory changes. APT was also added to the ASX20 in the month.

Whitehaven Coal (WHC +24.2%)

WHC rallied on the back of 15% higher global thermal coal prices for the month due to a combination of a cold winter, improved manufacturing activity and restricted supply (China's official coal ban mid-way through December actually drove the spot market higher).

Sandfire Resources (SFR +22.1%)

The company approved the development of its US$259m T3 Motheo copper-silver project in Botswana, with a forecast mine life of 12.5 years and first production expected in CY23. The approval provided investors with more confidence in providing a bridge in copper production post the decline of SFR's high grade Degrussa copper mine in Western Australia, albeit at half its production rate.

Iluka Resources (ILU +21.5%)

Expectation of improved global housing related construction activity for ILU's major products, zircon (major market is ceramic tiles which use the product as an opacifier) and rutile (contains titanium dioxide used for the production of paint pigments), pushed the stock price higher, as did the company's removal from the S&P/ASX 100 index which made it a material component of the benchmark for small cap investors.

GWA Group (GWA +21.2%)

Residential and commercial building fixtures and fittings company, GWA was up on no specific company news, but the strong rebound in consumer confidence (Westpac-Melbourne institute of Consumer Sentiment hit a 10 year high in December) lifted a number of companies in the discretionary spending sectors.

PolyNovo (PNV +20.9%)

Biotech company, PNV continued its stellar run after updating the market with further details of its IDE pivotal trial. This aimed to compare the safety and effectiveness of its NovoSorb BTM (BTM) to standard of care (SOC) in patients with severe full thickness burn injuries, with the primary endpoint being the comparative percentage wound closure in the BTM and SOC. The trial is expected to provide strong clinical evidence to support what many surgeons are already seeing with Novo BTM.

Nanosonics (NAN +20.6%)

Medical devices company, NAN continued its upward trajectory after its previous month's trading updates and broker upgrades.

FUND PERFORMANCE

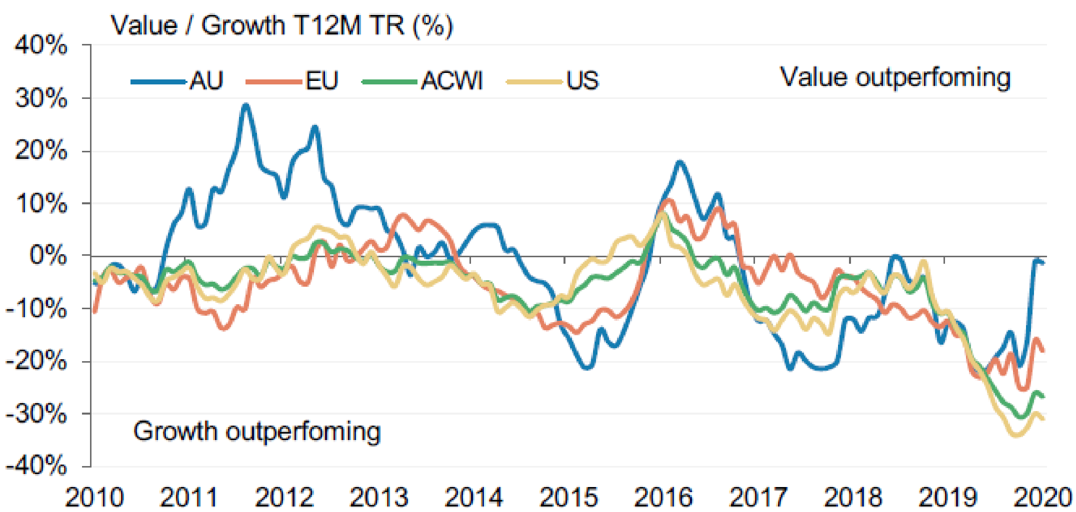
Following an exceptionally strong month in November, the Fund gave back some of the gains and posted a return of -1.36%, underperforming the benchmark return of 1.21%.

This brings the return for the FYTD to 14.98%, outperforming the benchmark of 13.20%. In terms of the outlook for 2021, we remain cautiously optimistic, as Central Bank monetary policy should be supportive, further fiscal stimulus is likely to be rolled out, and earnings will re-bound sharply off a low COVID-19 impacted FY20 base.

RETURNS[1] (%)	GROSS	BENCHMARK*	EXCESS	NET
1 MONTH	-1.36	1.21	-2.57	-1.46
3 MONTH	13.20	13.70	-0.50	12.88
FYTD	14.98	13.20	1.78	14.34
ROLLING 12 MONTHS	-4.64	1.40	-6.04	-5.66
5 YEARS (P.A.)	6.97	8.73	-1.76	5.84
SINCE INCEPTION (P.A.)	9.01	9.72	-0.72	7.84

Past performance is not a reliable indicator of future performance.

Despite a strong value rotation in recent months, Growth still outperformed Value in 2020 for the fourth year in a row.

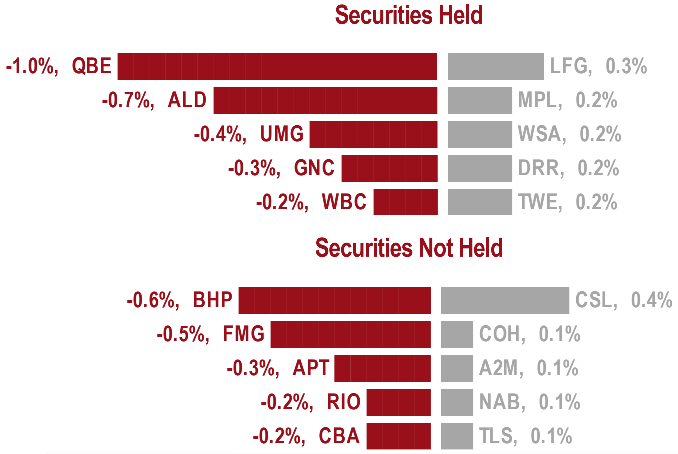


Source: RIMES, MSCI, Morgan Stanley Research

[1] The return figures are calculated using the redemption price for Class A Units and on the basis that distributions are reinvested. The Gross and Excess return figures are before fees and expenses whereas the Net Return figures are net of fees and expenses for the Class A Units. Returns of the Fund may include audited and un-audited results. Past performance is not a reliable indicator of future performance.

* The benchmark was changed from the S&P/ASX 200 Accumulation Ex REITS Index to the S&P/ASX 200 Accumulation Index on 1 July 2012.

Month of December Attribution



Source: Ellerston Capital.

The main positive contributors to this month's performance were overweight positions in: Liberty Financial (LFG +29.9%), Medibank Private (MPL + 5.6%), Western Areas (WSA +16.9%), Deterra Royalties (DRR +4.3%) and Treasury Wine Estates (TWE +9.4%).

Zero weight positions that also helped included CSL (CSL -4.8%), Cochlear (COH -14.3%), A2 Milk (A2M -17.1%), National Australia Bank (NAB -1.3%) and Telstra (TLS -2.9%).

The main detractors to performance for the month which more than compensated for the above were overweight holdings in: QBE Insurance (QBE -14.7%), Ampol (ALD -7.3%), United Malt Group (UMG -6.4%), Graincorp (GNC -4.1%) and Westpac Banking (WBC -3.8%).

Not holding larger cap shares that outperformed the broader market and constrained returns included: BHP (BHP +11.5%), Fortescue Metals Group (FMG +28.5%), Afterpay (APT +24.2%), Rio Tinto (RIO 12.3%) and Commonwealth Bank of Australia (CBA +3.8%)

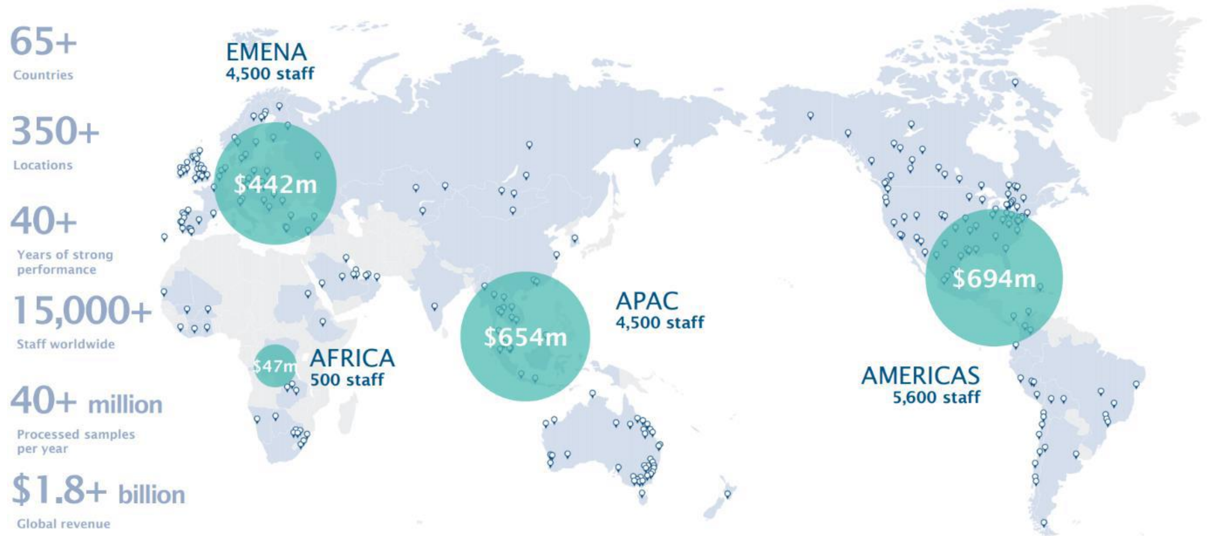
FUND ACTIVITY

Fund activity was rather subdued in the month of December. Of note, we exited residual holdings in Ramsay Health Care and Flight Centre and took profits in Deterra Royalties and NextDC following rallies. We also strengthened the position in gold producer Northern Star Resources. One new stock was added to the portfolio, ALS Limited (see commentary below).

NEW STOCKS ADDED	STOCKS EXITED
• ALS Limited	• Ramsay Health Care
	• Flight Centre
INCREASED	**DECREASED**
• Northern Star Resources	• Deterra Royalties
• Tabcorp	• NextDC

ALS

ALS is a global Testing, Inspection and Certification (TIC) Company with a focus on Life Sciences and Commodities sample testing. The Life Sciences segment generates 50% of group earnings and comprises the testing of samples in the environmental (~70%), food (~15%) and pharmaceutical (~15%) end markets. These three markets are growing around 1.5 to 2 times GDP, driven by an outsourcing trend where increasing TIC complexity and regulatory requirements are shifting more sample volumes to specialist third-party providers in each of these three end markets.



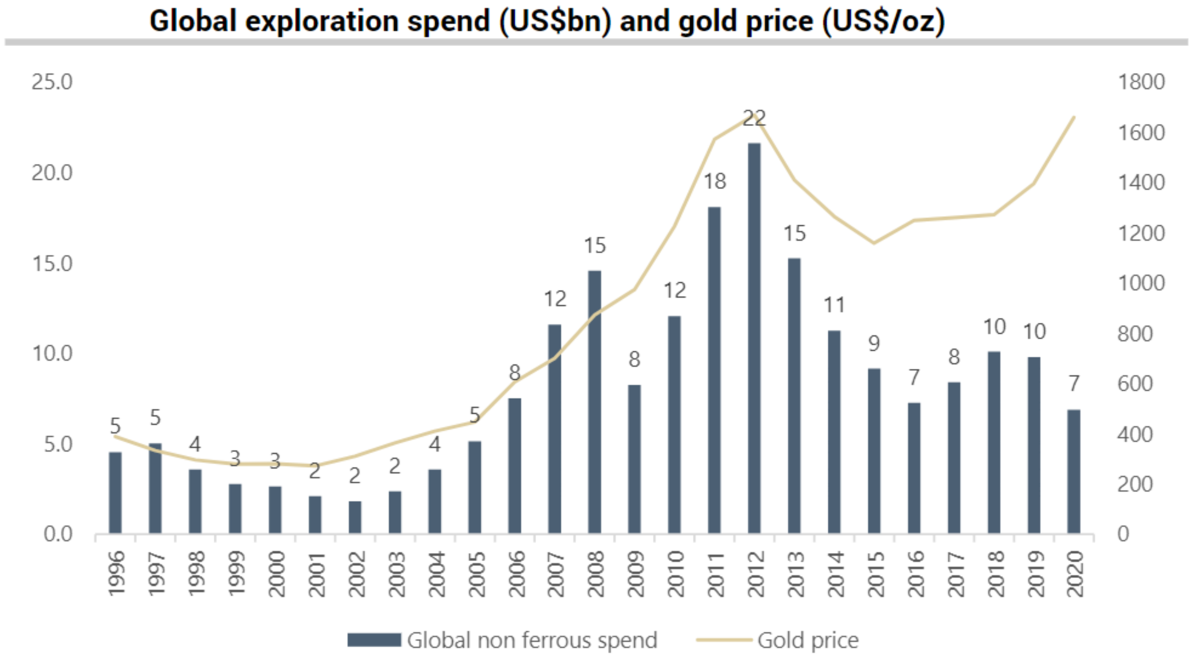
Source: ALS

Whilst Life Sciences TIC is an attractive business, we believe the real gem within the overall group is the Geochemistry business, responsible for ~80% of the earnings of ALS's Commodities segment. ALS's Geochemistry business has a dominant ~50% share of the global commodity testing market. Despite being an inherently cyclical business, given the end markets, ALS has built a highly strategic 'hub and spoke' business model which allows it to earn impressive returns on capital, both throughout and at each point in the cycle.

The nature of geochemistry testing is that samples (drill cores) do not degrade (structurally different to the life sciences business). This characteristic is the core reason why ALS's 'hub and spoke' business model is so powerful. ALS runs a global model centred around 5 key 'hub' locations. These hub locations are strategically positioned to optimise through-put. The spokes then act as small labs, which can quickly be flexed up and down depending on volumes. This provides the ability for the overall business to manage margins. ALS was able to move quickly at the beginning of the pandemic to pre-emptively make significant cost reductions, implicitly flexing the spokes down. The inherent operating leverage is immense in cyclical upswings which we believe is being under-appreciated by equity investors.

Half of the Geochemistry commodity samples are linked to gold, with a further 22% linked to copper. A sustainable move higher in the gold price should result in an increase in gold mining activity due to increased profitability. A lead indicator of such activity, particularly in the junior space, is typically gold miners' equity raisings, which leads to greater exploration activity and in turn, leads to an increase in core sampling volumes. Analysis of the past 12 years operating history and accounts, and mapping this to historical global exploration spend, confirms this relationship and provides a framework for assessing the earnings potential of the Geochemistry business going forward. If anything, ALS has actually improved their market share and industry position in recent years, as some larger competitors have exited the industry to remove cyclicality from their businesses.

Consensus EBIT estimates for the Commodities segment are $181m in FY22 and $189m in FY23. We estimate this is consistent with a US$11-US$12bn annual exploration spend. **We believe the risk to the exploration spend is firmly skewed to the upside and estimate that for every additional US$1bn of exploration spend, this leads to $25m-$30m of incremental EBIT to ALS.**



Source: Jefferies

Evidence from the most recent half yearly result and underlying sample volume trajectory, as well as the capital raising activity we've seen from junior miners in Canada and Australia in recent months, has given us further confidence in and reinforced our investment thesis. We would expect pending upgrades to consensus earnings estimates for FY21/FY22/FY23, and believe the investment in ALS represents a favourable risk/reward payoff at current prices.

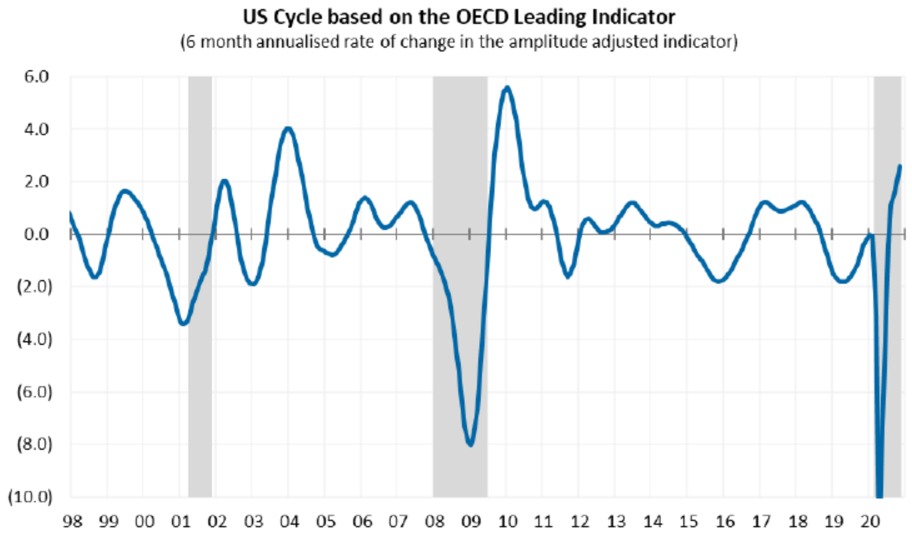
FUND STRATEGY AND OUTLOOK

We remain cautiously optimistic looking out into 2021, as Central Bank monetary policy should be accommodative, further fiscal stimulus is likely to be deployed and earnings will re-bound sharply off a low COVID-19 impacted FY20 base.

As long as the efficacies of the vaccines work as Big Pharma claim, we are rather excited about the pending reflation trade in 2021. We expect economic momentum to pick up strongly into 2021, after the RBA's $100bn QE program kicks in and we cycle through the first COVID-19 domestic shutdowns.

After flipping at least one Senate seat, the results of the Georgia Senate runoff election are now showing the real prospect of a mini blue wave that has the Democrats winning the House, Senate, and White House. A Democratic sweep would no doubt lead to more fiscal stimulus, higher corporate taxes (a hike to 28% down the track), but at the same time a likely attempt to roll back on the Trump Tax cuts. Market reaction reflecting this view has initially been positive, with small caps (Russell 2000), energy, financials and basic materials rallying hard on the back of the rotation back into the synchronized global economic recovery theme. The results of the Georgia Senate runoff election and a barrage of key US economic data later this month should drive elevated volatility in the short term.

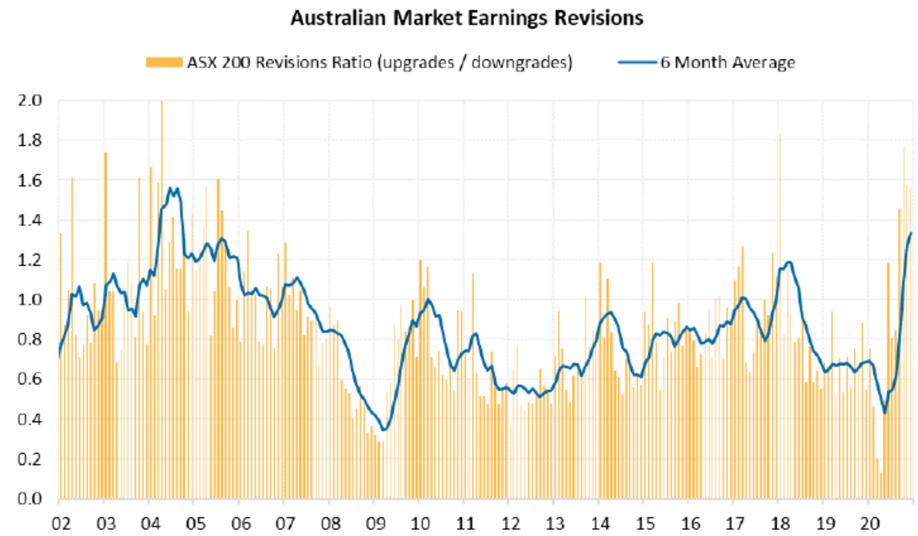
The US expansion continues to accelerate and is still less than half the initial rebound seen after the GFC



Source: FactSet, Macquarie Research, December 2020

The recent AGM season in Australia was cautiously upbeat (3:1 ratio of upgrades to downgrades) and earnings revisions in the past 4 months proved to be the strongest since 2002, heralding the commencement of the earnings upgrade cycle.

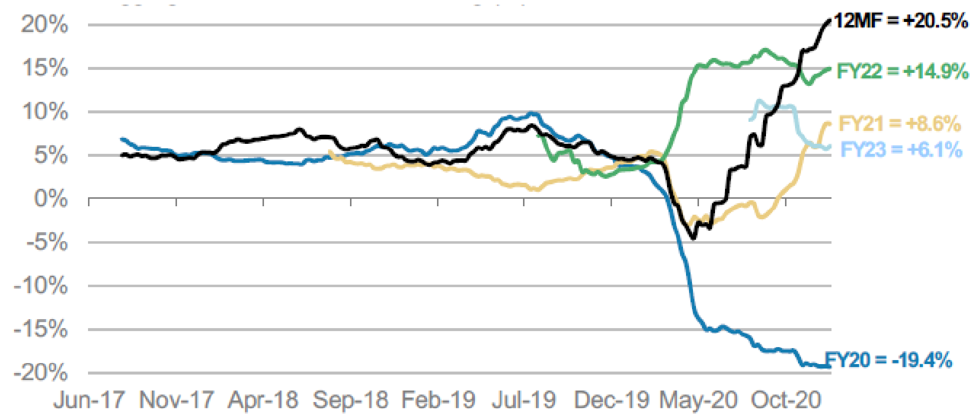
Over the last four months we have seen the strongest consecutive net EPS upgrades in over two decades



Source: FactSet, Macquarie Research, December 2020

Consensus implies forward EPS rises of ~10% in CY21. This appears very achievable and conservative, given the stimulus and pickup in activity expected following the vaccine roll out. Also, by way of reference, looking back in history when the cycle was at a similar point after the GFC, a 20% earnings recovery ensued a year later (which was not expected).

Aggregate Annual Consensus EPSg (%) Trends FY20-23

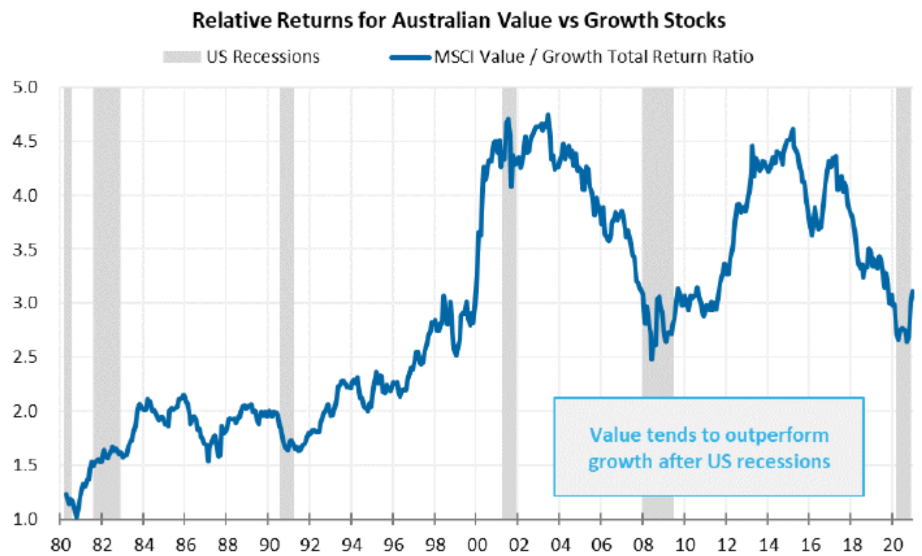


Source: RIMES, IBES, Morgan Stanley Research.

Coming off a low base, re-enforced by massive fiscal and monetary stimulus, vaccinations should lift confidence and as a result, we would expect a significant pickup in consumer spending as savings are drawn down. When coupled with strong commodity prices, it would not be unreasonable for earnings to lift ~20% again in CY21.

The so-called 'COVID-19 losers', particularly those exposed to entertainment, travel and leisure services should potentially see some of the largest upgrades. **Whilst it's been a bumpy ride, we would envisage the recent Value rotation to continue as bond yields edge higher**.

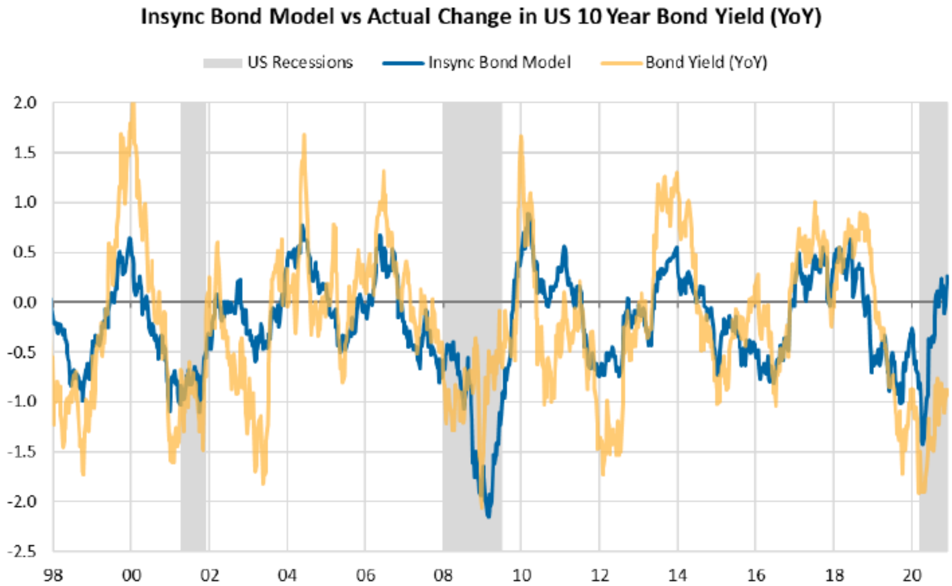
As expected, Value has started to outperform growth and we expect this trend to continue in 2021



Source: FactSet, Macquarie Research, December 2020

At the same time**, PE dispersion remains at record high levels**. We expect long bond yields to continue to nudge higher next year based on massive fiscal stimulus kicking in, which favours shorter duration cash flows, while also supporting the Financials sector where we have moved from a massive underweight position 6 months ago, to a more neutral stance (financials being a key value sector which has the potential to rally hard).

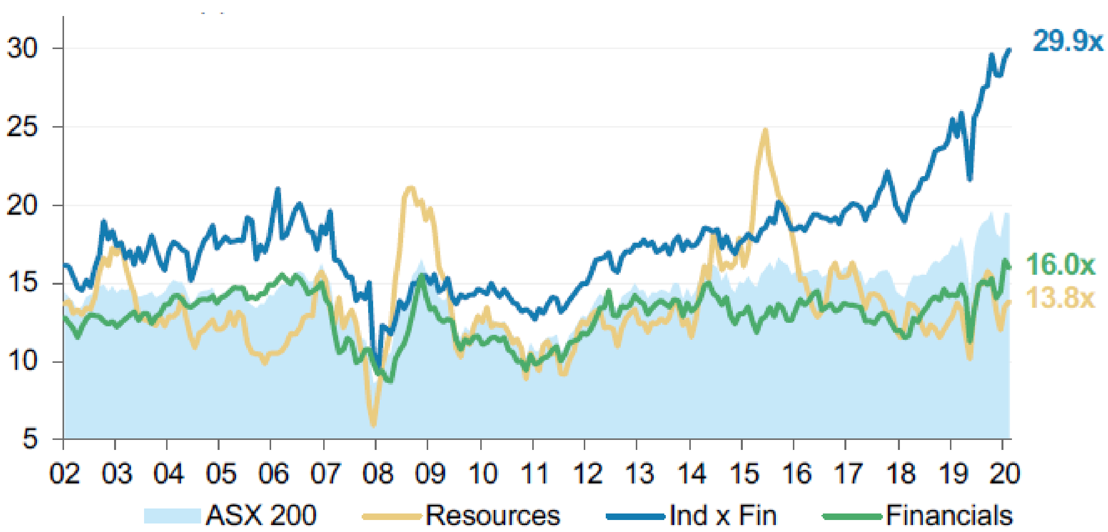
Macquarie's Insync Bond Model suggests the US 10-year should be around 2%, more than double the current level. This is consistent with Blackstone strategist Byron Wien in one of his 10 Surprises of 2021, contending that the surge in economic growth should cause the 10-year Treasury yield to rise to 2%.



Source: FactSet, Macquarie Research, December 2020

The market multiple should de-rate somewhat as yields rise, and consequently we continue to favour stocks that perform better in periods of reflation (i.e. resources, select financials and value) and stay cautious towards those names that benefit more from lower yields (bond proxies, growth-at-any-price, and healthcare, which tend to be $US denominated earners).

ASX 200 Macro Sector 12MF P/E



Source: RIMES, IBES, Morgan Stanley Research

To summarise your portfolio's positioning:

1. Quality Franchises, Growth at Reasonable, Attractive Valuations

Solid companies with strong/leading market positions and credible management with good balance sheets
James Hardie Industries, NextDC, Medibank Private, Reliance Worldwide, United Malt, Treasury Wines and ALS

2. Businesses that are highly cyclical or seasonal in nature, facing headwinds

Heavily discounted companies with strong market positions and strategic assets, but very sensitive to economic conditions/seasonality/weather
Graincorp, Nufarm, Downer EDI and Ampol

3. Turnarounds

Sound businesses that have historically generated poor returns, have been poorly managed, under-earned versus their potential, are in transition and where we think earnings/returns will improve over the medium term. Out of favour with the market, somewhat contrarian positions
QBE, Fletcher Building and Tabcorp Holdings

4. Deep Value Resource Plays

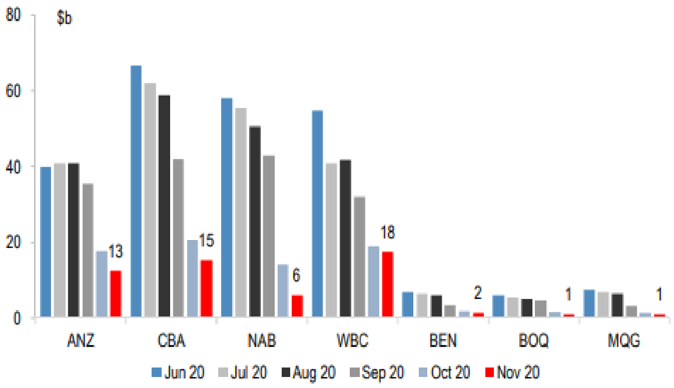
Stocks trading at discounts to NPVs, where much of the heavy lifting has been done (cost out, self help deleveraging)
South32, Woodside Petroleum, Deterra Royalties, Western Areas and Northern Star Resources

We recently reduced the underweight to Financials, where we now own 2 of the big 4 Banks.

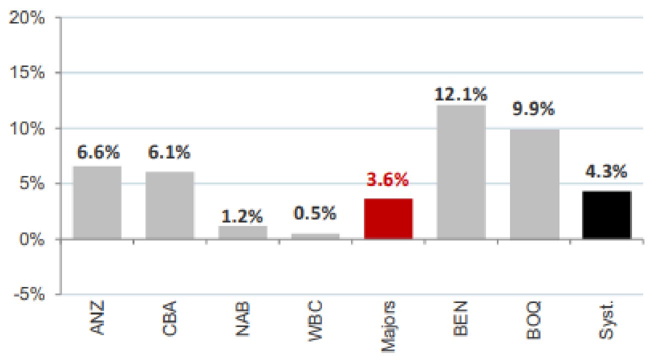
We also participated in the IPO of Liberty Financial, which has performed well post listing.

In looking for emerging green shoots in the financial sector, we were observe two key positive trends. First, loan deferrals continue to sharply trend down vs June 2020: there were $60bn of loan deferrals as at 30 November 2020, down 30% month-on-month. As an indicator of the underlying improvement in the economy and sentiment, SME deferrals have reduced materially in recent months and are now in line with housing (as a % of loans). The chart below (left) shows the trend in total loan deferral balances. Second, a sign that sentiment and economic activity was recovering can be seen in the pickup in housing loan growth. The system is now tracking at +4.3% (November 2020 annualised). See the chart below on the right. **These trends are very positive for the banks' revenue and earnings trajectory, with likely implications for dividends all pointing to the upside vs consensus forecasts.**

Total loan deferral balances



One-month annualised housing loan growth



Source: APRA

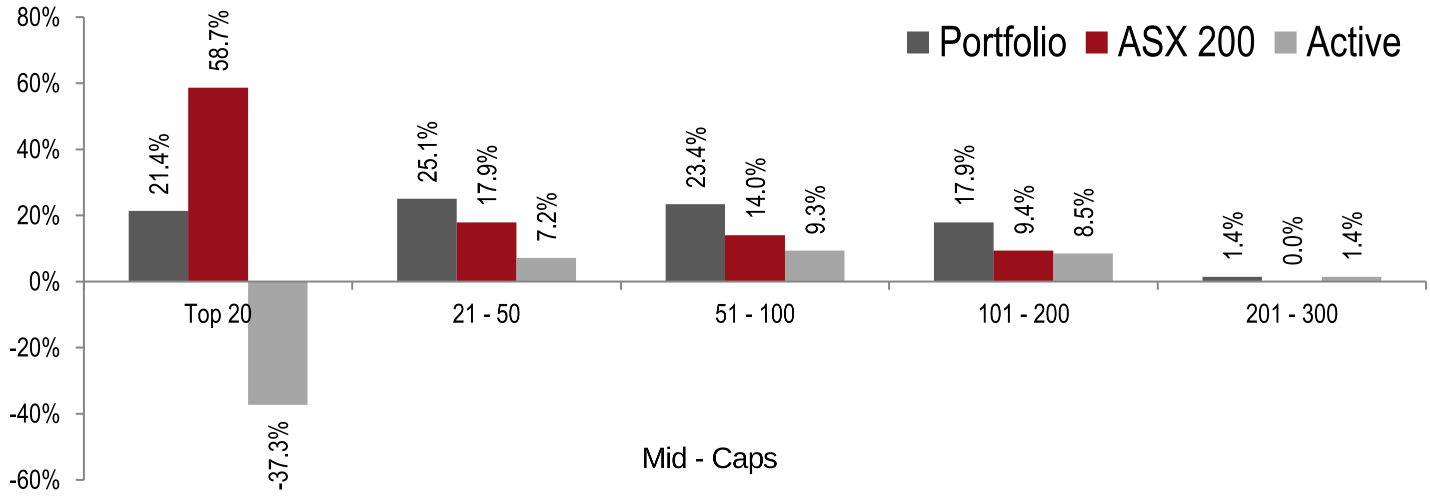
Warm Regards,

Chris Kourtis

Portfolio Manager

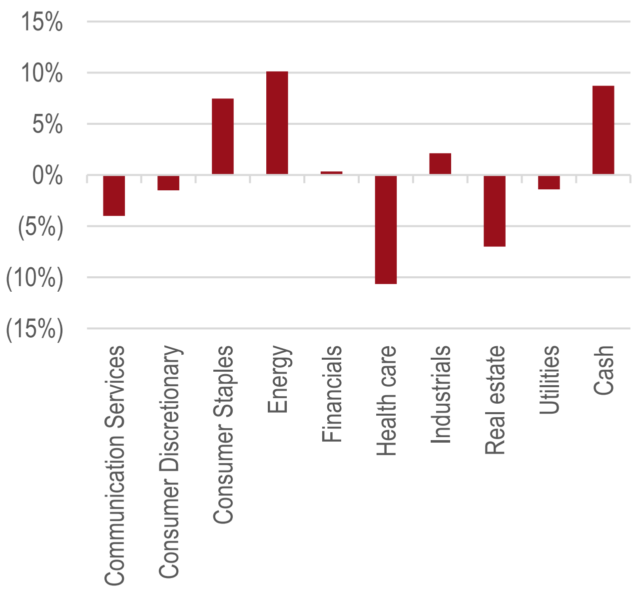
PORTFOLIO FEATURES

Size comparison Chart vs ASX 200^



^Size Comparison Data as at 31 December 2020
Source: Bloomberg, Ellerston Capital Limited

Active Sector Exposures*



TOP 10 HOLDINGS**
AMPOL
ANZ BANKING GROUP
GRAINCORP
MEDIBANK PRIVATE
NORTHERN STAR RESOURCES
QBE INSURANCE GROUP
TABCORP HOLDINGS
UNITED MALT GROUP
WESTPAC BANKING CORP
WOODSIDE PETROLEUM

Source: Ellerston Capital Limited

* Active sector exposures are determined by subtracting fund sector weights from benchmark weights. Positive percentages represent over-weight sector exposures relative to benchmark and negative percentages represent under-weight sector exposures relative to the benchmark.

** Top 10 Holdings are listed in alphabetical order.

ELLERSTON CAPITAL

ABOUT THE ELLERSTON AUSTRALIAN SHARE FUND

The Fund aims to achieve its performance objectives by adopting a fundamental “bottom-up” investment approach to stock selection which is focused on identifying and then constructing a portfolio of the highest conviction ideas.

Investment opportunities for the Fund are identified by analysing and understanding the factors affecting (amongst other things): business model, industry structure, management team and overall valuation. Ellerston Capital typically favours businesses that can sustain high returns or improve their return on capital and looks to invest in businesses with a market value below the value we attribute to them.

Benchmark weightings do not drive our stock decisions, our approach is totally benchmark independent.

Due to the high conviction nature of the portfolio and the resulting deviation in portfolio composition relative to benchmark weighting, it is expected that the returns from the Fund will differ significantly from the broader market indices.

FUND FACTS

STRATEGY FUNDS UNDER MANAGEMENT	$1 Billion
FUNDS UNDER MANAGEMENT – ASF UNIT TRUST	$14.85 Million
APPLICATION PRICE	$0.9415
REDEMPTION PRICE	$0.9369
NUMBER OF STOCKS	22
INCEPTION DATE	1 APRIL 2009

Source: Ellerston Capital Limited

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

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