

Ellerston Overlay Australian Share Fund (OASF)

Performance Report, September 2021

Investment Objective

The Investment objective for the Ellerston Overlay ASF 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

Class Inception**	1 July 2011
Portfolio Manager	Chris Kourtis
Application Price	\$1.2789
Net Asset Value	\$1.2757
Redemption Price	\$1.2725
Liquidity	Weekly
No Stocks	22
Management Fee	0.90% p.a.
Performance Fee	15% p.a. of outperformance
Buy/Sell Spread	0.25% on application 0.25% on redemption

Performance Class A (%)	1 Month	FYTD	1 Year	2 Years (p.a.)	5 Years (p.a.)	7 Years (p.a.)	Since Inception (p.a.)**
Net^	-0.89	4.24	37.08	10.19	6.99	7.68	8.09
Benchmark*	-1.85	1.71	30.56	8.27	10.42	9.14	9.54

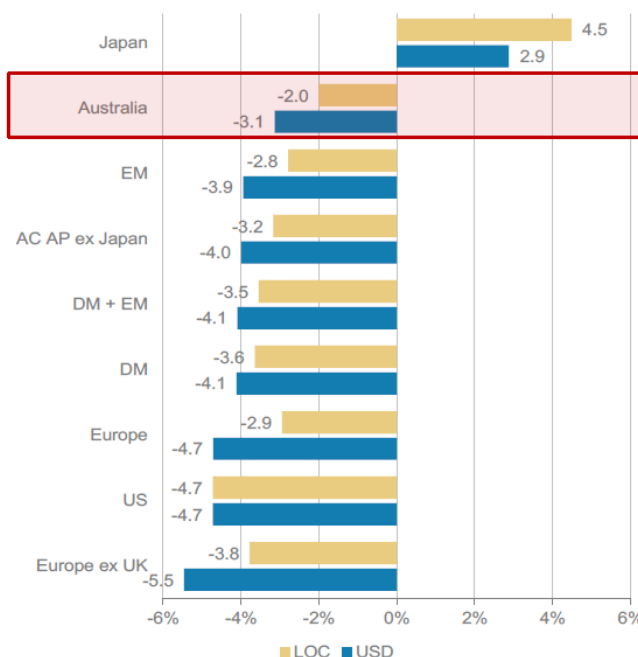
^Net return figure is calculated after fees & expenses. Past performance is not a reliable indication of future performance.

*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

MARKET OVERVIEW

Global equity market performance took a step backwards in September with the Developed Markets World Index declining 3.6% in local currency terms, largely driven by the 4.7% fall in the S&P 500. The evolving Evergrande imbroglio in China led to global uncertainty, driving a sell-off in the bond market and at the same time, highlighting potential contagion risk for the regional banking sector. Iron ore prices cratered a further 22% and energy prices spiked across all regions. The US Federal Reserve shifted to a more hawkish stance, signalling a faster and earlier tapering of asset purchases, leading to higher bond yields and a stronger US dollar. Global bourses were led by Energy, Financials and Consumer Discretionary sectors.

The Australian share market took a breather. After 11 straight months of positive returns, it dropped 1.9%, but still managed to outperform most global peers in what was a dismal month for all equity markets, except Japan.



Source: Morgan Stanley.

USA

At the press conference following the September FOMC meeting, Fed Chair Powell was very explicit that the tapering announcement will likely be made as early as the next FOMC meeting in November. He also said there was broad consensus on the timing and pace of the taper, such that the Committee expects net asset purchases to move to zero in mid-2022. Additionally, Powell also noted that supply-chain bottleneck effects have been larger and longer lasting than anticipated, leading to higher inflation projections. Powell was also less dismissive than in July on the impact that the new rise of COVID cases could have on the economy. He espoused that the Delta variant has affected return to work plans and that the August employment report weakness in travel and leisure was likely driven by the Delta variant. He still expects headwinds linked to the virus to fade over time supporting the recovery. However, it might take longer for employment to recover than previously thought. US bond yields rose 20bps over the next week and the S&P500 fell 3%.

September economic activity indicators were mixed. The manufacturing ISM ticked up to 59.9 from 58.5, which was above expectations. However, the rise in non-farm payrolls of just 235k in August was way below consensus and the July print of 943k, as leisure and government hiring momentum stalled, the likely result of labour market bottlenecks and Delta headwinds. At the same time, the unemployment rate ticked down to 5.2% due to a flat participation rate. The August core CPI at +0.1% mom (+4.0% yoy) was another step down from the inflation surges over the three months from April to June. Finally, August retail sales up 0.7% mom, exceeded expectations after being down 1.1% in the previous month.

Against this backdrop, US equities had their first drawdown since January this year, the Dow Jones Industrial Index down 4.2%, the S&P 500 ending the month down 4.7%, with the laggard being the Nasdaq Composite Index which fell 5.3%.

Europe

On the economic front, the August Eurozone Manufacturing PMI figures were weaker at 61.4 (62.8 in July), however, the Composite PMI was flat at 59.0.

The Euro STOXX 50 Index finished the month down 3.4%. Among the major exchanges, the UK's FTSE 100 fell 0.2%, France's CAC 40 was down 2.2% and Germany's DAX was the laggard, closing down 3.6%.

Asia

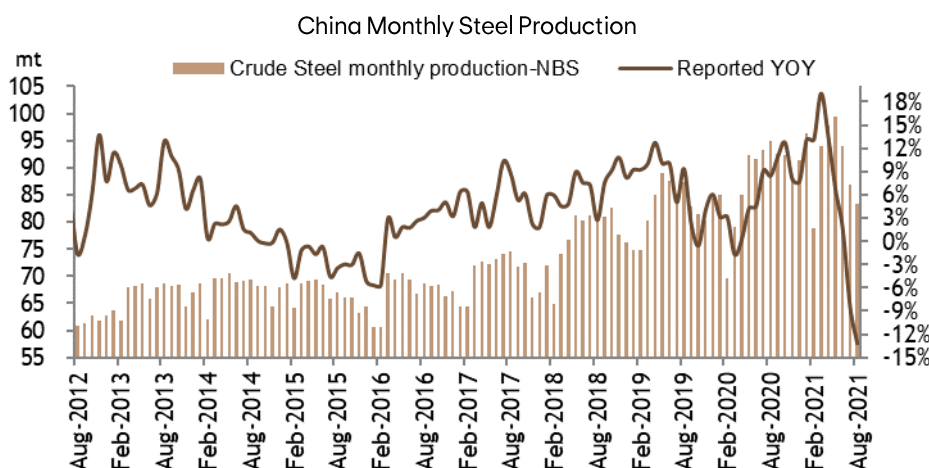
China's economic activity weakened across the board, hit by COVID restrictions, especially on the consumption side. August retail sales growth slowed sharply to +2.5%yoy (+8.5%yoy previously). COVID related mobility restrictions were mainly to blame, especially on catering (-4.5%yoy), travelling (auto sales -7.4%yoy) and other service activities. Property sales slowed notably as expected, while real estate investment growth also softened. Industrial production momentum cooled further to 5.3%yoy from 6.4%yoy and Infrastructure FAI narrowed yoy to -6.6%yoy versus -10.1%yoy, thanks to fading flood shocks and more explicit fiscal support. Surprisingly, export growth accelerated from 19.3%yoy to 25.6%yoy, partly on supply chain disruptions elsewhere which despite a rise on commodity imports, posted a trade surplus of \$58.3bn, 3% percent better than July.

The financial woes of Evergrande, China's second largest property developer, deteriorated further during the month. Investor concerns that a credit event could spill over to other developers, suppliers and de-rail the financial system seem overdone. Steps have been taken to ensure an orderly restructuring, Chinese banks lending to Evergrande are sufficiently collateralized and few banks have exposure to its corporate bonds, mainly held via wealth management products. However, there is the real risk that consumer psychology is impacted in such a way that potential homebuyers become increasingly unwilling to prepay for housing. Prepayments are a vital funding tool for all Chinese developers, and if this funding mechanism starts to dry up, other developers might follow Evergrande's path to default, especially those already exhibiting funding problems.

Asian equity markets were mixed with the Nikkei 225 up 5.4%, India's SENSEX up 2.8% and China's SSE Index up 0.5%, whilst the Hang Seng was down 4.7% and Korea's KOPSI down 4.1%.

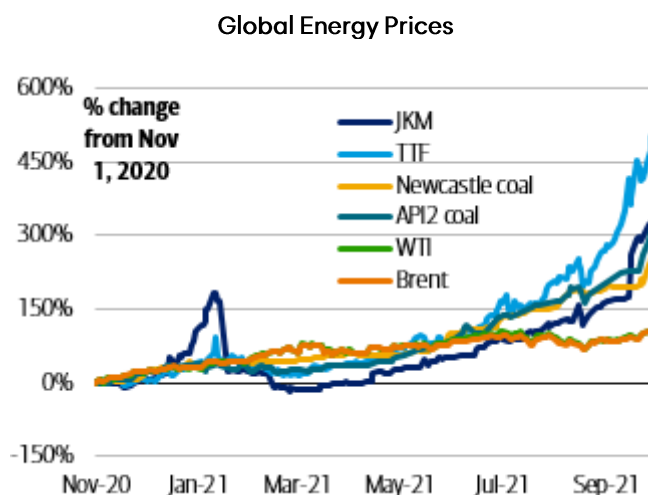
Commodities

Iron ore tumbled another 22% as Beijing's measures to cap Chinese steel output gained more traction, with large reductions year on year. The recent power shortage has materially impacted downstream demand, which will no doubt impact iron ore demand in future months. The iron ore benchmark price has surprised most observers with the speed and ferocity of the correction and prices have now pulled back from the record high of US\$238 (A\$304)/tonne in May, closing at US\$119/tonne for the month after hitting an intra-month low of US\$93/tonne, 50% from the record high.



Source: UBS.

Global energy prices encompassing oil, gas, thermal coal and electricity, and from China to Europe to the United States spiked in September. Record prices in the EU and Asia were achieved due to surging demand against a backdrop of supply disruptions and higher coal and EU carbon prices.



Source: BofA Global Research.

The Brent oil price ended 7.5% higher at US\$73 per barrel, as rigs in the Gulf have stayed offline longer than expected due to safety issues and damage from Hurricane Ida and concerns that demand is stronger than OPEC+ forecast when they pledged to lift oil supplies by an extra 400,000 barrels per month under their new production agreement. Gas prices went absolutely ballistic, with Asian Spot LNG prices up 70% to JKM at US\$31.10/mmbtu and US Henry Hub gas prices up 32% to US\$5.82/mmbtu. As a reference point, Asian spot LNG prices languished at US\$2.00/mmbtu at the height of the pandemic due to demand destruction. Thermal coal prices were up 25% in September, finishing at US\$218/tonne.

Gold closed the month down 3% at US\$1,757 per ounce as bond yields rose and the US dollar strengthened. The base metals complex was also weaker with the same drivers as gold, although late in the month, the power tightness in China raised concern on downstream demand for base metals.

Bulk commodities were the superstars of the month, with hard coking coal up 50% to US\$389/tonne (a far cry from US\$100/t at the start of the year) and alumina up 45% to US\$457/tonne - see the Trading Activity section for a run down on the dynamics of the alumina market.

Bonds

The Fed telegraphed an aggressive pace of QE tapering and although this was not entirely unexpected by the market, it did result in a large back-up in yields. US 10-year treasury yields rose 19 basis points to 1.49% and the Australian 10-year bond moved up 28 basis points to 1.16%. As the first DM central bank to tighten policy, Norges Bank decided to hike its official rate by 25 bps, the first of two rate hikes in 2021. Moreover, the Bank decided to use its freshly new countercyclical buffer mandate by raising it to 2.0% in December. This was justified by the rapidly rising housing prices and accelerating credit growth. The statement said that "the policy rate will most likely be raised further in December". Other developed market central banks are expected to follow their lead.

The AUD was slightly weaker at US72 cents as the US dollar Index hit its highest monthly close since October last year, driven by the rise in US treasury yields. Not surprisingly, given the lockdowns on the East Coast, the RBA left the cash rate on hold at 0.10%.

Australia

The Australia equity market finally retreated in September after 11th straight months of advances, its longest winning streak since 2007.

In September, the S&P/ASX 200 Accumulation Index fell 1.9%. The Energy sector (up 16.7%) was the most significant contributor to the Index's performance, adding 46 basis points, followed by Financials (up 1.6%), contributing 45 basis points and then Communication Services (up 1.3%) contributing 5 basis points. The bottom three contributing sectors were Materials (-172 points) again the worst, Healthcare (-53 points) and Consumer Staples (-19 points).

The best performing sub-index was the ASX 200 Industrial Index which fell only 0.8%, outperforming the broader benchmark, whilst the major underperformer was again the ASX 200 Resources Index, which was down 6.6% as a result of the further weakness in iron ore prices.

The top five stocks that made a positive contribution to the Index's return were: CBA (+35 points), Macquarie Group (+24 points), Woodside Petroleum (+20 points), South32 (+10 points) and Santos (+10 points).

Conversely, the top five stocks detracting from the Index's performance were: BHP Group (-73 points), CSL (-37 points), Fortescue Metals (-31 points), Rio Tinto (-21 points), and Wesfarmers (-18 points).

COMPANY SPECIFIC NEWS

The Market Hits

Beach Energy (BPT +42.4%) / Woodside Petroleum (WPL +22.5%) / Santos (STO +18.5%) / Oil Search (OSH +17.4%)

Energy was the best performing sector for the month with a return of +16.7%, driven by surging oil and gas prices. Oil prices were up 7.5% caused by global under investment in new projects and ongoing supply issues caused by Hurricane Ida in the Gulf of Mexico. Spot Asian LNG prices were up a massive 70% as coal outages in China and lower European gas inventories pushed the JKN LNG futures to near record highs above US\$30.00/mmbtu. Santos and Oil Search finally entered into a definitive agreement to merge the two companies in an all-scrip transaction after completing reciprocal confirmatory due diligence which started in early August. BPT announced it had entered into a Heads of Agreement with BP plc regarding purchasing 3.75 million tonnes of BPT's share of LNG commencing in H2 2023 from its Waitsia Gas Project Stage 2 in W.A., which saw the stock jump 10.5% on the day.

Flight Centre Travel (FLT +30.8%)

FLT was buoyed during the month as Australian vaccination rates soared. With the prospect of domestic and international travel looking like a 2021 year end reality, FLT's monthly cash burn should begin to recede.

AusNet Services (AST +30.2%)

Energy transmission company AST received an unsolicited, indicative, non-binding and conditional proposal from the infrastructure affiliate of Brookfield Asset Management to acquire all of the issued shares in AST at \$2.50 cash per share via scheme of arrangement. The bid price will be reduced by any dividends paid or declared by AST prior to the transaction. This proposal follows an initial bid at \$2.35 on 30 August 2021, and a subsequent revised proposal at \$2.45. AST granted Brookfield 8 weeks exclusive due diligence. The next day, local pipeline company APA announced a counter-offer at \$2.60, comprising scrip (0.0878 APA shares per AST share) plus cash (\$1.82 per AST share). Surprisingly, investors reacted negatively to APA's bid, pushing the stock down 5% on the day. APA has made an application to the Takeovers Panel to hear its case and seeks final orders, including that the exclusivity arrangements be terminated and/or be made subject to a customary "fiduciary out" in order to permit AST to respond to APA's proposal (and any other competing proposals). At the time of writing no decision by the Panel has been made.

Whitehaven Coal (WHC +27.7%)

WHC had another strong month as thermal coal prices continued to rally, with lower production in China and high global gas prices pushing thermal coal up 25% to an eye-watering record high of US\$218/tonne. Also, WHC reacted positively to the Federal Government's approval of the company's Vickery Extension Project after the NSW Independent Planning Commission had approved the project in August 2020.

Altium (ALU +19.6%)

ALU shares bounced back to pre-results levels after falling by ~14% in late August on the back of the release of a messy set of unaudited accounts. First there was a delay in reporting due to a COVID fuelled shortage in auditors, then the company was sued by its former CFO. To confuse matters, management then issued a downgrade to FY22 margin guidance, revealed a \$US118.5m tax liability (due to a disagreement between the ATO and IRS), and backed away from their previous aspirations by pushing their long term US\$500m revenue target out by a year to FY27. Despite these negative factors, the lack of a clear catalyst driving this month's price recovery may simply reflect that shares were oversold. Investors continue to see the underlying business as intact and their pivot to the 365 ecosystem as the right strategic move.

IDP Education (IEL +18.4%)

IEL shares surged in September as investors continued to look past the flat COVID affected FY21 results, focusing on the FY22/23 outlook and recovery profile of the business. The business has performed pretty well in a challenging year for international students. IELTS volumes have recovered and are showing solid momentum moving into FY22, with the northern hemisphere now above pre-pandemic levels. UK and Canadian student placements are seeing strong demand, and the acquisition of BC India is expected to produce a substantial uptick in leads in FY22. The recovery in the key Indian market, which now represents ~52% of PF group revenue, seems on track. IEL remains a favoured reopening play and domestically, as vaccination rates continue to climb, IEL's planned 2H22 recovery in Australian student placements looks increasingly feasible, which should re-enforce the FY23 step up in earnings. This is critical, as the stock trades on a lofty valuation of 96 times consensus FY22 expected after tax earnings.

Alumina (AWC +18.0%)

Alumina prices have risen 45%, mostly in the second half of the month, which has fired up alumina producer AWC's stock price. Please refer to the Trading Activity section for more detail on AWC, which was added to the portfolio, as well the recent changes in the alumina market which have propelled prices.

The Market Misses

IRESS (IRE -21.3%)

Iress shares pulled back sharply from recent highs of \$15.25 post the announcement that discussions with bidder EQT had concluded, with both parties unable to agree on a price. EQT's APAC Chairman also made a statement noting that no red flags had been uncovered during their due diligence process, but were unable to confirm their original investment hypothesis. IRE then went on to say that the company remained committed to their 2025 targets to double NPAT and at the same time, reaffirmed guidance for FY21 of \$164-168m. Management also noted that there will be ~\$4-5m of one-off costs related to the failed transaction. The stock price has now retreated all the way back to the theoretical undisturbed price of ~\$11.50/share, from when the rumours in the press first circulated in early June of a potential strategic buyer of the business.

Fortescue Metals (FMG -20.7%) / Mineral Resources (MIN -18.4%) / Champion Iron (CIA -18.0%)

All of the above iron ore producers were severely impacted by the collapse in iron ore prices from the sky high prices which have ruled mid-way through this year, peaking at US\$238/t in May. It was another rollercoaster ride during the month, with the benchmark price falling 40% to a low of US\$93/t, before re-bounding and finishing the month down 23% at US\$119/t. China's steel production was further impacted by severe power shortages, impacting downstream demand as well as the Ministry's imposed emissions restrictions which will last until after the Beijing Winter Olympics.

Magellan Financial Group (MFG -18.4%)

Hot on the heels of a disappointing profit result during the recent reporting season, MFG shares fell sharply after a string of sell side analysts cut their recommendations to "underweight". Analysts cited continued net retail outflow during August in its flagship Global Equity strategies and elevated fee pressure. Investment underperformance has shaken advisor confidence, with the Global Fund now ~19% below benchmark over the rolling 12 months and seemingly showing no signs of abatement. MFG's much higher than average retail fees (standing at 135bps) and below average performance has investors worried that base management fees will need to be sharpened, just to stay competitive. The last major fee adjustment was in 2017, when Platinum cut its rate from 150 bps to match MFG. The other concern weighing on sentiment is the concentration risk in MFG's institutional book (the potential for mandate losses and/or fee cuts if performance does not turn around) and the removal from July 2023 of huge tax benefits embedded in MFG's Offshore Banking Unit, where a concessional tax rate of just 10% is applied. This reverts back to a full corporate tax rate after that time post the introduction of a new bill in March 2021. Conclusion: expect more outflows and share price weakness.

BlueScope Steel (BSL -17.1%)

BSL fell in line with its US peers despite all-time high US hot-rolled steel prices, a positive messaged investor day late in the month and its \$500m share buyback kicking in. The jury is still out on when the current record prices will ease and by how much, which has seen US steel stocks' earnings multiples de-rate by ~20% during the month, unfortunately dragging down BSL with them.

Regis Resources (RRL -17.5%)

The 3.3% fall in gold prices saw the gold sector down a whopping 9.8%. However, RRL has been under pressure for months since completing its \$900m acquisition of a 30% interest in the Tropicana gold mine from Independence Group. Disappointingly, indigestion followed the associated \$650m deeply discounted capital raising at \$2.70/share, a level now 34% above where the stock price finished the month. The weak profit result announced on the 31 August didn't help management credibility and its performance this month either.

Appen (APX -16.6%)

Following a series of disappointing results, artificial intelligence data collection company Appen continued its downward trajectory after peaking at \$43.66 back in August 2020. APX's market cap has now fallen to \$1.1bn, down an astonishing 79% since those dizzy levels, with the former market darling closing at \$8.96. APX's reported results at the end August disappointed on the revenue line and saw a 44% drop in operating cash flow versus pcp. Management's guidance is heavily reliant on a pick up in the second half, with the expectation of a stronger order book, higher customer demand and a strengthening pipeline. The lack of visibility on the earnings outlook continues to prove challenging for the market to digest.

Codan (CDA -15.1%)

CDA predominantly designs and manufactures metal detection equipment for recreational, mining and military markets. The broad sell-off in technology companies during the month, the global shortage of semiconductors as well as the uncertainty with the search for a new CEO, after last month's announcement of the retirement of its long standing leader Donald McGurk, all weighed on the stock's performance.

Omni Bridgeway (OBL -14.9%)

OBL shares came under pressure this month after the company warned investors of a potential write-down on a judgement the company won in 2019 in relation to Brisbane's 2011 severe flooding. Queensland government owned dam operator, Seqwater, appealed against a NSW Supreme Court decision, which had found the operator liable for half the damage from the Wivenhoe dam flood. Disappointingly, the successful appeal slashed the \$900m expected pay-out for the ~6,500 victims' homes impacted by the flooding, leaving a \$440m settlement that Sunwater and the Queensland government had previously agreed to. The appeal ignited a sell off, with OBL shares sliding 5.7% on the day.

FUND PERFORMANCE

In a dismal month for global equity markets, the Fund's return of -0.80% outperformed the benchmark return of -1.85% on the downside, with Australia performing better than most markets. It caps off a strong performance by the Fund for the September quarter.

Our conviction in expecting lower iron ore prices and not owning BHP, RIO, Fortescue or Mineral Resources more than offset significant contributions to the benchmark return by the major banks which outperformed by 3.5%, where the Fund had very little exposure.

In terms of factor analysis, cyclicals and value outperformed. Financials (+1.6%), Energy (+16.7%) driven by Woodside Petroleum and Santos up 22.5% and 18.5% respectively and Communication Services (+1.3%) were favoured.

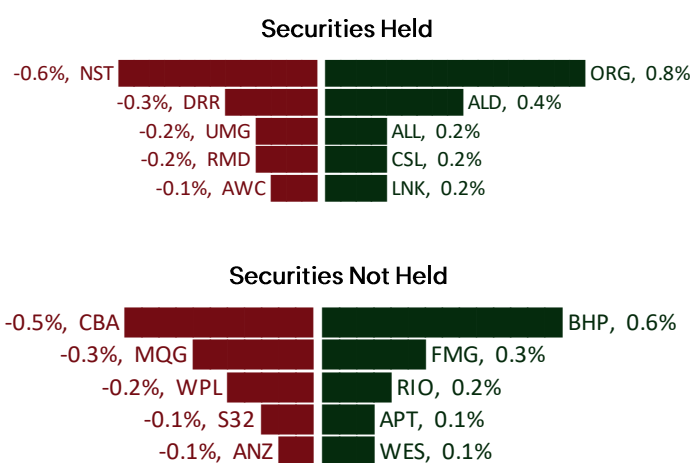
Returns [^] (%)	Gross	Benchmark [*]	Excess	Net
1 Month	-0.80	-1.85	1.06	-0.89
3 Months	4.54	1.71	2.82	4.24
2022 FYTD	4.54	1.71	2.82	4.24
1 Year	38.63	30.56	8.07	37.08
2 Years (p.a.)	11.38	8.27	3.11	10.19
3 Years (p.a.)	7.49	9.65	-2.17	6.33
5 Years (p.a.)	8.01	10.42	-2.41	6.99
7 Years (p.a.)	8.71	9.14	-0.43	7.68
Since Inception (p.a.) ^{**}	9.23	9.54	-0.31	8.09

[^]The return figures are calculated using the redemption price for Class A Units and are net of fees and expenses. Returns are also calculated on the basis that distributions are reinvested. 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.

^{**} Since Inception is 1 July 2011.

Month of September Attribution



Source: Ellerston Capital.

The main positive contributors to this month's performance were overweight positions in: Origin Energy (ORG +7.7%), Ampol (ALD+3.6%), Aristocrat Leisure (ALL +1.7%) and Link Administration (LNK +0.6%).

Zero weight positions that also helped included BHP Group (BHP -12.2%), Fortescue Metals (FMG -20.7%), Rio Tinto (RIO -10.6%) Afterpay (APT -9.9%) and Wesfarmers (WES -5.6%).

The main detractors to performance for the month were overweight holdings in: Northern Star Resources (NST -12.1%), Deterra Royalties (DRR -11.0%), United Malt Group (UMG -9.1%) and Resmed (RMD -9.4%).

Not holding the following shares that outperformed the broader market and somewhat constrained returns were: Commonwealth Bank (CBA +4.2%, fuelled by its \$6bn off market buy-back), Macquarie Group (MQG +9.2%), Woodside Petroleum (WPL +22.5%), South32 (S32 +15.0%) and ANZ Bank (ANZ+1.1%).

FUND ACTIVITY

Whilst many stocks and sectors have re-rated significantly from their March 2020 lows, we continue to seek, and more importantly are, finding opportunities that we believe are highly compelling.

The Fund strengthened core positions, namely Ampol, CSL, Deterra Royalties, JB Hi-Fi, Janus Henderson and Telstra. The Fund also locked in further profits and de-risked holdings that have outperformed over the past few months (namely Aristocrat Leisure, Resmed, Suncorp and Westpac). We totally exited NextDC post the CEO selling ~80% of his direct holding.

Having introduced Resmed (RMD) to the portfolio in March 2021 (initial purchases were around \$24.25), we de-risked and exited the bulk of the position at ~\$39.00 in early September, locking in a substantial ~60% return (before the stock sold off). This cull followed an extraordinary re-rating of the company post main competitor Phillip's product recall, where RMD is capturing market share. The weighting in RMD has been reduced from over 7% at the start of the month to 1.5% at the end of the month. We believe this story is now well known in the market, has largely played out and is priced in. Even post the late September pullback, at \$35.00, the shares are currently trading on 41 times consensus FY22 earnings. We are methodical in aggressively rotating out of stocks when they reach our assessed valuation a lot quicker than anticipated.

During the month we introduced two new stocks, Alumina and PointsBet Holdings into the portfolio (see detailed write-up on Alumina below).

NEW STOCKS ADDED

- Alumina
- PointsBet Holdings

STOCKS EXITED

- NextDC

INCREASED

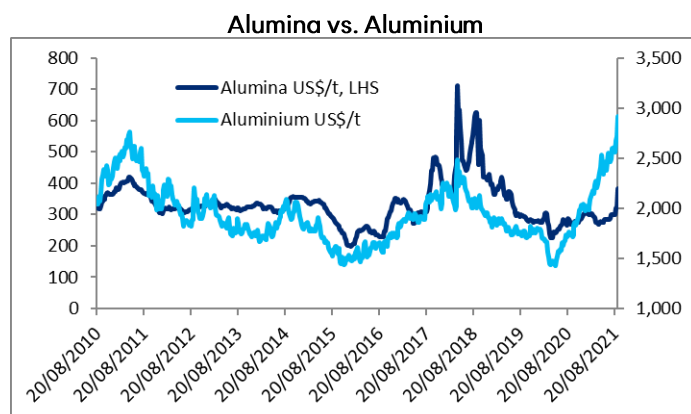
- Ampol
- CSL
- Deterra Royalties
- JB Hi-Fi
- Janus Henderson
- Telstra

DECREASED

- Aristocrat Leisure
- Resmed
- Suncorp Group
- Westpac Banking Corp

Alumina Limited (AWC)

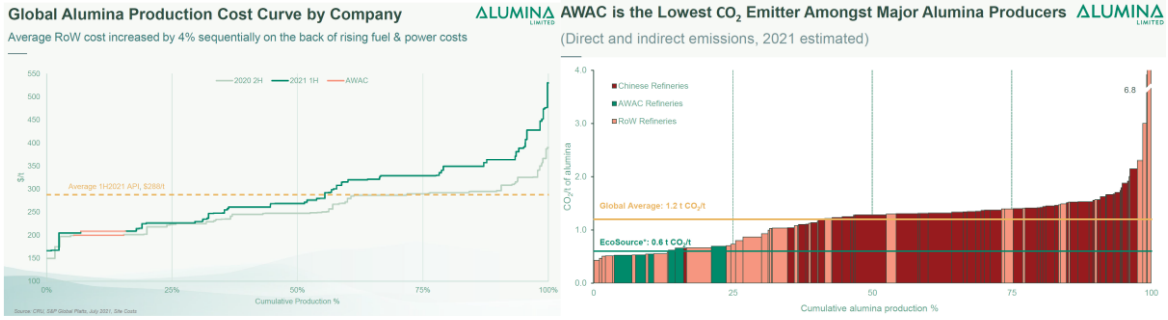
Having peaked at over \$6.00 in 2007 (pre-GFC), collapsing post the GFC and then subsequently raising equity at \$1.00 (to repair a weakened balance sheet), AWC shares have been highly volatile ever since. They have been a poor performer over time and we believe this is about to change. China's cap on aluminium capacity in its drive to reduce carbon emissions, make it difficult for the government to relax the cap, bearing in mind the Winter Olympics are just around the corner in February. This means that the 50%+ expansion in capacity over the last decade has now come to pass and with it, the growth in alumina capacity. New supply ex-China will be required to meet demand, resulting in higher average prices (aluminium prices are at decade highs). Recent disruptions only serve to amplify this dynamic.



Source: Citi.

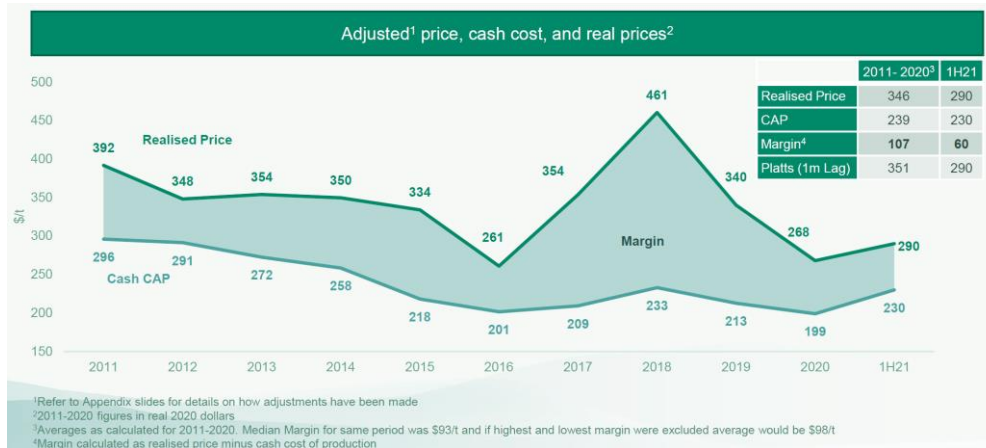
AWC owns 40% of AWAC (Alcoa 60%) which produces 12.8mtpa of alumina, with the Western Australian assets responsible for 75% of production but a higher share of earnings. AWAC's alumina refineries are in lowest quartile of costs and also for carbon emissions.

AWC is low on the cost curve and low on carbon emissions



Source: AWC.

Alumina prices need to be higher to incentivise new production, which should drive AWC's margins. Real long term prices are now 25% higher than the last 2 years, where they were around the unsustainable 50th percentile of the cost curve.



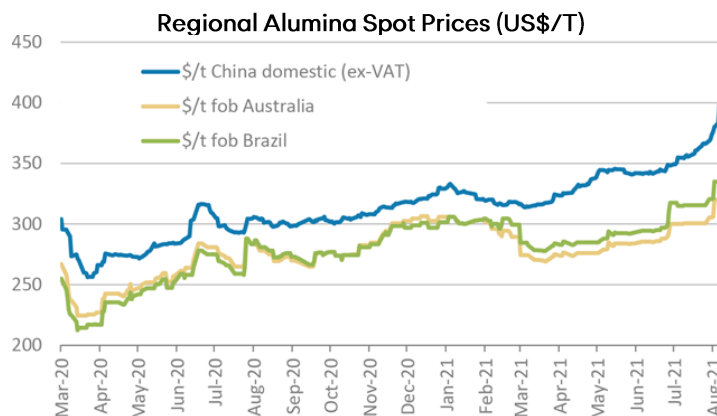
Source: AWC.

Alumina Market

A series of recent disruptions have tipped alumina's previously oversupplied, stable market into deficit, driving a sharp rise in prices and adding to the bullish outlook for aluminium. The disruptions began back in July with the reduction of the 3.8Mtpa Alumar refinery in Brazil to just two-thirds of its operating capacity due to issues with bauxite unloading at the port, which have not yet been resolved. That was joined in late August by the outage at the 1.1Mtpa Jamalco refinery in Jamaica due to fire. In total, 2.4Mtpa of capacity has been removed from the Atlantic market, enough to tip it into deficit and drive a rare premium over the Australia fob price.

The Pacific market has remained impervious to these developments, with China limiting smelter production and high freight rates deterring imports from Australia. But fast rising import costs and disruptions from July's severe flooding in Henan province has already begun to push China's domestic price higher. Power restrictions have spread and the cuts to refinery output have begun to outpace the cuts on the smelting side, leading China's domestic market into deficit. The latest curtailment measures were announced recently in Guangxi province (11% of China's supply), which announced that refineries would be restricted to 50% of their 1H21 output in September (vs 80% for the region's aluminium smelters).

The push to meet annual energy consumption targets and power shortfalls through winter are likely to remain and even spill over into 2022. Exacerbating these already-tight markets has come a military coup in Guinea, which supplies almost a quarter of the world's bauxite (and most importantly 58% of China's). It is too early to tell how this will impact the bauxite supply to China's alumina refineries, but it should drive bauxite prices higher, adding both a sentiment and further cost push to alumina's already disrupted markets.



Source: Morgan Stanley.

We have added AWC to the portfolio as we feel the market is underappreciating the above dynamics, assuming these supply curtailments will be short-lived. Having closed its own higher cost "swing" production facilities such as Point Comfort in the US (remembering the AWAC joint venture had over 18.5mt of system capacity), AWC is now leaner and very leveraged to re-bounding alumina prices. Earnings growth will accelerate and healthy dividend payments should follow. It has also significantly underperformed its 60% AWAC JV partner, Alcoa.



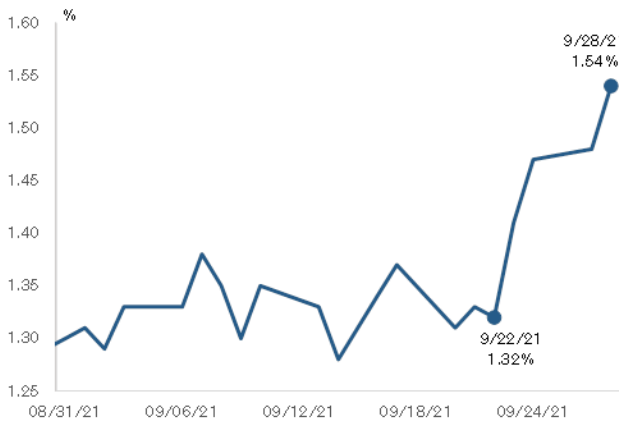
Source: Morgan Stanley.

FUND STRATEGY AND OUTLOOK

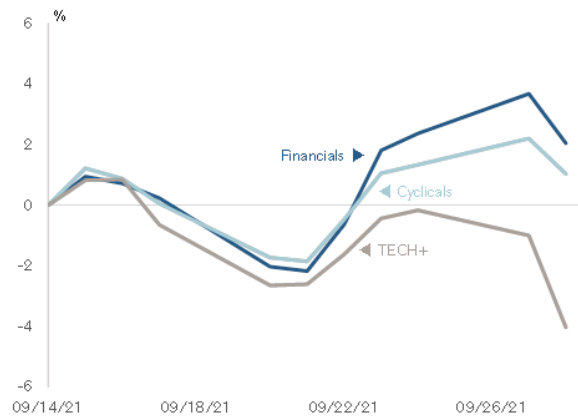
There is little that has changed with respect to our views since our August update. However, we continue to pivot where necessary as discussed in the Fund Activity section.

During the December quarter of 2020, US 10 yields were hovering around 0.80%, then spiked to 1.74% in March of this year, only to rally to below 1.2% in early August. As a reminder, treasury yields rose sharply following last November's Pfizer vaccine announcement, but quickly reversed course at the end of Q1 when inflationary fears were deemed 'transitory'. The direction of interest rates continues to be the key driver of sector and factor performance in the market. Higher yields have typically driven outperformance in the Value and Cyclical cohorts, with lower rates generally supporting TECH+ and Quality stocks. Rising interest rates have once again disrupted global markets on September 22, jumping 22 bps over the next 5 days, putting downward pressure on TECH+ and Growth sectors. This has caused elevated volatility and has driven a broad-based reversal in factor behaviour.

US 10-Year Treasury Yield



US Sector Returns

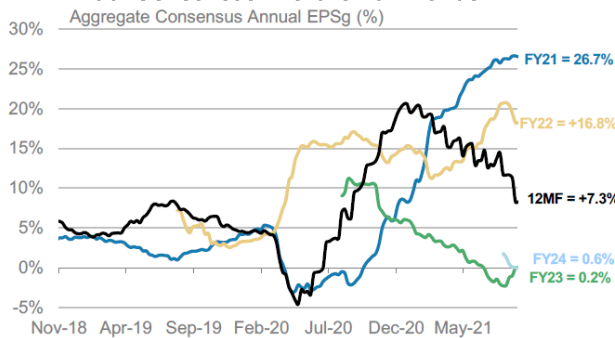


Source: UBS.

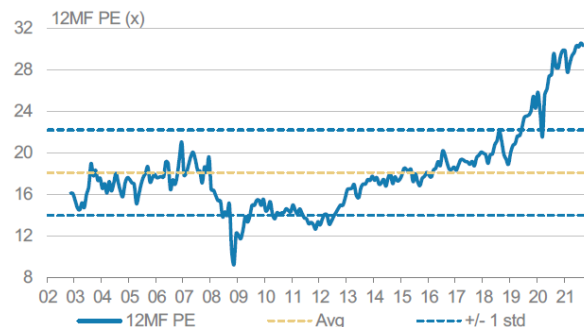
While we would like to believe that fundamentals will drive market internals, recent experience indicates that the direction of rates will dominate the debate, culminating in restless sector and factor rotation.

After a strong upgrade cycle and strong reporting season, FY22 and FY23 earnings momentum looks to have peaked. The December quarter will start to see NSW and Victoria relax restrictions, with the prospect of approaching "normal" again. The All Industrials ex Financials PE is suggesting that the re-opening trade has plenty of optimism already baked in and needs these stocks to deliver significant earnings upgrades over and above current forecasts.

Annual Consensus EPS Growth Trends FY21-24



ASX 200 Industrials ex Financials PE is at 30x



Source: Morgan Stanley.

Since our last newsletter, equity markets globally have softened as US 10-year treasuries and local long bond yields have sold off on concerns over tapering and the recent energy price inflation. Valuations to date have been supported by bond rates and earnings growth, although we have seen a trend of downward revisions acceleration. The inflation genie has been kept in the "transitory" bottle, albeit the forecast

transitory period has lengthened and needs to be monitored closely. The US debt ceiling and the passing of the tied Infrastructure and Social Investment bills are important but we've seen this movie before, a number of times. On the debt ceiling and the passing of the investment bills it's all about compromise which will be reached, although the social component may be watered down further.

In summary, despite the prospect of tapering by the Fed and RBA, central banks will aim to keep interest rates relatively low. Pent up global consumer demand, when overlaid with unprecedented Government and Central Bank stimulus and coupled with massive infrastructure spending, sows the seeds for a "Goldilocks" recovery. That said, more observers are moving into the "stagflation" camp, a period many participants in the market, particularly millennials, have never experienced. For this reason, we have maintained our exposure to the gold sector as a hedge, a strategy that CYTD, has yet to bear fruit, given the sector has performed poorly. The US debt ceiling and the passing of the tied Infrastructure and Social Investment bills are important but we've seen this movie before, a number of times, on the debt ceiling. The passing of the investment bills is all about compromise, which will be reached although the social component may be watered down further.

We believe that the portfolio is well positioned against this backdrop, with the right mix of sensibly priced Growth stocks with strong competitive advantages (e.g. Aristocrat, CSL, Carsales.com and PointsBet), Contrarian Value stocks, Cyclical and select Financials (namely Ampol, GrainCorp, Janus Henderson, JB Hi-Fi, Link Administration and Suncorp). These stocks continue to trade at attractive valuations and taking a medium term view, should re-rate over time.

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
Aristocrat Leisure, Carsales.com, CSL, JB Hi-Fi, Link Administration (cheaper entry into Pexa), PointsBet Holdings, Resmed and United Malt

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

Heavily discounted companies with strong market positions and strategic assets, but very sensitive to economic conditions/seasonality/weather
Ampol, Graincorp, Origin Energy and Suncorp Group

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
Janus Henderson and Telstra

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)
29Metals, Alumina, Deterra Royalties, Northern Star Resources and Western Areas

We have once again pivoted and are virtually zero weighted to the Banking sector, having locked in superior returns and rotated into stocks which we believe offer significant upside.

We are truly grateful for your continued support.

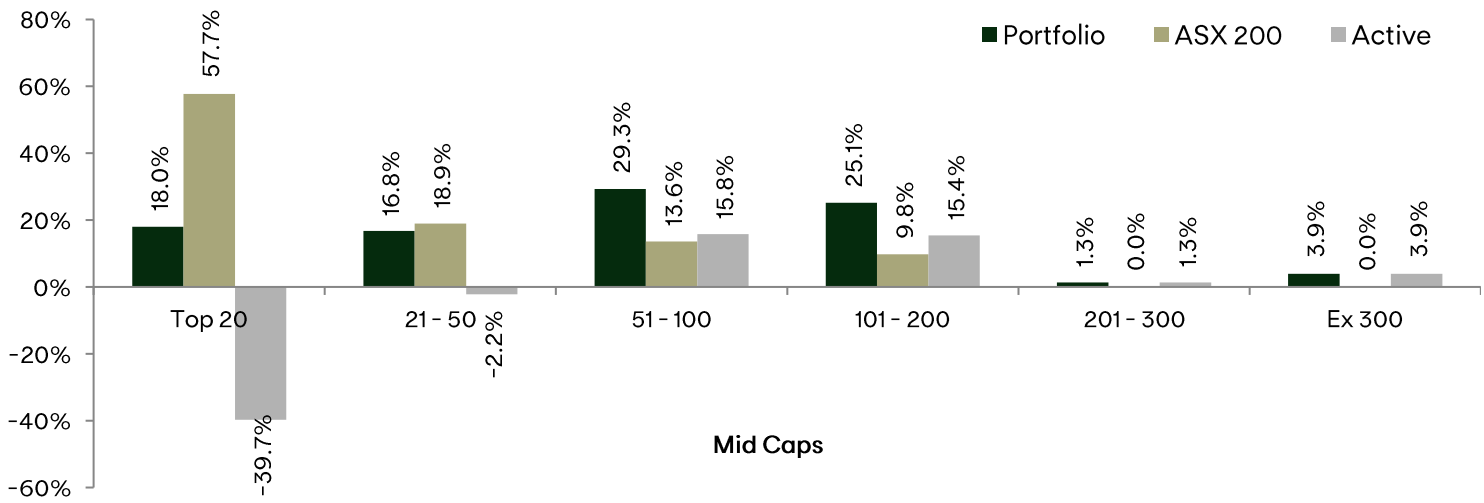
Warm Regards,



Chris Kourtis
Portfolio Manager

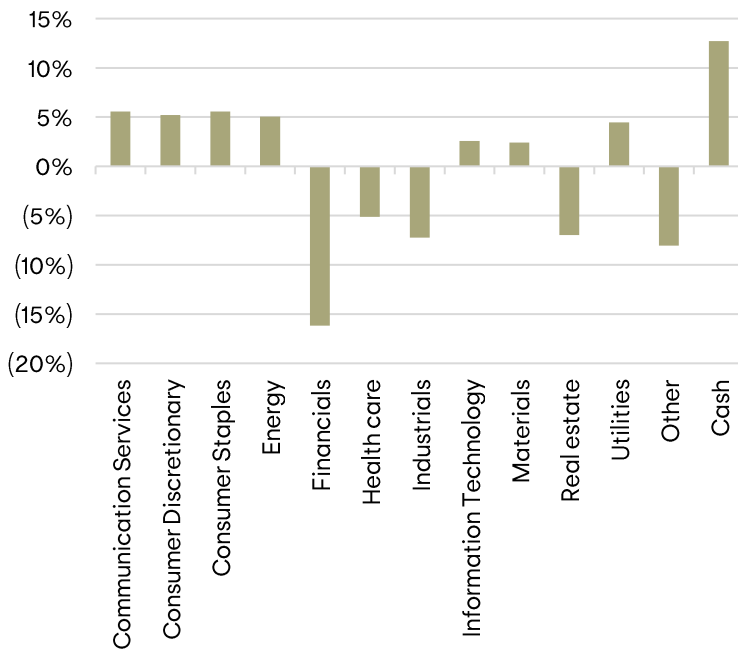
PORTFOLIO FEATURES

Size comparison Chart vs ASX 200^



^Size Comparison Data as at 30 September 2021.
Source: Bloomberg, Ellerston Capital Limited.

Active Sector Exposures*



Source: Ellerston Capital Limited.

TOP 10 HOLDINGS**

ALUMINA
AMPOL
DETERRA
GRAINCORP
JANUS HENDERSON
JB HI-FI
LINK ADMINISTRATION
NORTHERN STAR RESOURCES
ORIGIN ENERGY
TELSTRA

Asset Class Exposures

Exposure (% of NAV)	Net
Equity	95.34
Long Option	0.00
Short Option	-8.04
Effective Cash	12.71
Grand Total	100.00

* 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.

ABOUT THE ELLERSTON OVERLAY ASF

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	\$195.4 Million
FUNDS UNDER MANAGEMENT – OASF UNIT TRUST	\$8.4 Million
APPLICATION PRICE	\$1.2789
REDEMPTION PRICE	\$1.2725
NUMBER OF STOCKS	22
INCEPTION DATE	1 July 2011

Source: Ellerston Capital.

Contact Us

Sydney

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Find out more

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

All holding enquiries should be directed to our register, Link Market Services on **1800 992 149** or ellerston@linkmarketservices.com.au.

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